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## TREASURY CIRCULAR NO. 27/2016

THE PREMIER

THE MINISTER OF ECONOMIC OPPORTUNITIES  
THE MINISTER OF COMMUNITY SAFETY  
THE MINISTER OF CULTURAL AFFAIRS AND SPORT  
THE MINISTER OF EDUCATION  
THE MINISTER OF FINANCE  
THE MINISTER OF HEALTH  
THE MINISTER OF HUMAN SETTLEMENTS  
THE MINISTER OF LOCAL GOVERNMENT, ENVIRONMENTAL AFFAIRS AND DEVELOPMENT PLANNING  
THE MINISTER OF SOCIAL DEVELOPMENT  
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THE SPEAKER: PROVINCIAL PARLIAMENT  
THE DEPUTY SPEAKER: PROVINCIAL PARLIAMENT

For information

THE ACCOUNTING OFFICER: VOTE 1: PREMIER (ADV B GERBER)  
THE ACCOUNTING OFFICER: VOTE 2: PROVINCIAL PARLIAMENT (DR G LAWRENCE)  
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THE ACCOUNTING OFFICER: VOTE 6: HEALTH (DR B ENGELBRECHT)  
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THE CHIEF FINANCIAL OFFICER: VOTE 8: HUMAN SETTLEMENTS (MR F DE WET)  
THE CHIEF FINANCIAL OFFICER: VOTE 9: ENVIRONMENTAL AFFAIRS AND DEVELOPMENT PLANNING (MR T GILDENHUYS)  
THE CHIEF FINANCIAL OFFICER: VOTE 10: TRANSPORT AND PUBLIC WORKS (MR CR ISMAY)  
THE CHIEF FINANCIAL OFFICER: VOTE 11: AGRICULTURE (MR F HUYSAMER)  
THE CHIEF FINANCIAL OFFICER: VOTE 12: ECONOMIC DEVELOPMENT AND TOURISM (MS M ABRAHAMS)  
THE CHIEF FINANCIAL OFFICER: VOTE 13: CULTURAL AFFAIRS AND SPORT (MS BG RUTGERS)  
THE CHIEF FINANCIAL OFFICER: VOTE 14: LOCAL GOVERNMENT (MS B SEWLALL-SINGH)

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 THE DEPUTY DIRECTOR GENERAL: CORPORATE ASSURANCE, DEPARTMENT OF THE PREMIER (MS H ROBSON)

## **ASSET ACCOUNTING POLICY GUIDE ON THE CLASSIFICATION, RECOGNITION AND MEASUREMENT OF CAPITAL ASSETS**

### **1. PURPOSE**

1.1 The purpose of this circular is to:

- (a) provide departments with an Asset Accounting Policy Guide on the Classification, Recognition and Measurement of assets; and
- (b) To provide guidance to departments on the procedure to be followed when implementing an asset exclusion list.

### **2. BACKGROUND**

- 2.1 The Public Finance Management Act (PFMA), No. 1 of 1999, requires departments to "prepare financial statements for each financial year in accordance with generally recognised accounting practice". The Treasury Regulations further defines "generally recognised accounting practice" for departments as being the reporting framework prescribed by the National Treasury, Office of the Accountant General (OAG).
- 2.2 The OAG has developed and issued the Modified Cash Standard (MCS), which facilitates the transition from cash to accrual accounting for provincial and national departments. The MCS sets out the principles for the recognition, recording, measurement, presentation and disclosure of information required in terms of the prescribed formats.
- 2.3 The Asset Accounting Policy Guide (attached hereto marked Annexure A) was developed in collaboration with departments to provide a framework and guidance to departments on the classification, recognition, measurement and financial disclosure of movable assets based on the MCS/AMD.

### **3. ASSET ACCOUNTING POLICY GUIDE**

- 3.1 The Asset Accounting Policy Guide augments the requirements in the Provincial Treasury Instructions, Chapter 16 A part 14. The Guide further covers the accounting for capital assets in the annual financial statements in accordance with the MCS.
- 3.2 The subsequent measurement of assets is excluded from the Guide as departments prepare financial statements in accordance with the modified cash basis of accounting. Capital assets are not depreciated, or subject to impairment testing or valuation adjustments and continue to be carried at cost in the asset register and financial statements of the Department.

### **4. EXCLUSION LIST**

- 4.1 The Asset Accounting Policy Guide provides for an exclusion list to enable departments to focus on strategic assets for reporting purposes in the AFS and to exclude non-strategic assets from disclosure in the AFS. However, the assets excluded from reporting in the AFS will still require safeguarding and control on the system, for example LOGIS, SYSPRO, etc.
- 4.2 Authority for the implementation of an asset exclusion list is derived from the Asset Management Framework issued by NT in 2004, Chapter 6 - Asset Life-Cycle Management paragraph 6.2.5.2: Asset threshold - Dealing with minor assets which states "Certain entities set a 'recording' threshold i.e. assets where the historical cost or fair value is under a certain amount, are recorded in the registers of the entity but depreciated in full in the year of acquisition. The recording in the asset register is necessary in order that control can be exercised over the asset. The recording threshold is based on cost-benefit considerations in terms of accountability, probity and management of assets. The common example of items that are recorded is 'portable and attractive' items, which are generally below the 'reporting' threshold."
- 4.3 In terms of the following extract from the MCS, AO's need to be cautioned that the total amount of assets exempted from reporting in the AFS should not become material when compared to the total asset base.

MCS Chapter on Concepts and Principles, paragraph 25 "Material omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements. The size or nature of the information item, or a combination of both, could be factors in determining materiality of the omission or misstatement".

MCS Chapter on Concepts and Principles, paragraph 70 further states "In assessing whether an item meets these criteria and therefore qualifies for inclusion in the financial statements, regard needs to be given to the materiality considerations discussed in paragraphs .23 to .25".

MCS Chapter on Concepts and Principles, paragraph 23 states "The relevance of information is established by reference to the nature and the materiality of the information concerned".

Paragraph 24 further states that "Information is material if its omission, misstatement, or non-disclosure could influence the decisions of users made on the basis of the financial statements. Materiality depends on the nature or size of the item or error judged in the particular circumstances of its omission, misstatement, or non-disclosure in the financial statements. Thus, materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have to be useful".

- 4.4 Departments that decide to implement an asset exclusion list from 1 April 2016 are required to identify assets for exclusion from disclosure in the AFS based on the following:
- a) The Asset Accounting Policy of the department should include an asset exclusion list framework to be applied when selecting assets to be excluded, as well as the management of these assets by the department.
  - b) Compile a list of assets to be excluded that covers the Asset description, ICN number, Value, Control and Safeguarding.
  - c) The asset exclusion list and the content and policy framework must be approved by the Accounting Officer and finalised in consultation with the Provincial Treasury before implementation.
- 4.5 Departments may also apply the following guidelines when compiling an asset exclusion list:
- a) The use of a threshold as a point of reference;
  - b) The total accumulated value of the excluded assets must be assessed annually to ensure that it does not lead to an audit risk; and
  - c) From asset registers, a list of assets needs to be extracted, that will be included as part of the asset exclusion list. These assets must be identified through unique asset identification descriptions.

4.6 The following process must be followed when implementing the exclusion list:

- a) Before any changes are implemented, a full asset count must be performed by the department to ensure completeness (from floor to register) and existence (from register to floor) of the asset register;
- b) All assets not verified during the asset count may not be included in the Exclusion List and must be dealt with in terms of the Loss Control Process;
- c) The Department must include the following details of the assets included in the exclusion list:
  - Item ICN number. This is the standard unified identification code used in LOGIS. The list of ICNs must be submitted to the Provincial Treasury for review;
  - Item description;
  - Unit cost of the asset;
  - Control (processes and internal control mechanisms); and
  - Safeguarding measures.
- d) Assets identified for the exclusion list should be de-recognised from the asset note in the financial statements as "Disposals" with the following narrative explanation:

"Based on the asset accounting policy of the department, disposals include assets to the amount of R..... that have been identified and taken up in the asset exclusion list as they are not strategic in nature. The assets excluded will be managed separately."
- e) The asset disclosure note supporting the de-recognition of assets must also include the following:
  - The total value of assets affected by the de-recognition;
  - The total value and number of assets by class affected by the de-recognition;
  - A statement that a full asset verification of movable assets was performed and that all assets were verified.

A department who decides to control the de-recognised assets outside of LOGIS needs to follow the Disposal process as per Accounting Officer's System. Disposed/de-recognised assets needs to be manually controlled on the Departments own manual system.

A department who decides to control the de-re cognised asset through LOGIS do not need to capture any transactions on LOGIS.

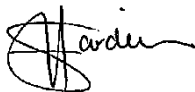
## **5. EFFECTIVE DATE**

The attached Asset Accounting Policy Guide must be adopted by the department with effect from 1 April 2016.

## **6. REQUIREMENT**

6.1 Accounting Officers are required to:

- (a) Adopt the attached Asset Accounting Policy Guide within his/her department (Annexure A).
- (b) Agree, in consultation with Provincial Treasury on the exclusion list and any amendments thereon.
- (c) Note the Asset Accounting Policy Guide Roll-out Plan (Annexure B).



**MR A HARDIEN**  
**PROVINCIAL ACCOUNTANT-GENERAL**  
**DATE:** 05-07-2016

# **ANNEXURE A**



## **Western Cape Provincial Asset Accounting Policy Guide on the Classification, Recognition and Measurement of Assets**

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## PART 1: ABBREVIATIONS, DEFINITIONS AND DESCRIPTIONS

In the Asset Accounting Policy Guide (AAPG) unless the context otherwise indicates, a word or expression to which a meaning has been assigned in the Act or Treasury Regulation has the same meaning as in the Act, and –

- 1) **“Act”** means the Public Finance Management Act, Act No.1 of 1999;
- 2) **“Department”** means the Western Cape Provincial Departments; and
- 3) **“Treasury Regulation (NTR)”** means the Treasury Regulations.

For the purpose of this Guide, the following abbreviations, definitions and descriptions have been used throughout the chapters and have the meanings as described below:

- 4) **Accounting Manual for Departments (AMD)** - an accounting manual that provide additional guidance on the Modified Cash Standard.
- 5) **Accounting Officer (AO)** - The Head of Department in accordance with section 36 of the Act.
- 6) **Accounting Standards** - Accounting standards as defined by the South African Standards Board.
- 7) **Accounting Standards Board (ASB)** - The board established in terms of section 87 of the Act.
- 8) **Accrual Accounting** - A basis of accounting in terms of which transactions and other events are recognised when they occur, and are recorded in the accounting records and reported in the financial statements of the periods to which they relate.
- 9) **Acquisition** - Acquiring assets needed to achieve program delivery objectives. Acquisition may include direct purchasing of assets as well as the receipt of assets constructed on own account, donations or from transfers from other government institutions.
- 10) **Acquisition date** - The date when control of the asset passes to the institution.
- 11) **Administered assets** - Assets administered but are not part of any core function or service for example Heritage assets of a department other than an institution specifically mandated to preserve heritage assets for current and future generations.

- 12) **Accounting Officers' System AOS** - The comprehensive operational framework for procurement and provisioning encompassing the policies, procedures and regulatory framework of the department.
- 13) **Annual Financial Statements (AFS)** - The financial reports representing –
- a) Statement of financial performance;
  - b) Statement of financial position;
  - c) Cash-flow statement;
  - d) Accounting policies
  - e) Any other statements that may be prescribed; and
  - f) Any notes to these statements.
- 14) **Annual Performance Plan (APP)** - This plan provides the direct linkage between long-term strategic goals outlined in the departmental strategic plans and what managers are expected to accomplish in financial year.
- 15) **Asset** - for the purpose of the AAPG means items classified as movable non-current assets of the department defined as follows:
- a) An asset is defined as a resource that:
    - i) Has service potential or future economic benefits meaning that that will flow to the entity;
    - ii) The entity controls the service potential or economic benefit associated with the asset;
    - iii) Originated as a result of a past transaction meaning it was either bought, received as a gift, transferred to the institution or officially procured in any other way that would be reflected in the institution's records; and
    - iv) The cost or fair value of the item can be measured reliably.
- 16) **Asset Accounting Policy Guide (AAPG)** - the AAPG is limited to the classification, recognition and measurement of the movable assets within Provincial Departments of the Western Cape Provincial Government.
- 17) **Asset category** - An accounting segment defined in the Standard Chart of Account (SCOA).

- 18) **Asset exclusion list** - A list of non-strategic assets of which the accumulative value over time does not exceed the audit materiality threshold value of the department and will not be reported in the AFS.
- 19) **Asset Lifecycle** - the lifespan of an asset, from the establishment of the need, through to its acquisition, operation and any maintenance or upgrading, to its disposal.
- 20) **Asset management official** - Official appointed within the section responsible for controlling assets and appointed in writing by the accounting authority in terms of his/her powers in accordance with section 38 of the Act.
- 21) **Asset Management (AM)** - The process of guiding the acquisition, use, safeguarding and disposal of an asset to make the most of its service delivery potential, and to manage the related risks and costs over its entire lifecycle.
- 22) **Asset Management Unit (AMU)** - The section responsible for ensuring that the department's asset management policies and standard operating procedures operate as intended.
- 23) **Asset registers** - The register/schedule of assets of the department, and maintained in accordance with the National Treasury's minimum requirements of an asset register.
- 24) **Asset strategy** - The manner in which the department proposes to manage its assets across all phases of their lifecycle, in order to meet service delivery needs, most cost-effectively.
- 25) **Asset unique number** - Unique asset identification/tag number that distinguishes one asset from another. This does not necessarily need to be a barcode number.
- 26) **Basic Accounting System (BAS)** - The National Treasury approved accounting system for Government.
- 27) **Book value** - In accordance with the Modified-Cash Basis of accounting the book value will be the same as the original/initial measurement cost.
- 28) **Capital asset** - Capital assets are non-current tangible or intangible assets of a department that are expected to be used or held by that department for longer than one year.
- 29) **Capitalised and maintenance costs** - Should a department incur costs relating to a capital asset already recorded (i.e. an existing capital asset), the subsequent costs will be treated according to the nature thereof.

In accounting, a capital expenditure is added to an asset account ("capitalised"), thus increasing the asset's value. Maintenance expenditure on the other hand must be expensed when incurred. Maintenance expenditure will allow the asset to realise its expected service levels and estimated useful life and does not:

- 30) **Chief user** - The duly appointed official held accountable for the assets under his/her control. The Chief user takes ultimate responsibility for the useful life, physical control and safeguarding of the asset.
- 31) **Chief user clerk** - The duly appointed official who is operationally responsible for the asset stock count in their respective unit also referred to as the **Asset Controller**.
- 32) **Class of assets** - a class of assets means a grouping of asset of a similar nature or function in a department's operations that is shown as a single item for the purpose of disclosure in the financial statements.
- 33) **Componentisation** - Components are parts of a capital asset. Such assets form part of the main capital asset, but have a useful life that is different to that of the main asset and is therefore managed separately. These items are often replaced over the lifetime of the main asset and form a significant part of the main asset in terms of their importance to its main use and value.
- 34) **Condition** - Assessed physical condition of the asset.
- 35) **Condition Assessment** - An assessment of the current condition of an asset and its components, in relations to its service performance, as well as the maintenance or renovations required. A condition assessment can be performed in the following way:
  - a) **Face value assessment** - this assessment is performed by an ordinary user or responsible official and is based on a visual inspection of the assets condition. This kind of assessment is suited to office furniture and equipment where a visual inspection will provide adequate indication of the condition of the asset.
  - b) **Technical assessment** - this assessment is typically performed by a skilled professional who will perform an in-depth and technical assessment of the performance standard of the asset, where the asset is of the highly technical nature. The annual technical assessment of assets needs to be conducted as indicated in the departmental asset management policy. Examples of assets that may require technical assessment include but are not limited to computer hardware, vehicles and medical equipment.

- 36) **Control of an asset** - Control exists where a department has the power to obtain or direct the future economic benefits or service potential from the underlying resource and to restrict the access of others to those benefits throughout the major portion of the lifecycle of the asset. Control of an asset is evidenced by the ability of the department to -
- a) Benefit from the asset in pursuing its objectives;
  - b) Deny or regulate the access of others to the that asset and its benefits;
  - c) Secure the service potential or the future economic benefit of the asset;
  - d) Make demand assessments; and
  - e) Carry the risk associated with the ownership and control of the asset.
- 37) **Cost of an asset** - The Modified Cash Standard further defines that the cost of the asset is its purchase price, including import duties and non-refundable purchase taxes, and any costs directly attributable to bringing the asset into location and condition for use, less any trade discounts and rebates.
- 38) **Current Asset** - An asset that would, in the normal course of operations, be consumed or converted to cash within 12 months of the last reporting date.
- 39) **Damaged items** - Items that are damaged/spoilt/flawed or inadequately impaired and no longer operational.
- 40) **Demand Management** - A management technique used to identify and control demand for services.
- 41) **Direct Costs** - Costs that can be specifically assigned and directly attributed to an asset.
- 42) **Disclosure** is the depiction of a recognised and or recorded item of information in the notes to financial statements in accordance with the requirements of the applicable accounting standard, whereas presentation refers to the layout and positioning of the item within the primary or secondary financial information.
- 43) **Disposal** - The process by which the department relinquishes control of an asset.
- 44) **Disposal Committee** - A committee appointed by the Accounting Officer to review and make recommendations regarding the disposal of assets under the control of the department, such assets being regarded as damaged, unserviceable, redundant or obsolete.
- 45) **Fair value** - Defined as a rational and unbiased estimate of the potential market price of an asset or the amount for which an asset could be

exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

- 46) **Finance leased assets** - A lease that transfers substantially all risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.
- 47) **Financial year** - means a year ending 31 March.
- 48) **Fruitless and wasteful expenditure** - means the expenditure that was made in vain and would have been avoided had reasonable care been exercised.
- 49) **Financial System (FS)** - The collection of accounting processes and procedures that allow an entity keep accurate financial records, monitor accounts, prevent fraud and mistakes, and catch any discrepancies. A financial system allows the department to maintain accountability for expenditures and revenues, and to control their finances to minimise waste and loss.
- 50) **Future economic benefits or service potential** – embodied in an asset is the potential to contribute directly, or indirectly, to the flow of cash and cash equivalents to the department or to the rendering of services by the department.
- 51) **Heritage assets** - Heritage assets are capital assets that have a cultural, environmental, historical, natural, scientific, technological or artistic significance and are held indefinitely for the benefit of present and future generations.
- 52) **Immovable asset** - An immovable asset is a capital asset consisting of land, infrastructure, buildings or a combination of thereof.
- 53) **Impairment** - An asset is impaired when its carrying value amount exceeds its recoverable amount.
- 54) **Initial measurement** - Is the measurement of costs that takes place when the asset is purchased (The date the asset is first brought into the movable AR). The Initial cost (purchasing price) of the asset taking into consideration all the costs involved in bringing the asset into operation, location for it to function as intended.
- 55) **Intangible items** - An identifiable, non-monetary asset without physical substance. It is an asset that cannot be seen, touched or physically handled. (For example computer software, patents, copyrights etc.).
- 56) **Information Technology IT** - Computer hardware and software used by a department.

- 57) **Investment property** - Investment property is a property (land or a building or part of a building or both) held with the primary purpose of earning rentals or for capital appreciation or both, rather than for:
- a) use in the production or supply of goods or services or for administrative purposes; or
  - b) sale in the ordinary course of operations.
- 58) **Irregular expenditure** - means expenditure, other than Unauthorised expenditure incurred in contravention of, or that is not in accordance with, a requirement of this Act or any other applicable legislation.
- 59) **Item record number (ICN)** - The uniform LOGIS item code and description that describes the asset.
- 60) **Lease** - An agreement that conveys the right to use an asset, usually for a specified duration, and for an agreed payment or series of payments.
- 61) **Lifecycle cost (LCC)** - Sum of all recurring and one-time (non-recurring) costs over the full life span of the asset.
- 62) **Location** - The physical location where the asset is located.
- 63) **LOGIS** - The Treasury approved supply chain management system also containing the Department's Asset Register.
- 64) **Maintenance** - The work needed to maintain an asset in a condition that enables it to reach its service potential over its useful life, provided that maintenance does not extend an asset's useful life, and related expenditure is treated as current expenditure.
- 65) **Major/minor asset classification** - Capital assets are split into major capital assets and minor capital assets for administrative convenience.
- a) Currently, minor capital assets include those items costing less than R5 000. To align this practice to the budget process they are budgeted for as "current" expenditure.
  - b) Major capital assets include those items costing more than R5 000.
  - c) Costs incurred for research purposes are also classified as "current expenses" without considering the threshold.

- 66) **Material omissions** - material omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements. Materiality depends on the nature or size of the omission or misstatement judged in the surrounding circumstances. The size or nature of the information, or a combination of both, could be the determining factor.
- 67) **Modified cash Standard (MCS)** - Generally Recognised Accounting Practice applied by National and Provincial Departments.
- 68) **Movable Asset Register (MAR)** - The record of information of all movable assets that supports the effective financial and technical management of assets and that meets statutory requirements. The asset register should facilitate proper financial reporting.
- 69) **Movable assets** - refer to those assets that can be moved or relocated for example, machinery, office equipment, computer hardware, vehicles or furniture.
- 70) **Movement** - The relocation of an asset, whether temporarily or permanently from its existing location to another location.
- 71) **Medium Term Expenditure Framework MTEF** - The MTEF is annual, rolling three year-expenditure planning. It sets out the medium-term expenditure priorities and hard budget constraints against which sector plans can be developed and refined. MTEF also contains outcome criteria for the purpose of performance monitoring.
- 72) **Non-current assets** - Non-Current assets have an extended useful life greater than one year and it is usually expected that these assets would be used during more than one reporting period.
- 73) **Non-operational asset** - Assets that are not in operation anymore due to obsolescence, de-commissioned or awaiting disposal.
- 74) **OAG** - Office of the Accountant General.
- 75) **Obsolete items** - An asset becomes obsolete when it is no longer appropriate for the purpose it was obtained due either to the availability of better alternatives or changes in user requirements. These assets are eligible for replacement.
- 76) **Operating Lease** - A lease, other than a finance lease, where the risks and benefits incidental to ownership are not substantially transferred to the lessee.



- 77) **Physical substance** - Physical matter of which a person or thing consists of.
- 78) **PT** - Provincial Treasury.
- 79) **PTI** - Provincial Treasury Instruction.
- 80) **Practitioner** - An asset management practitioner, employed by the department and appointed within the section responsible for controlling assets and appointed in writing by the accounting officer in terms of his/her powers in accordance with section 38 of the PFMA, Act No 1 of 1999.
- 81) **Procurement** - Process of acquiring goods or services.
- 82) **Redundant items** - Redundant assets are no longer essential to the ongoing operations of the institution but may still generate income or be of economic benefit if sold. Redundant assets are also referred to as non-operating assets.
- 83) **Refurbishment** - Modification works carried out on an asset to restore it to an acceptable condition. These costs are considered maintenance expenditure.
- 84) **Recognition** - Recognition is the process of incorporating in the statement of financial position or statement of financial performance an item that meets the definition of an element and satisfies the criteria for recognition. It involves the depiction of the item in words, and in monetary amounts, and the inclusion of those amounts in the statement of financial position or statement of financial performance totals. The elements for recognition include:
- a) The asset arises from a past event;
  - b) The department controls the economic benefit or service potential of the asset; and
  - c) Value can be reliably measured.
- 85) **Recording** - The process of capturing the financial information relating to a particular transaction, event, asset or liability in the electronic or manual accounting records of the department for the purposes of disclosure as secondary financial information.
- 86) **Reporting date** - The date of the last day of the reporting period to which the financial statements relate.
- 87) **Responsible official** - Is the individual responsible for executing the task assigned by the accounting officer to perform duties as contemplated in terms of section 44 of the PFMA.

- 88) **Standard Chart of Accounts (SCOA)** - The chart of accounts of the department, which identifies the structure of the ledger and represents the framework upon which the ledger and associated management reports are based. It comprises the coding of items used for classification, recording, reporting and budgeting purposes which is divided into the following;
- a) Assets;
  - b) Liabilities;
  - c) Net assets/net equity;
  - d) Revenue; and
  - e) Expenditure.
- 89) **Service potential** - Service Potential relates to the entity's ability to use/utilise their resources in a way that will allow the entity to provide better service to their customers.
- 90) **Standard Operating Procedure (SOP)** - Means a method of functioning that has been established over a period of time in order to execute a specific task or react to a specific set of circumstances or situation or process. SOPs document the normal or accepted methodology and help form the basis for compliance evaluation.
- 91) **Strategic Plan** - A document or statement setting out the strategies that the department intends to follow in the medium term in order to achieve the institution's objectives.
- 92) **Systems** - The manual and or computerised systems in use within the Department.
- 93) **Tangible asset** - An asset that has physical substance. These are assets that one can touch and feel.
- 94) **Valuation** - The process of assigning and recording a monetary value to an asset, which initially means the cost of acquisition.
- 95) **WCG** - Western Cape Government.

## **PART 2: INTRODUCTION**

2.1 The Asset Accounting Policy Guide (AAPG) provides guidance on the accounting for capital assets in the annual financial statements in accordance with Modified Cash Standard (MCS).

### **2.2 Specific Exclusions**

The AAPG does not cover the accounting treatment of the following class of assets, however it is covered to clarify the distinctions between these assets below and movable assets:

- a) Immovable Assets;
- b) Inventory;
- c) Public Private Partnerships; and
- d) Leases (excluding finance leased assets).

NB: A department must however apply the provisions of the AAPG on expiry of the lease if the department takes control over the leased asset.

2.3 The Public Finance Management Act (PFMA), No 1 of 1999, requires departments to “prepare financial statements for each financial year in accordance with generally recognised accounting practice”. The Treasury Regulations further defines “generally recognised accounting practice” for departments as being the reporting framework prescribed by the National Treasury, Office of the Accountant General (OAG).

2.4 The OAG has developed and issued the MCS, which facilitates the transition from cash to accrual for provincial and national departments and sets out the principles for the recognition, recording, measurement, presentation and disclosure of information required in terms of the prescribed formats.

2.5 Provincial departments prepare financial statements in accordance with the modified cash basis of accounting. Capital assets are not depreciated, subject to impairment testing or valuation adjustments and continue to be carried at cost in the asset register and financial statements of the department.

2.6 Departments must adhere fully with the principles, presentation and disclosure requirements contained in the MCS in order to achieve fair presentation, and compliance with the PFMA and its regulations.

2.7 The AAPG should be read in conjunction with the MCS and the Accounting Manual for Departments (AMD).

- 2.8 Accounting Policies are the specific policies and procedures used by a department to prepare its financial statements. These include any methods, measurement systems and procedures for presenting asset disclosure information. While the MCS represents the principles, the policies represent the manner in which the department intends to adhere to these accounting principles.
- 2.9 Over time, inadequate institutionalised compliance to Supply Chain Management (SCM) legislation, policies and procedures has resulted in disparate expenditure trends. Accounting policies on the other hand have an impact on almost every aspect of the assets lifecycle, for example; acquisition results in the measurement of initial cost and the subsequent measurement of assets resulting from an assessment of the assets condition, depreciation and determination of the remaining useful life.
- 2.10 Accordingly, the AAPG aims to provide a framework and guidance to officials responsible for the classification, recognition, measurement and financial disclosure of movable assets.
- 2.11 Asset Classification, Recognition and Measurement addresses the following key Asset Management (AM) objective by ensuring that assets are recognised in the departmental Movable Asset Register (MAR) in accordance with the prescripts of the MCS, through:
- a) The correct classification and recognition of the item as an asset where after applying the correct asset classification to the asset;
  - b) The determination of the initial measurement (cost) of the asset; and
  - c) The accurate financial disclosure of movable assets.
- 2.12 The AAPG should be read in conjunction with the AMD for further clarification, guidance and practical examples.
- 2.13 The AAPG is based on the current MCS and therefore does not discuss in any detail future developments in the field of accrual accounting.

### **PART 3:       REGULATORY FRAMEWORK**

The PFMA requires departments to prepare financial statements for each financial year in accordance with generally recognised accounting practice". The Treasury Regulations further defines "Generally Recognised Accounting Practice" for departments as being the reporting framework prescribed by the National Treasury, OAG.

3.1     In developing the MCS, the OAG also considers:

- a)    Best practices, both locally and internationally;
- b)    The capacity of departments to comply with the reporting requirements; and
- c)    The systems used by departments in preparing and collating the information required to comply with the reporting requirements.

3.2     The following references the relevant legislative framework and prescripts that governs movable asset management in provincial departments and must therefore be considered:

- a)    In section 195(1)(b) – The Constitution states the basic values and principles governing public administration as: efficient, economic and effective use of resources must be promoted;
- b)    The Constitution section 216 provides for National legislation to establish a National Treasury to prescribe measures to ensure transparency and expenditure control in each sphere of government by introducing general recognised accounting practice, uniform expenditure classification and uniform treasury norms and standards. It furthermore instructs National Treasury to enforce compliance with the measures so established;
- c)    To give effect to the various provisions of the Constitution and in pursuance of introducing uniform norms and standards, the PFMA, 1999 took effect. The PFMA (section 36) appoints Accounting Officers in departments and Constitutional Institutions whilst section 38 includes a legal requirement for the management, including safeguarding and maintenance of assets in government and section 42 prescribes the responsibilities of accounting officers when assets and liabilities are transferred;

- d) The responsibility for financial management, asset management, internal control and safeguarding of assets in his/her area of responsibility is awarded to all government officials in terms of section 45 of the PFMA;
  - e) In terms of section 76(4)(c) of the PFMA, the National Treasury may make regulations or issue instructions applicable to all institutions to which the act applies concerning the determination of a framework for an appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective;
  - f) In particular the following Treasury Regulations are to be considered in the implementation of this Guide:
    - i) Chapter 10: Asset and Liability Management
    - ii) Chapter 12: Management of Losses and Claims
    - iii) Chapter 16(a)(7): Disposal and Letting of Assets
    - iv) Chapter 21: Gifts, Donations and Sponsorships;
  - g) In terms of section 18(1)(c) of the PFMA the Provincial Treasury must promote and enforce transparency and effective management in respect of revenue, expenditure, assets and liabilities of provincial departments and provincial public entities;
  - h) Provincial Treasury must in terms of section 18(2)(a) of the PFMA issue Provincial Treasury Instructions not inconsistent with the Act;
  - i) In particular the following Provincial Treasury Instructions are to be considered in the implementation of the AAPG:
    - i) Chapter 16(a) Part 9 Movable Asset Management;
    - ii) Chapter 16(a) Part 10 Disposal Management;
    - iii) Chapter 16(a) Part 13 Risk Management and Internal Control; and
    - iv) Chapter 16(a) Part 14 Financial Treatment and Disclosure of Assets and Inventories.
- 3.4 The prescripts addressed above are not exhaustive and may be augmented by other directives. In the event of uncertainty the Provincial Treasury Accounting Unit must be approached for further clarification.
- 3.5 The AAPG and any Standard Operating Procedures (SOPs) issued must be consistent with the aforementioned legislative prescripts.

- 3.6 Should there be a conflict between legislation, regulations, institutional instructions and standard operating procedures referred to in this document; the following priority framework will prevail:
- a) Public Finance Management Act (Act 1 of 1999);
  - b) National Treasury Regulations, Instructions and Guidelines;
  - c) Provincial Treasury Instructions;
  - d) Accounting officer's or accounting authorities supply chain management system;
  - e) Institutional Instructions; and
  - f) Standard operating procedures.

## **PART 4: SYSTEMS**

- 4.1 Computerised integrated Financial Management Systems are at the heart of effective SCM and the accounting and reporting on assets. The LOGIS system is currently used as the approved Provisioning System and contains the Movable Asset Registers of Provincial Departments while the Basic Accounting System (BAS) system is used for effecting payments to suppliers. It is acknowledged that a number of other disparate systems exist within the Province and in certain instances excel spreadsheets are used.
- 4.2 Regardless of the state of financial systems in use, the asset register should not operate in isolation of other financial or management systems. It is an integral component of the financial management system and should be closely coupled to the general ledger to facilitate reporting.
- 4.3 It must be noted that information and data requirements specified in the AAPG constitute critical information required (irrespective of the system in use, whether manual or electronic) in order for institutions to make informed decisions about their asset needs and to comply with financial reporting and governance requirements.
- 4.4 The accounting treatment of assets has a direct impact on the asset management processes. Proper accounting and disclosure of capital assets will ensure better financial management, proper control and improved efficiency in the use of a department's assets.
- 4.5 Figure 1 below depicts the integration and impact of asset accounting on the lifecycle of an asset while Figure 2 depicts the current dataflow of information between disparate systems.
- 4.6 Critical Data Requirements of the MAR are further defined in Table 1 below and departments are required to identify their sources of data, whether manual or electronic to meet these requirements.

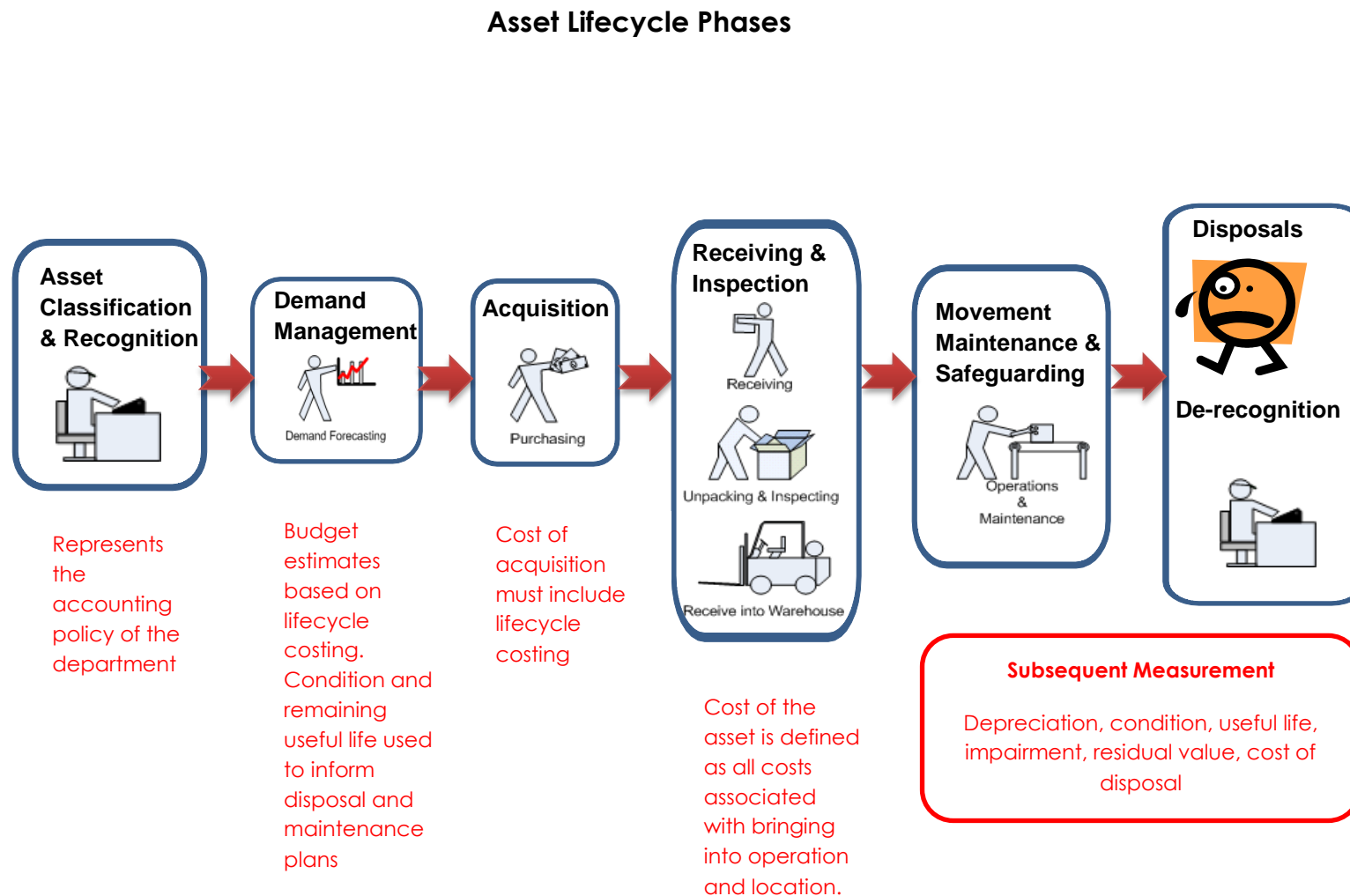


**Table 1 Critical data requirements of the MAR**

Data Requirements	Functional Integration Required	Link to Risk and Internal Control Framework
<p>A MAR containing the following information at a minimum per asset -</p> <p>a) General Master Data Required:</p> <ul style="list-style-type: none"> <li>• SCOA Asset Reporting Level</li> <li>• SCOA Asset Category</li> <li>• Program</li> <li>• Asset Description</li> <li>• Unique Number</li> <li>• Serial Number</li> <li>• Physical Location</li> <li>• Custodian</li> <li>• Cost Centre</li> <li>• Responsible Person</li> <li>• Purchase Price</li> <li>• Make</li> <li>• Manufacturer</li> <li>• Model</li> <li>• Warrantees/Guarantees</li> <li>• Acquisition date</li> <li>• Condition</li> <li>• Purchase Order Number</li> <li>• Asset Status (indicating whether the asset is actively in use or not, does not include disposed assets)</li> </ul> <p>b) Purchasing Data Required</p>	<p>a) Asset Maintenance System. Integration with the Asset Maintenance Planning System is required to obtain information relating to the current performance standards and planned and scheduled maintenance requirements of assets. This will enable users to determine:</p> <ul style="list-style-type: none"> <li>• Whether the asset will be available and be able to perform in accordance with the required performance standard rating.</li> <li>• The historical cost of maintenance and repairs;</li> <li>• Whether assets need to be disposed of;</li> <li>• What assets need to be procured;</li> <li>• Institutional arrangements required to safeguard and control assets.</li> </ul> <p>b) Payment Systems. Integration with payments systems will assist users with determining baseline estimates when developing the funding plan.</p> <p>c) Procurement and Provisioning. Integration with procurement and provisioning systems will assist users when defining asset specifications and enable supplier performance analysis.</p> <p>d) Asset reconciliations of assets purchased on Logis and assets paid on BAS must be compiled on monthly basis and all non-reconciling items must be cleared on monthly basis.</p>	<p>a) Needs assessment can be done incorrectly and assets are acquired that are not needed.</p> <p>b) Assets are acquired that do not comply with minimum specifications.</p> <p>c) Assets critical to service delivery are not available nor easily replaceable.</p> <p>d) Asset does not meet service delivery needs, over or under performance.</p> <p>e) Asset planning and budgeting is not linked to the institution's strategic plan and budget.</p> <p>f) Service delivery failure due to Non-availability of assets.</p> <p>g) The use of disparate systems/sources could result in inaccurate data conversion and data migration compromising data integrity.</p>

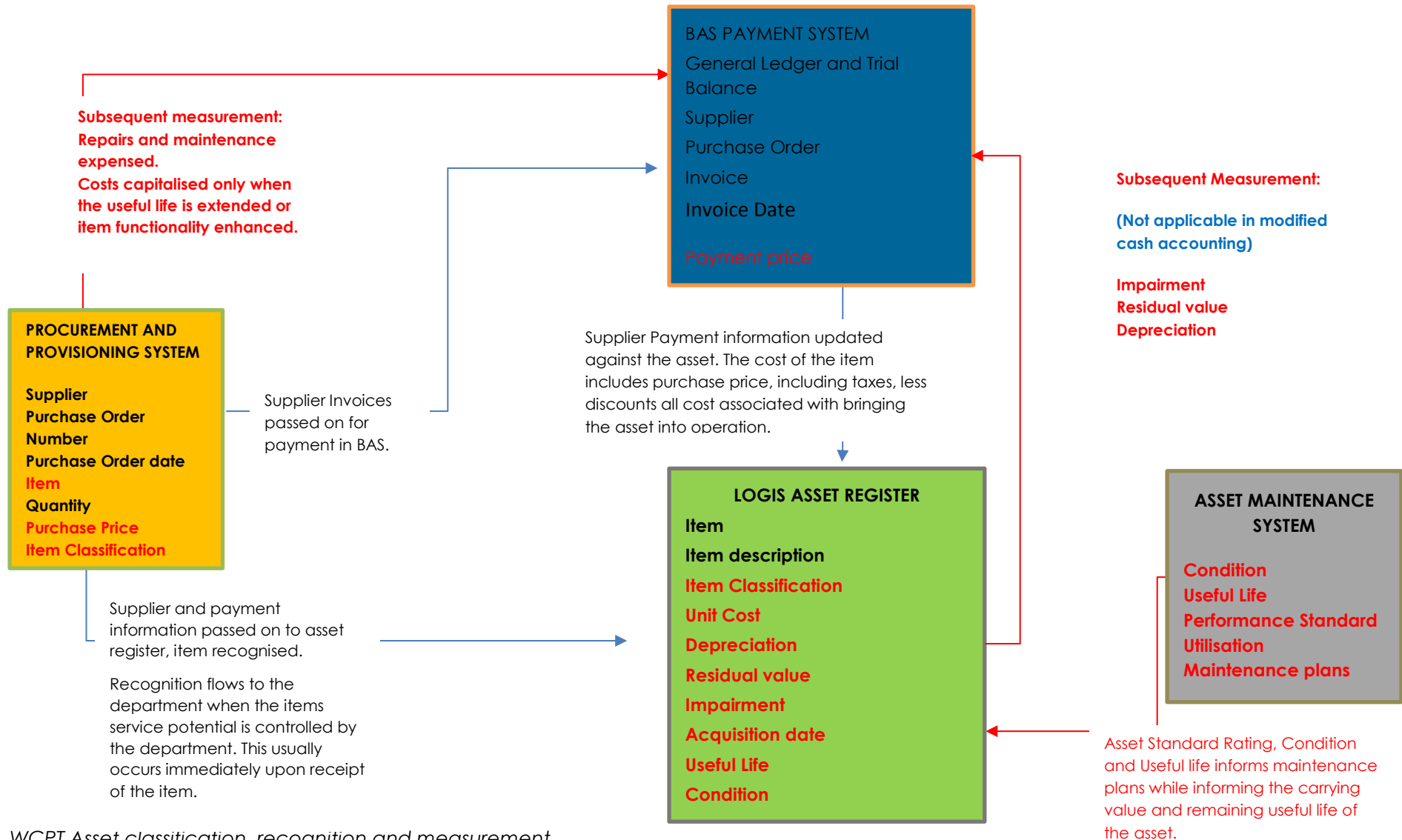
Source: Provincial Asset Management Policy

Figure 1 The asset lifecycle



4.9 A diagrammatic representation of dataflow between disparate systems is depicted below.

**Figure 2 Dataflow between disparate systems**



WCPT Asset classification, recognition and measurement

## **PART 5: CLASSIFICATION OF ASSETS**

### **5.1 The definition of an asset in the MCS is as follow:**

A resource controlled by a department as a result of past events and from which future economic benefits or service potential are expected to flow to the department.

### **5.2 Control of asset**

- a) The definition of the asset includes the term "controlled".
- b) Legal title and physical possession are good indicators of control but the right of ownership is not essential. The key principle is that of control of the economic benefits or service potential of the asset rather than 'physical' control. The capacity of a department to control benefits may be the result of legal rights, but benefits may satisfy the definition of an asset even when there is no legal control for example Heritage assets entrusted to a heritage entity without transfer of the legal title. The entity may not have legal title of the heritage asset but will preserve the asset to the benefit of current and future generations.
- c) Possession or ownership would ordinarily be synonymous with control over the future service potential embodied in the asset. The key question for determining control is however, whether the department not only has the benefit of the service potential but also whether it has control over the service potential of the asset i.e. the authority to decide if and how the asset will be used and is usually evidenced by the department's ability to control all of the following:
  - i) Use the asset to achieve its objectives;
  - ii) Restrict or change access to the asset;
  - iii) Surrender the asset to another entity;
  - iv) To dispose of the asset; and
  - v) Bear the risks associated with holding the asset.

### **5.3 General classification of assets**

Assets are generally classified as either Current or Non-current.

- a) Current assets have an expected short life due to their inherent nature i.e. they are either perishable, will be consumed in the production process or be converted into cash within a short time frame. These

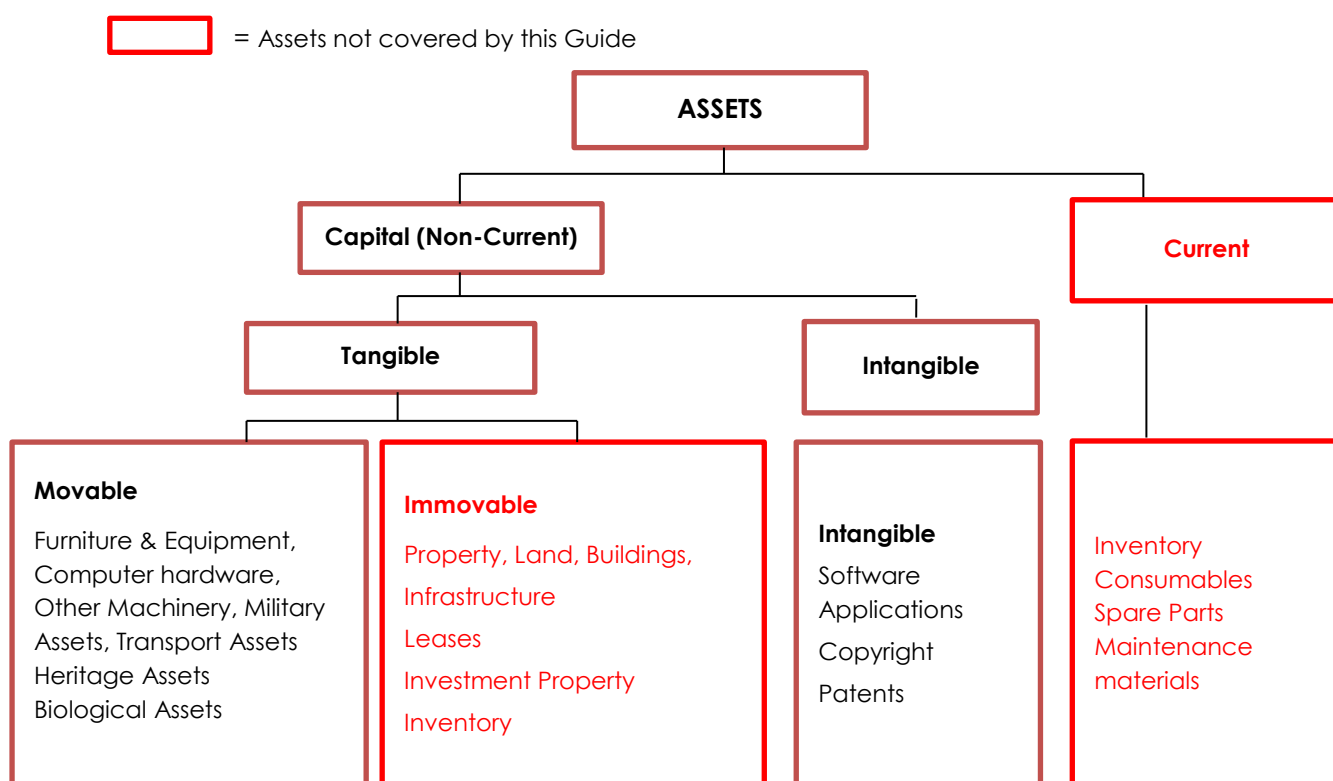
assets are referred to as “current” in accounting terms because they can be consumed or converted into something else within the next financial reporting period.

- b) Non-current/Capital assets have an extended useful life beyond one year and are used repeatedly during more than one financial reporting period.

5.4 The classification of the item as an asset is done in accordance with MCS that establishes the attributes of the item for the purpose of determining how the item is to be treated in the accounting records of the department. Once the item has been assessed as a non-current asset, the correct asset category and SCOA allocation must be determined in line with the MCS.

5.5 Figure 3 below describes the asset tree, a useful tool for understanding the hierarchy of asset classification.

**Figure 3 The Asset Tree**



5.6 In identifying whether an item constitutes a current or capital asset, judgment is required. In further assessing whether an item meets the criteria for recognition and determining the accounting treatment thereof, consideration also needs to be given to the materiality considerations, its underlying substance and economic reality and not merely its legal form.

- 5.7 However, the MCS currently distinguishes capital assets between Major and Minor Assets. Major assets are defined as tangible or intangible capital assets with a threshold equal to or greater than R5 000 while Minor Assets have a threshold less than R5 000 as prescribed by National Treasury.
- 5.8 A number of exceptions are found when identifying and classifying assets. The MCS chapter on Capital Assets include the following:
- a) "Loose tool, spare parts and servicing equipment:
    - i) Spare parts and servicing equipment are usually accounted for as inventory. However, certain spare parts and stand-by equipment qualify as capital assets when a department expects to use them during more than one period. Similarly, if the spare parts and servicing equipment can be used only in connection with a capital asset, they are accounted for as capital assets. For example, loose tools, such as saws, spades, knives, axes, hammers, screwdrivers and spanners or wrenches, are normally not considered as capital assets, even though they are often used repeatedly, or continuously, in production over many years. This is because such tools are small and relatively inexpensive. Expenditure on such tools takes place at a fairly steady rate and, because of their value, is normally treated as a minor capital asset or as a consumable.
    - ii) Some degree of flexibility is however needed, depending on the importance of such tools. For example, a department may have a very extensive maintenance unit where the total value of the tools is high. These tools may be treated as capital assets and their acquisition and disposal recorded as such. An example is where toolboxes are used. The toolbox including all tools can be treated as one unit and as a major capital asset since the value of all the tools could be significant and collectively exceed the capitalisation threshold."

**Example of Loose tools capitalised (AMD)**

- i. Department B purchases a medical toolkit which includes scalpels, forceps and tongs for R10 000.00. The equipment can be treated as one unit. The toolkit is a major capital asset and will be recorded in the major asset register as a unit since the toolkit can be allocated to a specific custodian who can be held responsible for the content therein.
- ii. A forceps included in the toolbox as per scenario above is lost and the Department purchases a new forceps for R300 to replace the lost one. The purchase of individual items within the toolbox is treated as maintenance (Current Expenditure – Goods & Services), the R300 would therefore not be capitalised but expensed.

**b) Movable assets purchased by servicing departments as inventory**

- i) Some departments (Servicing Departments) acquire capital assets for distribution as part of their service delivery mandate. The MCS states that these capital assets should be classified as inventory only if they meet the definition of inventory as outlined in the MCS on Inventory by the servicing department. The following are examples of assets held as inventory for distribution to be taken on as assets by the client department:
  - Office furniture provided by the Department of Transport and Public Works.
  - Safety equipment provided by the Department of Transport and Public Works including evacuation chairs.
  - Telephones provided by the Department of the Premier.
  - Security infrastructure or assets provided by the Department of Community Safety.
- ii) Movable assets purchased on behalf of a client department shall be purchased as Inventory by the servicing department where the servicing department is the budget holder and transferred to the client department in accordance with section 42 of the PFMA.
- iii) Where the client department is the budget holder the asset is purchased by the servicing department as an asset. Upon the transfer of funds to the servicing department, a section 42

certificate shall be issued by the servicing department and the client department will recognise the asset at its cost as indicated in the section 42 certificate.

- iv) The client department and servicing department shall sign and authorise the section 42 Transfer Certificate as evidence that the assets have been transferred in good condition.
  - v) A copy of the Invoice for the asset shall be attached to the section 42 Transfer Certificate in order for the client department to classify and recognise the asset in its asset register at the correct value.
  - vi) The monthly reconciliation of transferred assets shall be accompanied by all duly signed and authorised transfer certificates.
- c) Assets transferred between departments
- i) All assets shall be transferred at cost where cost information is available. Where the asset is recorded at R1 or at its fair value in the asset register of the transferor then the asset should be transferred at that value.
  - ii) All the documentation supporting the value should accompany the transferred assets. If the transferor cannot sufficiently substantiate the cost or fair value of the transferred asset, the transferee may take on the asset at R1 as an interim measure until such time as a reliable fair value has been determined.
- d) Safety Equipment as per the MCS chapter on Capital Assets:
- "Safety equipment (used for more than one year) qualify as capital assets if they enable related assets to generate future economic benefits or service potential in excess (over and above its current economic benefit) of what these benefits would have been if this safety equipment was not acquired."



**Example (AMD chapter on Capital Assets)**

- i) New legislation is enacted that requires x number of fire hydrants per floor of every building. The installation of the hydrants is needed to enable the continued use of the building and its future economic or service potential, in compliance with the new safety standards. The cost of the hydrants and the installation thereof will be recorded as a capital asset, major or minor depending on the cost.
- ii) An old building still in use has asbestos ceilings which were installed when the building was constructed. As a result of medical conditions that are directly attributed to asbestos the building can no longer be used as is. To enable further use the ceilings must be removed or covered up. A decision is made to cover up the existing ceilings with a new false ceiling made from special material that will protect users of the building from the asbestos particles. The cost of the new technology and installation thereof will be recorded as capital assets.

## **PART 6: TANGIBLE AND INTANGIBLE ASSETS**

6.1 The term Capital Asset is generally used to describe both tangible and intangible assets. Tangible assets are Items that have a physical substance, unlike intangible assets, that have no physical substance, such as copyright and trademarks. Paragraph 6.2 and 6.3 below provide definitions for intangible and tangible assets respectively.

### **6.2 Intangible Assets**

6.2.1 Identifiability of an intangible asset in accordance with the MCS Chapter on Capital Assets (paragraph 19):

"An asset meets the identifiability criterion in the definition of an intangible asset when it:

- a) Is separable i.e. is capable of being separated or divided from the department and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the department intends to do so; or
- b) Arises from binding arrangements (including rights from contracts) regardless of whether those rights are transferable or separable from the department or from other rights and obligations."

6.2.2 "Other types of intangible assets include the following as per the AMD Chapter on Capital Assets:

- a) Rights under licensing agreements for films, videos, plays and manuscripts in entities such as broadcasting, tourism, arts and culture;
- b) Patents and copyrights held by government entities in fields such as tourism, research, education, health, agriculture, archives;
- c) Databases and database management software created and maintained by government entities, such as those containing information on the demographic statistics of the population, land ownership, private sector entity ownership and registers of securities and charges;
- d) Airport landing rights;
- e) Import/export licenses; and
- f) Right to control the extraction of mineral resources."

### 6.2.3 Internally generated intangible assets as per the AMD and MCS chapter on Capital Assets:

- a) "It is sometimes difficult to assess whether an internally generated intangible asset qualifies as an intangible asset because of problems in:
- Identifying whether and when there is an identifiable asset that will generate expected future economic benefits or service potential; and
  - Determining the cost of the asset reliably. In some cases, the cost of generating an intangible asset internally cannot be distinguished from the cost of maintaining or enhancing the department's day-to-day operations.
- b) To assess whether an internally generated intangible asset meets the criteria for being recorded, a department classifies the generation of the asset into:
- A research phase; and
  - A development phase.
- c) If a department cannot distinguish the research phase from the development phase of an internal project to create an intangible asset, the department treats the expenditure on that project as if it was incurred in the research phase only.
- d) Research phase
- Research is the original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.
  - No intangible asset arising from research (or from the research phase of an internal project) must be recorded as a capital asset. Research expenditure is included as part of current expenditure in the financial statements.
  - In the research phase of an internal project, a department cannot demonstrate that an intangible asset exists that will generate probable future economic benefits or service potential.

- Types of research activities include:
  - Activities aimed at obtaining new knowledge;
  - The search for, evaluation and final selection of, applications or research findings or other knowledge;
  - The search for alternatives for materials, devices, products, processes, systems or services; and
  - The formulation, design, evaluation and final selection of possible alternatives for new; or
  - Improved materials, devices, products, processes, systems or services.

e) Development phase

- Development is the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of production or use."

6.2.4 "Recognition and initial measurement of costs (as per the AMD chapter on Capital Assets):

- a) Recognising/recording of costs to the cost of the capital asset commences with the development phase.
- b) An intangible asset arising from development (or from the development phase of an internal project) must be recorded if, and only if, the department can demonstrate all of the following criteria:
  - The technical feasibility of completing the intangible asset so that it will be available for use or sale;
  - Its intention to complete the intangible asset and use or sell it;
  - Its ability to use or sell the intangible asset;
  - How the intangible asset will generate probable future economic benefits or service potential.
  - Among other things, the department can demonstrate the existence of a market for the output of the intangible asset or the intangible

asset itself or, if it is to be used internally, the usefulness of the intangible asset;

- The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
  - Its ability to measure reliably the expenditure attributable to the intangible asset during its development.
- c) In the development phase of an internal project, a department can, in some instances, identify an intangible asset and demonstrate that the asset will generate probable future economic benefits or service potential. This is because the development phase of a project is further advanced than the research phase.
- d) Types of development activities include:
- The design, construction and testing of pre-production or pre-use prototypes and models;
  - The design of tools, jigs, moulds and dies involving new technology;
  - The design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production; and
  - The design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.
- e) Availability of resources to complete, use and obtain the benefits from an intangible asset can be demonstrated by, for example, a strategic plan showing the technical, financial and other resources needed and the department's ability to secure those resources.

### Examples of intangible assets

- i. Department X purchases 1 Lenovo Desktop T440 for R12 000.00. This laptop came with Windows Vista as the operating software. Windows Vista is not separable (doesn't meet the identifiability criterion) from the hardware and is the integral part of the laptop without which the laptop wouldn't work and therefore should be treated as part of the hardware (Computer Equipment) and not disclosed separately as an Intangible asset.
  - Computer Equipment (Tangible Asset) = R12 000.00
  - Software (Intangible Asset) = R0.00
- ii. Department Y purchases Windows 7 package to replace the still working Windows Vista initially purchased with the laptop as Windows 7 is more advanced and as a result more desirable for R6 000.00. The newly acquired Windows 7 is not an integral part of the hardware even though it performs the same function as Windows Vista, however this software was purchased separately (Can be sold individually and monetary value attached – Off the shelf package is always likely to be an intangible asset as defined and meet the identifiability criterion). The acquisition meets the definition on intangible assets and is separable and should therefore be treated as the Intangible asset and be disclosed separately.
  - Computer Equipment (Tangible Asset) = R0.00
  - Software (Intangible Asset) = R6 000.00
- iii. Software licence fees. Department X purchases Microsoft Office package for R10 000.00 cash and the department is also to pay R1 000 licence fee on an annual basis for as long as the package is in use. This licence fee will entitle the department to any Microsoft Office update or upgrades. The Microsoft Office package is the intangible as per previous example above and licence fee will be expensed (Current Expenditure) as the amount doesn't relate to the actual acquisition of the package but the maintenance thereof.
  - Software (Intangible Asset) = R10 000.00
  - Computer Equipment (Tangible Asset) = R0.00
  - Software License fee (Current expenditure) = R1 000.00

### **Example of Research and development costs – restoration costs incurred**

Department R&D received information of the existence of voice recordings of private conversations between Jan Smuts and Winston Churchill during the Second World War that may be of historical significance and subsequently underwent exploration costs to search for the recordings. At the reporting date, 31 March 20x2, nothing was found as yet. The exploration cost for the period amounted to R500 000.

On 1 April 20x2, department R&D discovered the voice recordings and preliminarily verified the authenticity. No further costs were incurred. However, the recordings were badly damaged and had to be restored and digitally remastered, after which an extensive verification process was followed to guarantee the authenticity. The costs of the verification, restoration and re-mastering amounted to R300 000.

- The R500 000 will be treated as research cost under current expenditure.
- The R300 000 will be treated as development cost under capital expenditure heritage assets. "

#### **6.2.5 Website costs (as per the AMD chapter on Capital Assets)**

- a) A website does not have physical substance. As a result, development costs associated with website are intangible assets if they meet the definition of an intangible asset and the development phase criteria.
- b) Some websites are developed to comply with a statute or to be used mainly to provide information on the function, services, objective and performance of a department to the public at large. These websites will not meet the development phase criterion regarding generating probable future economic benefits or service potential and as such the costs incurred for the development of these websites should be expensed.
- c) Determining whether a website can be capitalised as an intangible asset.
  - i) It is important to note that a department will need to demonstrate how the website will generate probable future economic benefits or service potential, in order to capitalise the website as an intangible asset. If the department cannot demonstrate this, all expenditure on such a website should be recognised as a current expense under goods and services when it is incurred.

- ii) It is difficult to demonstrate that probable future economic benefits or service potential will be generated from a website developed solely or primarily to promote and advertise its own products or services; consequently all costs on developing such a website will be classified as a current expense. It is thus treated in the same manner as traditional 'advertising' cost as the impact thereof on the business is difficult to estimate or measure."

### 6.3 **Tangible Assets (as per the AMD chapter on Capital Assets)**

"Tangible assets are non-monetary assets having physical substance that:

- a) Are held for use in the production or supply of goods and services, for rent to others, for administrative purposes or for the development, construction, maintenance or repair of other tangible assets;"
- b) Have useful economic life extending beyond one financial year;
- c) Are not for re-sale in the ordinary course of operations (the purpose of the acquisition of the asset is to use it in the department, not to buy it and then sell it immediately to other departments or entities).



## **PART 7: IMMOVABLE ASSETS**

7.1 The following section is aimed at clarifying instances where departments may have difficulty in distinguishing between movable and immovable assets. This Guide does not deal with the treatment of immovable assets.

7.2 Immovable assets consist of:

- a) Tangible assets, e.g., land, subsoil assets, and water resources; and
- b) Fixed structures, e.g. bridges, houses, office buildings, roads.

7.3 As per the AMD chapter on Capital Assets, there are different types of properties and treatments. For example a department has three properties which are used as follows:

- a) The first property is used as employee accommodation.

The property is held for employee housing to contribute to the department's provision of services and therefore is not investment property. The building should be classified as residential buildings. It is not important whether there is alternative accommodation available for the employees or not.

- b) The second property is used as the offices of the department.

The property is held by the department for administrative purposes and is specifically excluded from the definition of investment property. The building should be classified as non-residential buildings and should be treated in accordance with MCS.

- c) The third property was specifically developed and constructed to earn rental income and is rented out to another entity for a monthly rental income.

The property is held exclusively to earn rentals and this property is specifically included in the definition of investment property and should therefore be classified as investment property and be treated in accordance with MCS.

7.4 Distinguishing between assets being movable or immovable assets (as per the AMD chapter on Capital Assets):

- a) While it may be true that certain movable assets have been affixed to other structures to facilitate the safeguarding and safe operation of the

asset, the asset still remains classified as a movable asset e.g. television mounted onto a wall.

- b) Mobile, portable structures temporarily located in specific areas due to a shortage or lack of capacity within other fixed structures, such as a temporary site office constructed on a building site, intended to be movable rather than permanently located are therefore classified as movable assets and forms part of fixed structures, residential or non-residential depending on the use thereof.
- c) Mobile units designed to provide services that would ordinarily be found within constructed buildings for example libraries, clinics and ambulances, take the form of vehicles that have been equipped/transformed in order to make services readily accessible to the public. These mobile units should be classified as Transport Assets.
- d) Prefabricated structures that are installed or constructed fixed, such as those mounted on a concrete slab on brick plinths and prefabricated units on suspended floors that cannot be relocated due to health and safety risks, are immovable assets. Such structures should be classified as non-residential buildings. These would include mobile classrooms provided by the Department of Education. In as much as these are referred to as mobile, they have become fixed structures and the intention is not to relocate them in the short to medium term.

#### 7.5 Distinguishing between building improvements and immovable assets

- a) Where any capital improvement on property owned by government exceeds 15% of the value of the immovable asset it must be transferred to the Department of Transport and Public Works.
- b) Examples of building improvements included:
  - i) Electric lighting fixtures.
  - ii) Interior partitions.
  - iii) Floor finishing such as carpets.
  - iv) Air-conditioning systems.
  - v) Fitted furniture such as kitchen cupboards.
  - vi) Hydraboils installed in kitchens.
  - vii) Security access control systems such as biometric readers and turnstiles.

- c) Repairs and maintenance is expensed as current expenditure as they are done to retain the status of the capital asset rather than improve it and they do not meet the definition of a capital asset.
- d) Should the department have a project with elements of repairs and maintenance, upgrading and additions to it shall be assessed upfront to determine whether the project is significantly a current or a capital project. The project costs shall be recorded as capital assets in the asset register where the project is predominantly capital in nature.
- e) The department shall not include in the carrying amount of a capital asset the costs of the day-to-day servicing of the item. Rather, these costs are expensed. Costs of day-to-day servicing are primarily the costs of labor and consumables, and may include the cost of small parts. The purpose of these expenditures is often described as for the 'repairs and maintenance' of the capital asset.
- f) A leasehold improvement is an improvement made to a leased building by a department that has the right to use this leasehold improvement over the term of the lease. Leasehold improvements are disclosed and recorded as capital assets if they meet the definition of a capital asset. As a lessee, the department is responsible for recording the improvement that they have paid for. The terms of the binding agreement may specify if the improvements will revert to the lessor at the expiration of the lease or the lessee should remove them without damaging the leased property.
- g) If a department carries out capital works on property that is leased from a private party, the total value of the improvements must be recorded in the asset register of the department when ready for use and the asset register updated. This "asset" is removed/derecognised and transferred out of the asset register when the department vacates the property.
- h) For detailed guidance on departments that have the responsibility to account for the immovable assets belonging to the state, refer to the Treasury Immovable Asset Guide.

## **PART 8: INFRASTRUCTURE ASSETS**

- 8.1 Some assets are commonly described as "infrastructure assets". While there is no universally accepted definition of infrastructure assets, these assets usually display some or all of the following characteristics:
- a) They are part of a system or network;
  - b) They are specialised in nature and do not have alternative uses;
  - c) They are immovable; and
  - d) They may be subject to constraints on disposal.
- 8.2 Examples of infrastructure assets include:
- a) Road networks.
  - b) Sewer systems.
  - c) Water and power supply systems.
  - d) Communication (Telephones and internet) networks.
- 8.3 Infrastructure systems or networks consist of multiple different assets that work together to achieve a specific service. As a result the asset should be unbundled into its components before recording in the asset register.
- 8.4 Departments however do not separate infrastructure assets into components at this point in time and the entire cost of the infrastructure asset is capitalised against the primary asset. When components are replaced or repaired, these costs are expensed.

## **PART 9: OPERATING AND FINANCE LEASES**

- 9.1 In an operating lease, the lessee acquires the right to pay and use the asset for an agreed period of time. At the end of the lease period the lessee does not acquire any title to the asset and cannot decide how the asset should be dealt with as the ownership remains with the lessor.
- 9.2 In a financial lease, the lessee acquires the economic benefit of the use of the leased asset for the major part of its useful life and is obliged to pay for that right. At the end of the term, the lessee has full control over the asset to deal with it in anyway considered appropriate.
- a) Departments are present not required to include capital assets acquired through finance leases in its asset register where the finance lease period has not yet expired. These assets must however be reflected in the finance lease register maintained by the department.
  - b) Where the finance lease agreement has expired and the department continues to use the capital asset, and ownership of the asset has been transferred to the department, the capital asset must be recorded in the department's asset register.
  - c) The following movable assets are classified as finance leases assets within the Province:
    - i) Motor vehicles.
      - These assets are managed and accounted for by Government Motor Transport (GMT) under the auspices of the Department of Transport and Public Works. Departments receive a list of these assets annually from GMT.
    - ii) Cellphones
      - Only in instances when the contract is between the department and the service provider.

## **PART 10: LIBRARY MATERIAL**

- 10.1 Library materials under the control of the department that meet the definition of a capital asset must be accounted for by the department using the principles contained in this chapter, no matter how it was acquired.
- 10.2 This chapter must be read together with the Treasury Accounting Guide for Library Material.
- 10.3 Treasury regulations require a department that controls library materials to have a Library Policy and/or Procedures in place. The existence of any one or a combination of the following criteria would indicate that the department controls library material:
- a) The department sets the policies and procedure for the management of library material;
  - b) The department maintains the books, i.e. the books are restored and brought to a good condition;
  - c) The department has a budget to manage and maintain the library activities;
  - d) The department makes demand assessments;
  - e) The department makes replacement decisions; and
  - f) The department bears the loss for missing or lost books.
- 10.4 Classification of library material
- a) When classifying library material the nature, (such as periodicals versus reference books), and use (i.e. for own use or for distribution to others), should be considered. The department will consider the following to determine the appropriate classification of library material:
    - i) Does the library material meet the definition of an asset?
    - ii) Is the intention to distribute the library material to users?
    - iii) Is the intention to lend library material to the public or employees for a specified period?
    - iv) Is it the intention to use the library material for own consumption in the delivery of services (such as for research purposes)?

- b) In the considering the nature and use, the department will also consider its unique situations. For example, there are instances where periodicals or journals can meet the definition of an asset, particularly in legal environment. In these instances the periodicals or journal will be accounted for as capitals assets.

#### 10.5 Recognition of Library material

- a) Library material that meets the definition of an asset shall be recognised in the financial statements and must be recorded in the departmental asset register.

- b) Community libraries

Some departments have arrangements with other entities e.g. municipalities or non-governmental agencies, for the running of community libraries. Every arrangement has to be assessed on its own merit to determine which entity controls the library material. The entity that controls the library material must account for the library material. Control means that an entity has the rights to regulate the access of others to the benefits of an asset. In assessing control the entity must consider amongst others, legislation or any other binding arrangement.

- c) Departmental library

A department that has an in-house library at a central location for use by employees must account for library material acquired.

- d) Mini-libraries

The acquisition of library material is not limited to an official library. Other units within a department can purchase their own library materials. For example, legal services may purchase work-related books for employees and keep it in the unit.

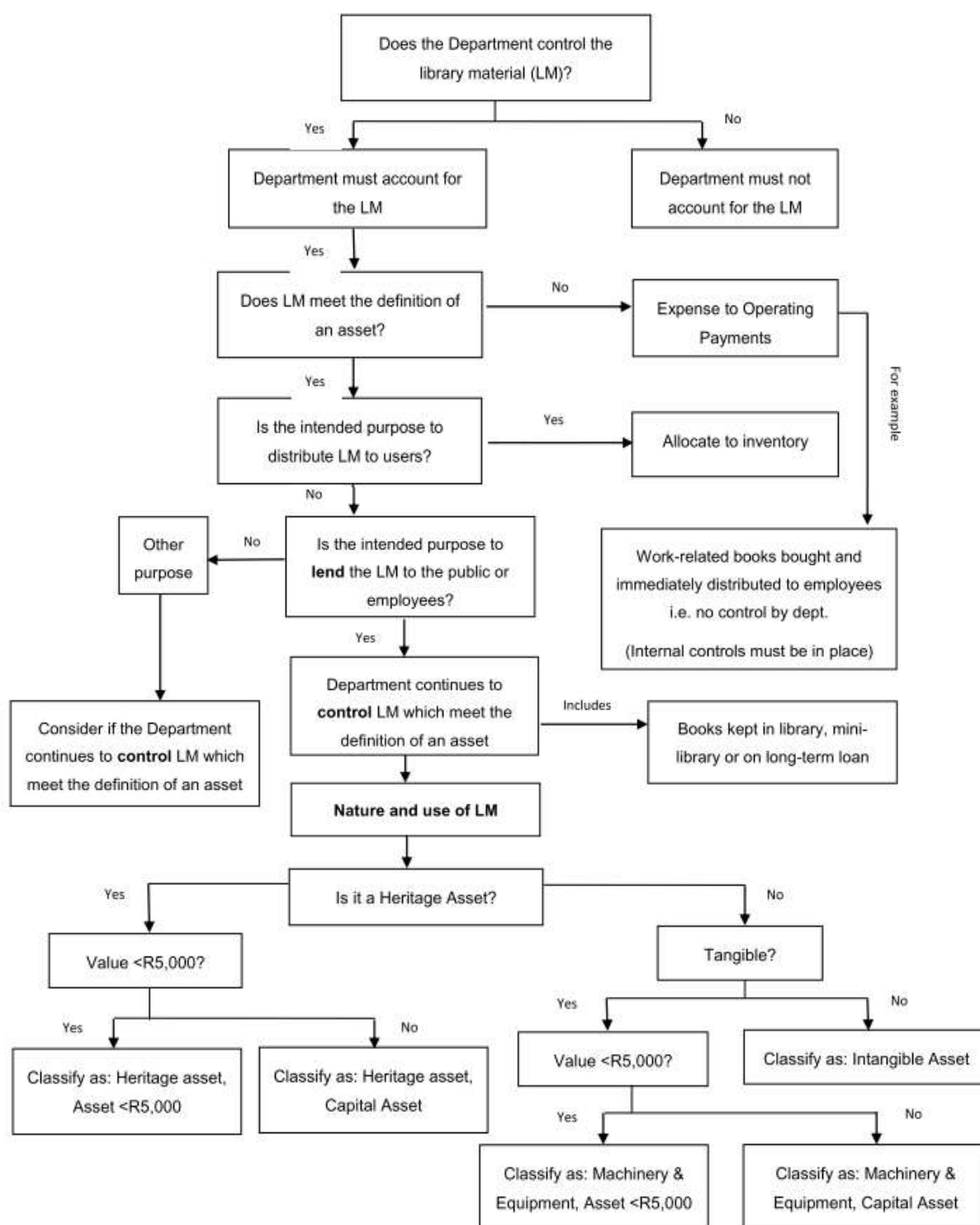
- e) Books and materials that are updated, i.e. the content has become irrelevant/outdated shall not be treated as library materials. Library materials falling in this category would typically be annual publications, magazines, periodicals that will be used for less than one reporting period.

- f) Work related books purchased for direct distribution to users shall be expensed. Departments are required to ensure adequate control measures are in place to safeguard these assets.

- g) Some library materials are purchased to be distributed to external parties; for example textbooks bought for immediate distribution to schools. The department must apply the inventory policy and procedures in accounting for these items.
- h) The following are examples of library materials that should be classified as assets:
  - i) Books, fiction and non-fiction, that can be borrowed by users
  - ii) Reference books, for example encyclopedia
  - iii) Audio Visual material, for example CD's
  - iv) Educational Materials
  - v) Electronic books
- i) The treatment of collections/sets of books
  - i. A library can account for a set of books, such as a set of encyclopedia, as one asset or each books making up the set as an asset. The option selected by the department must be stated in the department's library material policy.
  - ii. The department electing to record library books assets or collections must consider the following disadvantages:
    - The disadvantage of recording the set as one asset is that if one book in the set is lost, the cost of the set will not be a true reflection of the content of the set.
    - Without updating the content (loss of a book) the set will further not reflect the true existence of the books unless each book in the collection is recorded in a component structure.
    - The MCS currently classifies assets into major and minor assets based on a value threshold. While a collection might exceed the value threshold, individual books may not. The MCS further has different disclosure requirements for major and minor assets.



## 10.6 Decision tree for the recognition of library material



## PART 11: HERITAGE ASSETS

- 11.1 This Guide must be read together with the MCS and the National Heritage Resource Act of 1999.
- 11.2 The Modified Cash Standard requires a heritage asset that meets with the criteria for classification as a heritage asset to be recognised if:
- a) It is probable that future economic benefits or service potential associated with the asset will flow to the entity; and
  - b) The cost or fair value of the asset can be measured reliably.
- 11.3 Some characteristics often displayed by heritage assets include:
- a) Their value in cultural, environmental, education and historical terms is unlikely to be fully reflected in monetary terms;
  - b) The value of these assets increase over time even if their physical condition deteriorates;
  - c) They are often irreplaceable;
  - d) They have indefinite useful lives and their value appreciates over time due to their cultural, environmental, historical, natural, scientific, technological or artistic significance;
  - e) Ethical, legal and/or statutory obligations may impose prohibitions or severe stipulations on disposal by sale; and
  - f) They are protected, unencumbered, cared for and preserved.
- 11.4 For a heritage asset to be recognised in accordance with the criteria stated above it needs to be controlled by the entity.
- 11.5 The National Heritage Resource Act, 1999 requires entities to preserve items relating to the 'national estate' no specific guidance currently exists to determine when an item has cultural, environmental, historical, natural, scientific, technological or artistic significance.
- 11.6 The National Heritage Resource Act, 1999 states the following regarding the national estate:
- “(1) For the purposes of this Act, those heritage resources of South Africa which are of cultural significance or other special value for the present community and for future generations must be considered part of the national estate and fall within the sphere of operations of heritage resources authorities.

- (2) Without limiting the generality of subsection (1), the national estate may include —
- (a) Places, buildings, structures and equipment of cultural significance;
  - (b) Places to which oral traditions are attached or which are associated with living heritage;
  - (c) Historical settlements and townscapes;
  - (d) Landscapes and natural features of cultural significance;
  - (e) Geological sites of scientific or cultural importance;
  - (f) Archaeological and paleontological sites;
  - (g) Graves and burial grounds, including —
    - (i) Ancestral graves;
    - (ii) Royal graves and graves of traditional leaders;
    - (iii) Graves of victims of conflict;
    - (iv) Graves of individuals designated by the Minister by notice in the Gazette;
    - (v) Historical graves and cemeteries; and
    - (vi) Other human remains which are not covered in terms of the Human Tissue Act, 1983 (Act No. 65 of 1983);
  - (h) Sites of significance relating to the history of slavery in South Africa;
  - (i) Movable objects, including—
    - (i) Objects recovered from the soil or waters of South Africa, including archaeological and paleontological objects and material, meteorites and rare geological specimens;
    - (ii) Objects to which oral traditions are attached or which are associated with living heritage;
    - (iii) Ethnographic art and objects;
    - (iv) Military objects;
    - (v) Objects of decorative or fine art;
    - (vi) Objects of scientific or technological interest; and

(vii) Books, records, documents, photographic positives and negatives, graphic, film or video material or sound recordings, excluding those that are public records as defined in section 1(xiv) of the National Archives of South Africa Act, 1996 (Act No. 43 of 1996).

(3) Without limiting the generality of subsections (1) and (2), a place or object is to be considered part of the national estate if it has cultural significance or other special value because of —

- (a) Its importance in the community, or pattern of South Africa's history;
- (b) Its possession of uncommon, rare or endangered aspects of South Africa's natural or cultural heritage;
- (c) Its potential to yield information that will contribute to an understanding of South Africa's natural or cultural heritage;
- (d) Its importance in demonstrating the principal characteristics of a particular class of South Africa's natural or cultural places or objects;
- (e) Its importance in exhibiting particular aesthetic characteristics valued by a community or cultural group;
- (f) Its importance in demonstrating a high degree of creative or technical achievement at a particular period;
- (g) Its strong or special association with a particular community or cultural group for social, cultural or spiritual reasons;
- (h) Its strong or special association with the life or work of a person, group or organisation of importance in the history of South Africa; and
- (i) Sites of significance relating to the history of slavery in South Africa."

11.7 The above are general principles and may well guide the practitioner in classifying heritage assets however the assessment of heritage requires critical analysis of the content and nature of an asset to ascertain its significance and remains the domain of heritage practitioners. The NHRA further provides no guidance for recognition and disclosure of heritage assets in the financial statements of an entity. These are defined in the MCS for Provincial and National Departments. It is therefore essential that practitioners and preparers of financial statements are able to interpret and apply both the provisions of

the accounting standard in a manner which gives effect to the principles enshrined in the Act.

- 11.8 Departments are therefore required to define the guidelines/policies to determine when items would be considered as being part of the national estate, in other words when does the item have cultural, environmental, historical, natural, scientific, technological or artistic significance and how they are to be valued.

#### 11.9 Immovable Heritage

Older buildings can be of an age where they may attain heritage status. Prior to any alterations being done the relevant national or provincial agency should be contacted to ascertain whether the structure is considered a heritage asset or not. There may be different conditions attached such as preserving of the façade but the interior could be altered or the entire structure may not be altered. Any conditions should be noted and flagged in the asset register.

#### 11.10 Dual Purpose Assets

There are instances where heritage assets can have a dual purpose, for example where an historical building meets the definition of a heritage asset, but it is also used for offices. These assets that are used for more than one purpose should be classified as a heritage asset when a significant portion of the asset meets the definition of a heritage asset. The department cannot split an asset into more than one classification. For example:

- i. A portion of a property cannot be classified as buildings and another portion classified as heritage assets. The full asset is either a heritage asset or it is not a heritage asset. Determining whether or not the heritage portion is significant or not is a judgement that should be made by management. This judgement should be applied consistently over all the assets. To ensure consistent application of the criteria, it is recommended that management include the judgement criteria as part of their asset management policy.

#### 11.11 Heritage classification

- a) A class of heritage assets is a grouping of assets of a similar nature or function that is shown as a single item for the purpose of disclosure in the financial statements.

- b) The department must define in its policy on heritage assets, the various classes recognised by the department for example; Buildings, Objects and Artefacts, Paleontology etc.
- c) Accounting for heritage as a collections versus individual items
  - i. In assessing the historical significance of an item it is often associated with an individual or an event in history and its value is associated with the collection. Therefore when accounting for these items GRAP 103.42 provides as follows: "In determining the fair value of a collection, the entity should consider whether the entire collection has a higher value than the sum of the values of the individuals making up that collection". If items are removed from the collection, the value of the collection may need to be reassessed.
  - ii. Departments must define the classes of heritage assets and indicate where heritage assets are recognised as collections.

#### 11.12 Library Books Heritage

If library books meet the definition of heritage assets, it should be accounted for in accordance with MCS on Heritage assets. Examples of such items could include:

- i. The books are scarce copies from various sources and limited copies are available.
- ii. No publishers are willing to reproduce these books.
- iii. The books will only be available for research purposes.
- iv. The general public will not be allowed to take them out; they can only be viewed in the library.
- v. The books will be held for an indefinite period, unless destroyed by circumstances beyond human control.

#### 11.13 Recognition and measurement of heritage assets

- a) The most contentious issue is the valuation of items. Heritage assets may be essential to the performance of the principal objectives of entities for example, the fundamental objective of a museum is to restore, conserve and preserve heritage assets for the benefit of present and future generations. Yet, a heritage asset may also be incidental to the fundamental objective of the entity, such as a bequest of an art collection.

- b) When it comes to the valuation of heritage assets it goes against the professional opinion and against ethical values of researchers and curators that heritage should be assigned a cash value; rather its value is spoken of in terms of science or public interest.
- c) Although the MCS recognises that the value of some heritage assets cannot be determined, it is a risk that entities will be qualified by the Auditor General where there is no basis to the decision not to value certain items.
- d) The MCS provides the following methods of valuation with regard to the valuation of heritage assets:
  - i. A heritage asset that qualifies for recognition as an asset shall be measured at its cost.
    - Heritage assets should be valued at cost. Where values could be determined with sufficient supporting documentation to base those values on, those values should be used. The entity can perform an asset count and allocate costs where documentation details and initial cost are available as per the accession register. This option will result in audit queries where proof cannot be provided for initial cost allocated to each asset.
  - ii. Where a heritage asset is acquired through a non-exchange transaction, its cost be measured at its fair value as at the date of acquisition.
    - The assessment of assets under the heading of Fair Value falls within the discipline of Open Market Value (Open Market Value (OMV) of movable assets. The generally accepted method to be adopted in the determination of 'Market Value' is defined as:
 

*"The estimated value the assets herein described will bring if exposed for sale in a market between a willing buyer and willing seller, allowing a reasonable period to find a purchaser who buys with full knowledge, all of the uses to which item is adapted and for which it is capable of being used. In this definition it is assumed that the transaction is based on cash or a cash equivalent consideration. Favourable or unfavourable terms of sale are bound to affect the transaction price, which the subject property can command in a normal trading environment"*.

- The existence of published price quotations in an active market is the best evidence of fair value, such as the quoted price from sellers or recent auctions published in local newspapers; however if the fair value cannot readily be ascertained by reference to quoted prices in an active and liquid market; then plausible value can be applied by an experienced valuation professional.
- The fair value of a heritage asset can be determined from market-based evidence arrived at by appraisal. An appraisal of the value of the asset is normally undertaken by a member of the valuation profession, who holds a recognised and relevant professional qualification. Income generating approach. The fair value will be ascertained by reference to quoted prices in an active and liquid market.
- Future economic benefits or service potential flowing from a heritage asset may include revenue, for example an entrance fee charged by a museum or the hire of the asset for economic or educational purposes. The revenue generated by the entity under such circumstances is normally insignificant compared to the operating costs of the museum and will not result in accounting for the heritage asset as an investment property. The valuation method applied should not necessarily be determined using the income producing approach. The revenue generated is rather used towards the maintenance and preservation of the heritage asset.
- In the case of specialised heritage buildings and other man-made heritage structures, such as monuments, the entity may need to determine fair value by using a replacement cost approach. The reproduction cost or the restoration cost approach may be the best indicator of the heritage asset's replacement cost.
- Where the fair value of an asset cannot be determined, and where no evidence is available to determine the market value in an active market of a heritage asset; a valuation technique may be used to determine its fair value. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, if available, and reference to the current fair value of other heritage assets that have substantially similar characteristics in similar circumstances and locations, adjusted for any specific differences in circumstances. If there is a



valuation technique commonly used by market participants to price such an asset, and that technique has been demonstrated to provide reliable estimates of prices obtained in actual market transactions, the entity may use that technique in determining the fair value.

- Lastly where no value can be placed on an item, it will not be recognised, but information should be disclosed about such items and the reason why such items cannot be valued. There could be many instances where no value can be attached to an item; this option will result in audit queries where proof cannot be provided that the hierarchy of valuation options as stated above was first considered.
- e) Departments that recognise heritage assets must define the valuation basis.

#### 11.14 Exclusions from initial cost measurement of heritage assets

- a) In some instances items of property, plant and equipment may be required to safeguard the heritage assets. For example air conditioning to maintain the room temperature for the preservation of an artefact. Such items are recognised as assets in accordance with the requirements for PPE.
- b) The department does not recognise in the carrying amount of a heritage asset the day-to-day operating costs of the heritage asset. Rather these costs are expensed. For example the day-to-day operating costs to maintain the air conditioning system in a library where heritage books are held.
- c) Costs incurred to enhance or preserve the heritage asset should be capitalised as part of its costs and be included in the carrying amount when incurred.
- d) Upon receipt of an item archivists will assess the content of the item to determine its nature, classify, value and accession the item. Un-accessioned items are not available for use and service potential will only flow to the department upon the completion of the accessioning process. Un-accessioned items are therefore controlled but not accounted for until the accessioning and valuation process is complete.

- e) Where the department engages in exploration or further research prior to the recognition of a heritage asset, the department must apply the provisions of the MCS applicable to Intangible assets and recognise these cost as an expense as the department cannot confirm that at the end of such research or exploration a heritage asset that meets the criteria for recognition will exist. Only when the criteria for development costs are met will the department recognised the cost of a heritage asset.

#### 11.15 Transfers from heritage assets

- a) Transfers from heritage assets shall be made when, and only when the particular asset no longer meets the definition of a heritage asset. For instance, if an item in an art collection is destroyed in a fire and the remaining paintings in the collection no longer meet the definition of a heritage asset, the remaining value of the collections should be transferred from Heritage to capital asset.
- b) Assets may be reclassified as heritage assets after initial recognition and subsequent measurement when an asset subsequently meets the definition of a heritage asset.

Transfers between Heritage assets PPE or any other class of asset does not result in a change in the carrying value of the asset transferred or its cost measurement for the purpose of financial disclosure.

#### 11.16 The treatment of Reference Materials

Reference Materials includes Newspaper clippings, annual reports and research materials. These materials are not considered part of the national estate as envisaged in the National Heritage Resource Act. However their content may add value to the mandate of a heritage institutions and it may therefore elect to preserve some of these materials indefinitely. There is usually no commercial value for these items and for the purpose of valuation these items are collectively considered Reference Materials and are not considered to be assets. No cash value is assigned to reference materials.

### 11.17 Replicas/Prints/copies

- a) Departments may identify item categories within heritage classes that will not be considered for recognition. These decisions are based on the following criteria:
- i. Originality/Authenticity
- Originality or authenticity refers to those aspects of the asset's characteristics that identify the asset as being the first copy/production, not necessarily the only copy/reproduction. For example a print of an original artwork is made. The print is not the original/authentic artwork and its value will negatively affect when it exists alongside and original.
  - Uniqueness  
Uniqueness relates to availability/scarcity of the asset. In other words several original/authentic productions exist. Where an item is irreplaceable the value may be affected depending on its assessed historical or cultural significance.
- b) Replicas serve a purpose of preserving the original Artefact. Replicas are not regarded as heritage assets as they do not form part of the heritage asset collection and therefore not recognised for accounting purposes.
- c) Copies are intended to be used freely and replaced as needed, and therefore will not be recognised for accounting purposes.
- d) While assessing each of the criteria above on its own may assist a department in determining the service potential of the asset, combining the criteria may provide management with more meaningful insight. If uncertainty still exist after the above criteria together with the principles defined in the NHRA and the characteristics of heritage assets have been considered, the main intention or purpose of the asset should be considered, i.e. is the asset used to execute the entity's activities (to fulfil the mandate of the department) or for another purpose. For example, the intention of the accounting standard is not to preserve copies and replicated heritage assets while the intention of the NHRA is to ensure that the national estate is adequately preserved.

## PART 12: BIOLOGICAL ASSETS

12.1 This section is explained by way of the examples below, as per the AMD and MCS:

Biological Asset	Agricultural Produce	Products resulting from processes after harvesting
Sheep	Wool	Carpet
Trees in a plantation	Felled trees	Logs, timber
Plant	Cotton, Cane	Sugar, Thread
Dairy Cattle	Milk	Cheese
Pigs	Carcass	Sausage
Bushes	Leaves	Tea
Vines	Grapes	Wine
Fruit Trees	Picked Fruit	Fruit Juice

### Biological Assets examples

Department B purchases a dairy cattle for R20 000.00 on the 1st of June 2014.

At year end (31/03/2015), the fair value of the dairy cattle is R25 000.00

The cattle will be disclosed at R25 000.00 at year end if the department's policy is to show the dairy cattle at fair value otherwise it must be reported at cost as MCS Capital assets chapter paragraph 84 allows the departments to use either of the two.

The department's choice of either reporting at fair value or cost regarding biological assets must be clearly indicated in the department's asset management policy.

12.2 A department that controls biological asset shall maintain a policy, directive or similar document that clearly states the nature, management, accounting treatment and all other useful information of the department's biological assets.

12.3 Measurement of Biological assets

- a) Upon initial recognition, biological assets are recorded at cost or fair value.

- b) When determining the fair value of biological assets, the following should be considered:
- i. If an active market is not available, a department can consider using one or more of the following:
    - The most recent market transaction price, given that the economic circumstances between the date of that transaction and the reporting date has not changed significantly;
    - The market price for similar assets adjusted to reflect differences; and
    - Sector benchmarks, for example value of cattle expressed per kilogram of meat.
  - ii. Sometimes the sources above may result in different values for an asset. It is then necessary to consider the reasons for the differences in order to determine the most reasonable estimate of fair value.
  - iii. No available market-determined values.
    - Under some circumstances, the market prices or values (i.e. the two methods of determining the fair value as above) are not available for a biological asset in its present condition. In such a situation the department uses the present value of expected net cash flows from the asset. The net expected cash flows are discounted at a current market determined rate.
    - Where biological transformation is negligible or the impact of the biological transformation on the price is not expected to be material, the cost of the assets may approximate fair value.
  - iv. Bear in mind when using the discounted cash flow method of valuation that:
    - It is used to determine the fair value of a biological asset in its present location and condition. This should be taken into account in determining an appropriate discount rate to be used;
    - Fair value is determined for a biological asset in its present condition; therefore it excludes any increase in value from additional biological transformation not yet occurred;

- Cash flow for financing the assets, taxation (if applicable) or re-establishing biological assets after harvest should be excluded as well;
- Fair value reflects any possibility of variations in cash flows of the transaction therefore the expectations about possible variations in cash flows will be included in either the cash flows or the discount rate or a combination of the two; and
- The important thing to remember is that double-counting must be avoided, therefore if a specific assumption or condition is included in the cash flows, the same assumption or condition cannot be included in the discount rate.

**Example: Fair value of biological asset cannot be determined**

Department C owns a sugar plantation on approximately 220 hectares of land.

Currently no active market exists for the plantation. The fair value for the land with the plantation together is R25 million. Empty lands in the neighbouring area are sold at a market price of R72 000 per hectare.

The fair value of the sugar plantation can be determined as follows:

- Fair value of combined asset R25 000 000
- Fair value of land (R72 000 x 220) R15 840 000
- Fair value of plantation R9 160 000.

The fair value of the plantation could change over a period of time as biological transformation takes place, therefore it will be necessary to determine the fair value of both the neighbouring land and combined asset on a regular basis.

#### 12.4 Other measurement considerations

- In the unlikely situation where market-determined prices or values are not available and alternative estimates of fair value cannot be reliably measured, biological assets should be measured at cost. As soon as the fair value can be reliably measured, biological asset should be measured at fair value less estimated point-of-sale costs.
- It is of the utmost importance that the methodology used is documented properly and applied consistently for a class of assets. This will ensure systematic and comparable values period on period.

## **PART 13: INVENTORY AND CONSUMABLES**

13.1 To the extent that inventories and consumable are referred to, it serves to assist departments with distinguishing between inventories and assets.

### **13.2 Definitions**

- a) Inventories are those goods purchased/produced and held or distributed specifically for executing the service delivery mandate of the Department and comprises of the following:
  - i. In the form of materials or supplies to be consumed in the production process,
  - ii. In the form of materials or supplies to be consumed or distributed in the rendering of services,
  - iii. Held for sale or distribution in the ordinary course of operations, or
  - iv. In the process of production for sale or distribution.
- b) Inventories can encompass finished goods produced, or work-in-progress being produced, by the Department. Inventories also include materials and supplies awaiting use in the production process and goods purchased or produced by an Department, which are for distribution to other parties through a non-exchange transaction; for example, educational books produced by an education authority for donation to schools. Examples of inventory are:
  - i. Ammunition and security supplies, (Based on their nature);
  - ii. Maintenance materials;
  - iii. Learning and teaching support materials – Department of Education (DoE);
  - iv. Items bought for distribution, e.g. school furniture, municipal dustbins;
  - v. Library materials prepared for distribution;
  - vi. Medicine, e.g. medicine purchased by a department of health to be distributed/sold to a patient;
  - vii. Spare parts for plant and equipment other than those that qualify as capital assets;
  - viii. Strategic stockpiles;
  - ix. Uniforms and protective clothing bought for the use of department staff, e.g. police uniforms;
  - x. Work-in-progress related to inventories; and
  - xi. Land or property held for sale or distribution.

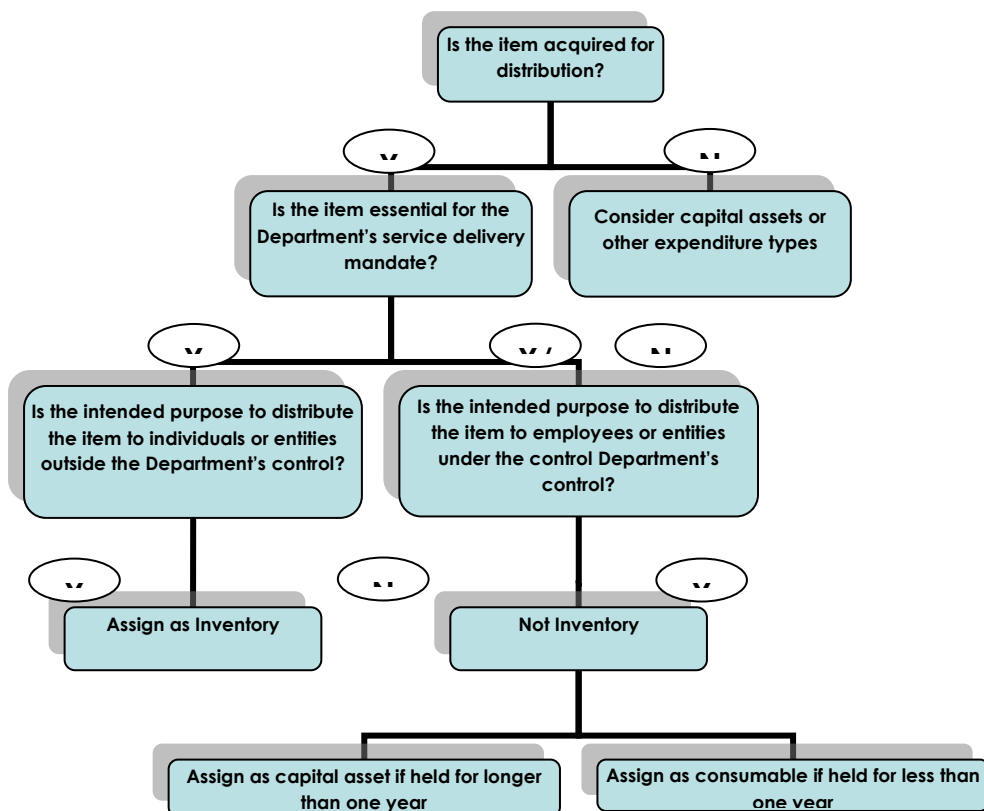
- c) In terms of SCOA Version 4, Inventory has now been broken down into two main categories namely "Inventory" and Consumables". This split in classification will only have an effect on the budgeting and expense side of operations and not on the physical treatment of inventory.
- d) All those goods within a Department that do not meet the criteria of Inventory or Assets will be treated as consumables and accounted for as an expense.

### 13.3 Consumables are items:

- a) that are used and replaced on a regular basis;
- b) capable of being consumed, destroyed, wasted, discarded or spent;
- c) that are in contrast to durable items that can be used repeatedly over a substantial period; and
- d) that are not directly linked to the service delivery needs of a department.

### 13.4 Classification of Inventory and Consumables

- a) The following decision tree will be used to distinguishing between inventory and consumables:





- a) To further assist in this process, a list of assets in terms of the definition and SCOA classification, but which within this department will be treated as consumable items due to their nature, value and risk profile, will be drawn up and submitted for approval on an annual basis to the Head of the Department (HOD). All other items not listed and or not meeting the definition of a consumable item will be treated as assets.
- b) Departments are required to define in its accounting policy whether it manages inventory and to develop accounting policies for the management of inventories.

## **PART 14: RECOGNITION**

- 14.1 Recognition is defined as the process of incorporating in the statement of financial position or statement of financial performance an item that satisfies the criteria for recognition. Under the modified cash basis of accounting, only certain elements are recognised in the Statement of Financial Position and Statement of Financial Performance, while others are recorded for presentation as disclosure notes.
- 14.2 The first step in recognition is to establish whether the items meet the definition of an asset. The attributes of the asset should be determined and thereafter the recognition criteria are applied.
- 14.3 The following are applied when determining whether an item satisfies the recognition criteria:
- a) The department controls the economic benefit or service potential of the asset. This requirement does not limit control to the physical control of the asset, but the control over the service potential of the asset. The department must not only benefit from the service potential but also have the ability place restrictions on the service potential and carries all the risks associated with the use, safeguarding and disposal of the asset; and
  - b) Value can be reliably measured. The value of the asset must be reliably measurable either by its cost or through fair value.
- 14.4 Recording is the process of capturing the financial information relating to a particular transaction, event, asset or liability in the electronic or manual accounting records of the department for the purposes of disclosure as secondary financial information.
- 14.5 Disclosure is the depiction of a recognised and or recorded item of the information in the notes to the financial statements in accordance with the requirements of the MCS, whereas presentation refers to the layout and positioning of the item within the primary financial information.

## PART 15: MATERIALITY AND RECOGNITION

15.1 In terms of the MCS, materiality could be viewed as follows:

“Material omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements. Materiality depends on the nature or size of the omission or misstatement judged in the surrounding circumstances. The size or nature of the information item, or a combination of both, could be the determining factor.”

15.2 The capitalisation threshold is the value above which assets are capitalised. The Modified Cash Standard currently separate's capital assets into Major and Minor Assets.

15.3 Major assets are defined as tangible or intangible non-current assets with a capitalisation threshold equal to or greater than R5000 while minor assets have a capitalisation threshold less than R5000.

15.4 Neither the MCS nor standards of GRAP make provision for a value threshold that forms of part of the attributes/criteria when an item assessed as an asset. However it is common practice for departments to adopt an internal policy defining a value threshold, over and above the major and minor classification prescribed by the Treasury, below which it will expense items in the year of acquisition.

15.5 Treasury Accounting Guide for Property Plant and Equipment (GRAP 17), states that “It is important to note that assets should be capitalised in accordance with GRAP 17 when it meets the definition of property, plant and equipment, regardless of the cost price of an asset. Therefore, in accordance with GRAP 17, if an asset is expected to be used for more than one reporting period, it should be capitalised. If an entity does have a policy with a capitalisation threshold below which assets are expensed, this policy should be an internal policy of the entity and should not appear in the accounting policies to the financial statements, as this would constitute non-compliance with GRAP 17”

- 15.6 The Treasury Asset Management Guide states that “any discussion of asset management pre-supposes that participants understand what an asset is – not just in an accounting sense – but what it represents to an entity and how it contributes to programme delivery” while the Framework for Strategic Plans states that “The effective and efficient management of public sector assets is fundamental in an environment where there are competing demands for Government resources”.
- 15.7 Movable capital assets constitute the majority of assets used by departments in the day to day administration of their functions and amounts to huge numbers and billions of rand. Recording capital assets and reporting thereon has a material impact on financial statements due to the continued investment in new assets on an annual basis and the value involved. However, the need to control a myriad of assets that cannot be classified as capital assets because of their value but, clearly have lifespans far in excess of one year has resulted in the adoption of value thresholds where departments have found themselves allocating financial and human resources to the management of items where the cost of controlling these assets far exceeds the benefit of control. As a result, value thresholds have a significant impact on the size of the asset register and the complexity of asset management.
- 15.8 These internal policies place departments at risk of negative audit findings as they constitute non-compliance with standards of GRAP and the risks of capitalisation thresholds be set to high resulting in material misstatement. Materiality is an important concept both for financial reporting and for the work of the external auditors. Audit procedures are designed to detect cumulative or individual errors that would result in material misstatement of departments financial statements and financial statements that contain material misstatements cannot obtain an unqualified audit opinion.
- 15.9 Departments are advised to depart from the common practice of simple value thresholds in favour of considering the cost-benefit of controlling the asset versus the risk to service delivery and the materiality of non-disclosure.

15.10 Departments may approach the assessment on the basis of categories. Therefore after careful analysis of the nature, quantity and cumulative impact of non-disclosure, a risk assessment might conclude that Kitchen Equipment as a category will be excluded from recognition.

The application of judgement by each department means that the information provided may not be consistent across departments in all cases. It does however mean that more meaningful information is provided to the users of the financial statements.

15.11 The exclusion list should be included in the policy of the department and revised on an annual basis.

15.12 A list of all assets derecognised from the AFS shall be compiled and be approved by the accounting officer at least annually. Should the need arise to add an assets to the list, a proper motivation as to the reasons for treating the asset differently must be compiled and forwarded for approval.

15.13 As opposed to a simple value threshold, the abovementioned approach is aimed at improving the integrity and achieving a greater degree of consistency in management assumptions and the resulting presentation of financial statements.

15.14 In addition, departments are required to ensure that all assets, current and non-current, irrespective of nature and value, are safeguarded and will include in its policy adequate provisions for physical control and safeguarding of all assets.

15.15 All movable assets shall be allocated an ICN linked to the relevant SCOA Code according to the SCOA Asset segment types. This will result in less discrepancies and a more accurate account of Departmental assets.

15.16 ICNs are standardised throughout the department and ensure that a unified naming convention and asset classification is applied to the description of assets. A correct ICN (item record number) must at all times be used as it is

the only way to identify the correct asset that needs to be procured. It also enables the department to have a complete and accurate description of the assets required. If the incorrect ICN is used the consequences can lead to:

- a) Incorrect deliveries of either services or goods;
- b) Incorrect classification of assets resulting in additional reconciliation at month-end and a risk of classification misstatement in the financial statements of the department; and
- c) Incorrect useful life determination.

15.17 All requests for ICNs shall be reviewed and authorised by the delegated official. Officials from both SCM and Finance are required to review and authorise ICN requests. These requests will include the SCOA allocation and LOGIS classification.

## PART 16: ASSET EXCLUSION LIST

- 16.1 The Asset Accounting Policy Guide provides for an exclusion list to enable departments to focus on strategic assets for reporting purposes in the AFS and to exclude non-strategic assets from disclosure in the AFS. However, the assets excluded from reporting in the AFS will still require safeguarding and control on, for example LOGIS, SYSPRO etc.
- 16.2 Authority for the implementation of an asset exclusion list is derived from the Asset Management Framework issued by NT in 2004, Chapter 6 Asset Life-Cycle Management paragraph 6.2.5.2 Asset thresholds- Dealing with minor assets states "Certain entities set a 'recording' threshold i.e. assets where the historical cost or fair value is under a certain amount, are recorded in the registers of the entity but depreciated in full in the year of acquisition. The recording in the asset register is necessary in order that control can be exercised over the asset. The recording threshold is based on cost-benefit considerations in terms of accountability, probity and management of assets. The common example of items that are recorded is 'portable and attractive' items, which are generally below the 'reporting' threshold.
- 16.3 In terms of the following extract from the MCS, AO's need to be cautioned that the total amount of assets exempted from reporting in the AFS should not become material when compared to the total asset base.

MCS Chapter on Concepts and Principles, Paragraph, 25 "Material omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements. The size or nature of the information item, or a combination of both, could be factors in determining materiality of the omission or misstatement".

MCS Chapter on Concepts and Principles, Paragraph 70 further states" In assessing whether an item meets these criteria and therefore qualifies for inclusion in the financial statements, regard needs to be given to the materiality considerations discussed in paragraphs .23 to .25".

MCS Chapter on Concepts and Principles, paragraph 23 states “The relevance of information is established by reference to the nature and the materiality of the information concerned”.

Paragraph 24 further states that “Information is material if its omission, misstatement, or non-disclosure could influence the decisions of users made on the basis of the financial statements. Materiality depends on the nature or size of the item or error judged in the particular circumstances of its omission, misstatement, or non-disclosure in the financial statements. Thus, materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have to be useful.

16.4 Departments that decide to implement an asset exclusion list from 1 April 2016 are required to identify assets for exclusion from disclosure in the AFS based on the following:

- i. The Asset Accounting Policy of the department should include an asset exclusion list framework to be applied when selecting assets to be excluded, as well as the management of these assets by the department;
- ii. Compile a list of assets to be excluded based on the template provided (see Annexure); and
- iii. The asset exclusion list and the content and policy framework must be approved by the Accounting Officer and finalised in consultation with the Provincial Treasury before implementation.

16.5 Departments may also apply the following guidelines when compiling an asset exclusion list:

- i. The use of a threshold as a point of reference;
- ii. The total accumulated value of the excluded assets must be assessed annually to ensure that it does not lead to an audit risk; and



- iii. From asset registers, a list of assets needs to be extracted, that will be included as part of the asset exclusion list. These assets must be identified through unique asset identification descriptions.

16.6 The following process must be followed when implementing the exclusion list:

- a) Before any changes are implemented a full asset count must be performed by the department to ensure completeness (from floor to register) and existence (from register to floor) of the asset register;
- b) All assets not verified during the asset count may not be included in the Exclusion List and must be dealt with in terms of the Loss Control Process;
- c) The Department must include the following details of the assets included in the exclusion list:
  - Item ICN number. This is the standard unified identification code used in LOGIS. The list of ICNs must be submitted to the Provincial Treasury for review;
  - Item description;
  - Unit cost of the asset;
  - Control (processes and internal control mechanisms); and
  - Safeguarding measures.
- d) Assets identified for the exclusion list should be de-recognised from the asset note in the financial statements as "Disposals" with the following narrative explanation:

"Based on the asset accounting policy of the department, disposals include assets to the amount of R..... that have been identified and taken up in the asset exclusion list as they are not strategic in nature. The assets excluded will be managed separately".
- e) The asset disclosure note supporting the de-recognition of assets must also include the following:
  - The total value of assets affected by the de-recognition;
  - The total value and number of assets by class affected by the de-recognition;

- A statement that a full asset verification of movable assets was performed and that all assets were verified.

A department who decides to control the de-re cognised assets outside of LOGIS needs to follow the Disposal process as per AOS on LOGIS. Disposed / de-recognised assets needs to be manually controlled on the Departments own manual system.

A department who decides to control the de-re cognised asset through LOGIS do not need to capture any transactions on LOGIS.

## **PART 17: COMPONENTS**

- 17.1 GRAP requires the various components of an asset to be identified separately if they have differing patterns of benefits and are significant relative to the total cost of the item.
- 17.2 Components are usually not functional in their own right. These items are often replaced within the lifetime of the main asset and form a significant part of the main asset in terms of their importance to its main use and value. Such capital parts form part of the main capital asset, but have a useful life that is different to that of the main asset.
- 17.3 Components may wear out or depreciate at different rates, and some may have a higher risk of impairment or obsolescence than others.
- 17.4 Therefore, where a significant component is expected to wear out more quickly than the overall asset, it is depreciated over a shorter period and any subsequent expenditure on restoring or replacing it is capitalised. This approach means that different depreciation periods may be used for each component.
- 17.5 It is appropriate to account for component parts of an asset separately when the component assets have different useful lives and provide benefits to an entity in a different pattern from that of the complex asset.
- 17.6 Decisions about which components are accounted for separately usually reflect the systems put in place to ensure that the service delivery capabilities of the complex assets are monitored, managed and maintained on an appropriate basis. Items are only componentised where the master and sub-asset relationship is maintained for the componentised asset.
- 17.7 Significant parts of an asset with similar useful lives and patterns of consumption can be grouped together. There is no minimum requirement for how many parts of an asset should be identified. The number of parts may vary depending on the nature and complexity of the asset. All relevant parts of an asset are identified at the date of initial recognition and the number of identified parts should not vary after the date that the asset is ready for use.
- 17.8 The challenge is to determine how far the asset should be broken down into components for the purpose of separate recognition by applying the concept of 'materiality'. To perform materiality testing, a de-minimised limit is normally set, below which assets are excluded from component accounting. Materiality may be considered in terms of the effect on the reported

depreciation cost and the carrying values of assets but essentially it is a matter of professional judgment.

- 17.9 Once a materiality level has been set, the meaning of 'significant component' needs to be considered and applied to individual assets. A significant component may be one that has a significant value compared to the asset as a whole but a significantly shorter useful life and will require replacement on at least one occasion during the life of the asset as a whole. Clearly, any measure used to determine components is subjective.
- 17.10 In accordance with the MCS, thresholds are not applied at a component level where the asset has been recorded in the asset register on a component level. Components are always capital in nature by virtue of being part of a capital asset even where separately recorded in the asset register; they still form part of the overall asset.
- 17.11 Where a component is replaced or restored, the carrying amount of the old component is derecognised to avoid double-counting and the new component reflected in the carrying amount, subject to the recognition principles. Recognition and de-recognition occur regardless of whether the replaced part has been depreciated separately. De-recognition of a capital asset component takes place when no future economic benefits are expected from its use – that is, its service potential is used up.
- 17.12 A capital asset is enhanced when a new component is added to the asset, an existing asset component is refurbished or upgraded, or when an asset component is replaced.
- 17.13 For the purpose of this Guide departments do not componentise any assets and must separately record items desirable for control on the asset register or else recognise only the single asset and expense components when replaced.

### **Example of Componentisation: Computer equipment**

- i. A department purchases a desktop computer for a new employee. The desktop provided to the new employee comprises of a screen, a mouse, a keyboard and the CPU. The total cost of the desktop is R8 500 and is made up as follows:
  - Screen R2 000
  - Mouse R200
  - Keyboard R1 200
  - CPU R5 100
- ii. The screen, mouse, keyboard and the CPU are components of the main asset, the desktop. If any of the parts are not there the asset cannot be used. The components should be capitalised as part of the main asset in the asset register of the department. The asset will be recorded as one asset at its full cost i.e. R8 500.
- iii. Should a component be replaced at a future date, the transaction will be classified as maintenance or a consumable depending on the departmental policy. The asset register is however updated with the new serial number but without amending the existing value of the asset. Alternatively, where the components are recorded separately as part of the computer asset, replacement of a component will impact on the asset register. The old component will be removed and the new component recorded. The overall value of the asset 'the computer' will thus change to reflect the 'new' component.

## **PART 18: MEASUREMENT OF CAPITAL ASSETS**

- 18.1 A department evaluates all costs on the date of acquisition and subsequent costs to add to, replace part of, or service the capital assets.
- 18.2 All movable assets shall be allocated a cost when the asset is included in the movable asset register in accordance with the standards of generally recognised accounting practice as defined in the Modified Cash Standard.
- 18.3 A movable asset that qualifies for recording as a capital asset shall be measured at its cost.
- 18.4 Where the cost cannot be determined accurately, the movable capital asset shall be stated at fair value.
- 18.5 A movable asset acquired before 1 April 2002 (or another date as approved by the OAG) will accordingly be measured at R1 if the cost cannot be determined accurately.
- 18.6 Where a movable asset is acquired through a non-exchange transaction, its cost shall be measured at its fair value as at the date of acquisition.

- a) Fair value

- i. Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.
- ii. For many assets, the fair value will be readily ascertainable by reference to quoted prices in an active and liquid market. For example, current market prices can usually be obtained for land, non-specialised buildings, motor vehicles and many types of machinery and equipment.
- iii. If no evidence is available to determine the market value in an active and liquid market of an asset, the fair value of the item may be established by reference to other items with similar characteristics, in similar circumstances and location or with reference to recent arm's length transactions concluded for similar assets. For example, the fair value of vacant land that has been held for a long period during which time there have been few transactions may be estimated by reference to the market value of land with similar features and topography in a similar location for which market evidence is available.

- iv. If an asset is of a specialised nature, and market-based fair value is not available, a department may need to estimate the fair value using either the reproduction cost or replacement cost.
  - v. In some cases, an asset's reproduction cost will be the best indicator of its replacement cost. For example, in the event of loss, a parliament building may be repaired to its original state rather than be replaced with alternative accommodation because of its significance to the community.
- b) Depreciated replacement cost
- i. In many cases, the depreciated replacement cost of an asset can be established by reference to the buying price of a similar asset with similar remaining service potential and similar condition in an active and liquid market.
  - ii. The value is determined by the cost of a new asset of the same type. The cost is then adjusted to take into account the differences between the old asset and the new in terms of bigger capacity and depreciation to reflect the remaining useful life of the actual asset on hand.
  - iii. The replacement cost is the cost to replace the service potential of an asset as new and must therefore be adjusted for condition and age to bring into account that the asset being valued has already lost some service potential through its use.
  - iv. To facilitate cost-effective compliance with the MCS and to avoid unnecessary duplication of costs across different spheres of government, departments are encouraged to as far as possible make use of existing available information (for example municipal valuation rolls) as an alternative to undertaking their own professional valuations on each individual immovable asset. Should the municipal valuation change the department should not revise the initial recognition amount except if there is evidence that the initial recognition value was erroneous.

### **Example: Capital assets acquired through a non-exchange transaction**

#### *Scenario 1*

A private entity not related to any government institution donates a laptop to the Government Department together with all its historical supporting documentation including the original invoice and the asset register details on the 28th of February 2014 and the details as per the asset register are as follows

- Cost Price = R9 000.00 (Agrees to the invoice supplied)
- Accumulated depreciated = R3 000.00
- Book Value = R6 000.00
- Purchase Date = 01/03/2013

The asset is the donation from the non- government entity, therefore the Department is still required to fair value the donated asset as much as all the supporting documentation was provided. This is to ensure that the asset is initially recorded at its fair value since the book value provided doesn't necessarily translate to the fair value of the asset. Government in general is gaining an asset that was never on its books.

#### *Scenario 2*

Government Department A donates a laptop to the Government Department B on the 15<sup>th</sup> of September 2014.

Accompanying the donation is the original purchase invoice amounting to R10 000.00 with the purchase date of 01/06/2010 and all the applicable PFMA S42 requirements being complied with. This is the transfer from one department to the other department, therefore Department B will accept and record the laptop at the provided amount of R10 000.00. Government in general is not gaining any additional asset as the asset was already within government environment.



### Scenario 3

Same scenario as in 2 above except Department A recorded the laptop at a value of R1 as it did not keep a proper asset register at the time of acquisition. As the Department did not retain documentation as required by the Treasury Regulations it cannot provide substantiating documentation on the cost of the laptop. Department A must therefore determine the fair value of the laptop, update its asset register, and then transfer (section 42) to Department B providing documentation as to how the fair value was arrived at. Department B will record the laptop at its fair value.

### Scenario 4

Example: Donation of library material.

External parties donate five new books to the library of Department E. The donor does not furnish details of the value of the books. The librarian searches three booksellers' websites on the internet to determine the cost of the books. The average cost of books from the three booksellers is R5 800.

The books meet the definition of capital assets and are in good condition.

Each book will be captured in the major asset register at R5 800.

## 18.7 Elements of Cost

- a) The cost of a capital asset comprises:
  - i. Its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
  - ii. Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
- b) Examples of directly attributable costs are:
  - i. Compensation of employees directly involved in the construction or acquisition of the asset to the extent that the department can reliably estimate the amounts to be treated as capital expenditure;
  - ii. Costs of site preparation;
  - iii. Initial delivery and handling costs;

- iv. Installation and assembly costs;
  - v. Costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as
  - vi. Samples produced when testing equipment); and
  - vii. Professional fees.
- c) Recording of costs as part of a capital asset ceases when the capital asset is in the location and condition necessary for it to be capable of operating in the manner intended by management. Therefore, costs incurred in using or redeploying an item is not included. For example, the following costs are excluded:
- i. Costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity;
  - ii. Initial operating losses, such as those incurred while demand for the item's outputs build up; and
  - iii. Costs of relocating or reorganising part or all of the department's operations.
- d) The cost of a self-constructed asset is determined using the same principles as for an acquired asset.

#### 18.8 Project expenditure - construction of capital assets

- a) Costs incurred to acquire a capital asset through construction by way of a project that spans over more than one financial year should be accumulated and will be added to determine the cost of the ultimate asset once available for use based on the principles above.
- b) During the stage where the capital asset is being constructed, all costs will be shown as capital work in progress.

## 18.9 Warranty costs

- a) When a department acquires an asset, such as a motor vehicle, the invoice price sometimes includes an element relating to the manufacturer's warranty. These costs are deemed to form part of the initial cost of the asset as they are directly attributable to bringing the asset to its location and condition necessary for it to be capable of operating in the manner intended by management. The warranty enables the department to derive service potential from related assets in excess of what could be derived had the warranty not been there. The cost of the warranty is therefore accounted as part of the asset acquisition cost.
- b) Where a warranty is bought subsequently the definition of an asset should be applied to determine whether it should be recorded as such or not. An example is the warranty on major parts which can be purchased for vehicles or extended service warranties. These items will not form part of the cost of the asset.

## 18.10 Assets transferred between departments

- a) All capital assets must be transferred at cost where cost information is available. Where the asset is recorded at R1 or at its fair value in the asset register of the transferor then the asset should be transferred at fair value, except for movable assets acquired before 1 April 2002 (or another date approved by the OAG) where they have been recorded at R1.
- b) All the documentation supporting the value should accompany the assets transferred.
- c) Transfer of assets should take place in terms of section 42 of the PFMA.

## 18.11 Subsequent Costs

- a) The MCS prescribes the following with regard to subsequent costs: " A department does not include in the carrying amount of a capital asset the costs of the day to-day servicing of the item. Rather, these costs are recognised in surplus or deficit as incurred. Costs of day-to-day servicing are primarily the costs of labour and consumables, and may include the cost of small parts. The purpose of these expenditures is often described as for the 'repairs and maintenance' of the capital asset".

- b) The following definitions apply as defined in SCOA Classification Circular 3 of 2009:
- i. Maintenance and repairs – Activities aimed at maintaining the capacity and effectiveness of an asset at its designed level. The maintenance action implies that there is an attempt to restore the asset to its original condition and there is no significant enhancement to its capacity, or the value of the asset. Such transactions are always classified as current payments.
  - ii. Upgrades and additions – Activities aimed at improving the capacity and effectiveness of an asset above that of the initial design purpose. The decision to renovate, reconstruct or enlarge an asset is a deliberate investment decision which may be undertaken at any time and is not dictated by the condition of the asset, but rather in response to a change in demand and or change in service requirements. Projects that in the past were identified as capital maintenance should be included in this item, as the decision to capitalise implies that the capacity of the asset will be improved beyond its initial design. Upgrades and additions are always classified as payments for capital assets.
  - iii. Rehabilitation and refurbishment – Activities that are required due to neglect or unsatisfactory maintenance or degeneration of an asset. The action implies that the asset is restored to its originally intended condition, thereby enhancing the capacity and value of an existing asset that has become inoperative due to the deterioration of the asset. Such transactions are always classified as payments for capital assets.
- c) Any subsequent expenditure incurred on an existing capital asset (owned or to be owned by the department) that is of a capital nature (i.e. extends the useful life of the asset and results in a change in functional specification) is added to the cost of that asset.
- d) Where the subsequent expenditure relates to a project that spans over more than one financial year, the total project costs are added to the cost of the capital asset at the end of the project. (i.e. when the capital asset is ready for use).

## **PART 19: RECORDING OF CAPITAL ASSETS**

- 19.1 For the purposes of recording capital assets, a department should maintain an asset register that will enable it to manage its assets, which includes the maintenance and replacement thereof, as well as to ensure that appropriate safekeeping measures can be put in place. It also assists with compliance with the disclosure requirements in the notes to the financial statements.
- 19.2 Upon initially recording a capital asset, a department must determine whether the capital asset is a minor or major capital asset and record the asset as such.
- 19.3 The threshold value for distinguishing between minor and major capital assets is determined by the OAG, which is currently R5 000, meaning any asset costing R5 000 or above should be recorded as a major capital asset.
- 19.4 Even though minor capital assets are not recorded under expenditure for capital assets, the total rand value and quantities of these assets are separately disclosed under the capital assets notes (refer to the section on Notes for the disclosures required). The minor capital assets register must be made available to the external auditors at year-end. The controls over safekeeping, etc. of these assets are the same as for major capital assets. The register should be as at 31 March of the respective year. The minimum requirements of the minor capital assets register are the same as those of the major capital assets register.

## **PART 20: FINANCIAL DISCLOSURE**

- 20.1 Recognition is the process of incorporating into the statement of financial position or statement of financial performance, an asset that meets the definition of an asset and satisfies the criteria for recognition.
- 20.2 An asset item should be recognised in the financial statements if it meets all of the following criteria:
- a) Probability criteria (it is probable that any future economic benefits or service potential associated with the asset will flow to the entity); and
  - b) Measurement criteria (the asset has a cost or value that can be measured with reliability).
- 20.3 For departments, Financial Statements are prepared in accordance with the MCS.
- 20.4 Any changes to the format for reporting of assets in the Financial Statements will be indicated in the modified cash standard as issued annually by the National Treasury.
- 20.5 When an item meets the definition of an asset, the item shall be grouped in the appropriate asset category as defined below:
- a) Transport Assets
  - b) Computer equipment
  - c) Furniture and Office Equipment
  - d) Other Machinery and Equipment
  - e) Heritage Assets
  - f) Biological Assets
  - g) Specialised military assets
  - h) Intangible Assets
- 20.6 Only items controlled by the department shall be recognised in the financial statements of the department.
- 20.7 All items costing R5 000.00 or more are classified as major assets.
- 20.8 All items costing less than R5 000.00 are classified as minor assets.

20.9 Assets shall be disclosed in the relevant note to the financial statements as prescribed in the modified cash standard, as amended annually by the National Treasury.

- a) The Opening Balance for a specific financial year (20X1) should be equal to the closing balance as at 31 March of the previous financial year (20X0). This column represents the cost/value of the assets included in the asset register as at the beginning (including any corrections made relating to the prior year or years prior to that) of the financial year. The note for the prior year must be completed first as the closing balance pulls through automatically to this column.

Prior year errors: Any prior period errors that affect the opening balance of the prior period (e.g. in this case prior to the 20x0 year) will be adjusted in the prior period error column via the Prior Yr TB sheet. Similarly where there are errors identified relating to the prior period (e.g. in this case in the 20x1 year) the corrections must be made via the Prior Yr TB in the respective column where the error occurred.

Any capital assets acquired in prior financial years that have only been included (captured) in the asset register during the current financial year should be included in the prior year comparatives. This is necessary to ensure that only the actual movement in capital assets (cash and non-cash), for the reporting period is reported as 'movement'.

- b) Any prior period error corrections in the current year relating to assets already recorded in the asset register prior to the beginning of the current year should therefore also be included in the relevant column of the comparatives. This can include corrections to cost and a change of asset category. Documentation relating to changes must be retained for audit purposes. The following can give rise to adjustments:
  - i. Prior year additions and shortages identified during the last stock take for the previous year which had not been corrected on the balances before the end of the previous year. The additions and shortages therefore represent the difference between recorded asset amounts and physical existence;
  - ii. Reclassification of inventory or consumables to assets after the previous year end. All assets previously classified as inventory or consumables need to be accounted for and transferred from inventory to either the major or minor assets register;

- iii. Reclassification of Assets to Inventory or Consumables after the previous year end. All inventory or consumables that were previously classified as assets need to be accounted for and transferred from the asset register to the inventory register or expensed;
  - iv. Reclassification of Assets incorrectly allocated to asset categories and SCOA allocations; and
  - v. Price Adjustments: This represents correction of errors that occurred in the previous financial year that relate to the initial recognition amount (cost of asset purchased).
- c) Additions. The additions column includes all movable assets relating to transactions effected during the current financial year, whether involving cash or non-cash. The additions must agree to the total amount in the "ADDITIONS TO MOVABLE TANGIBLE CAPITAL ASSETS PER ASSET REGISTER FOR THE YEAR ENDED 31 MARCH. These include the costs of multi-year projects completed in the current year.
- i. Additions/Purchases-Cash: All cash additions for the year must be reflected.
    - The cash additions as per MAR should reconcile with the amount reflected for assets in the BAS system; and
    - Additions and purchases on BAS must be reconciled to the AR on a monthly basis and all non-reconciling transactions must be reconciled in the following month.
  - ii. Additions, non-cash: The fair value or cost price, if supplied, of assets received in kind or as donations from sources outside of the government or as transfers without costs from other institutions during the reporting year is disclosed here. Adequate supporting documentation of such receipts should be kept.
  - iii. When multi-year projects are ready for use in the current year, the total cost of the ready for use asset to date should be taken on as a non-cash addition in the asset register and note.
  - iv. Finance leases. Finance lease assets should be taken on as a non-cash addition where the finance lease period has expired and the asset is still in use by the department.



Department shall include the sub-note on Finance lease expenditure in expenditure or capital assets. Note that this sub-note is effective for financial years beginning 1 April 2013, therefore only the current year information need to be disclosed. For future financial years, comparatives will also be shown.

- d) Capital work-in-progress current costs and finance lease payments: The payments made during the current reporting period on projects that have not been completed at year end as well as finance lease instalments for the current year should be included in this column and deducted from the calculation of the total column. The reason for this is that these payments are included in the amount reflected as 'cash' and are also reflected in the statement of performance (Expenditure for capital assets), but due to the fact that only assets ready for use and assets that remain in the department on expiry of the finance leases are taken on the asset registers of departments, the WIP costs and the finance lease instalments for the year are excluded from the note.

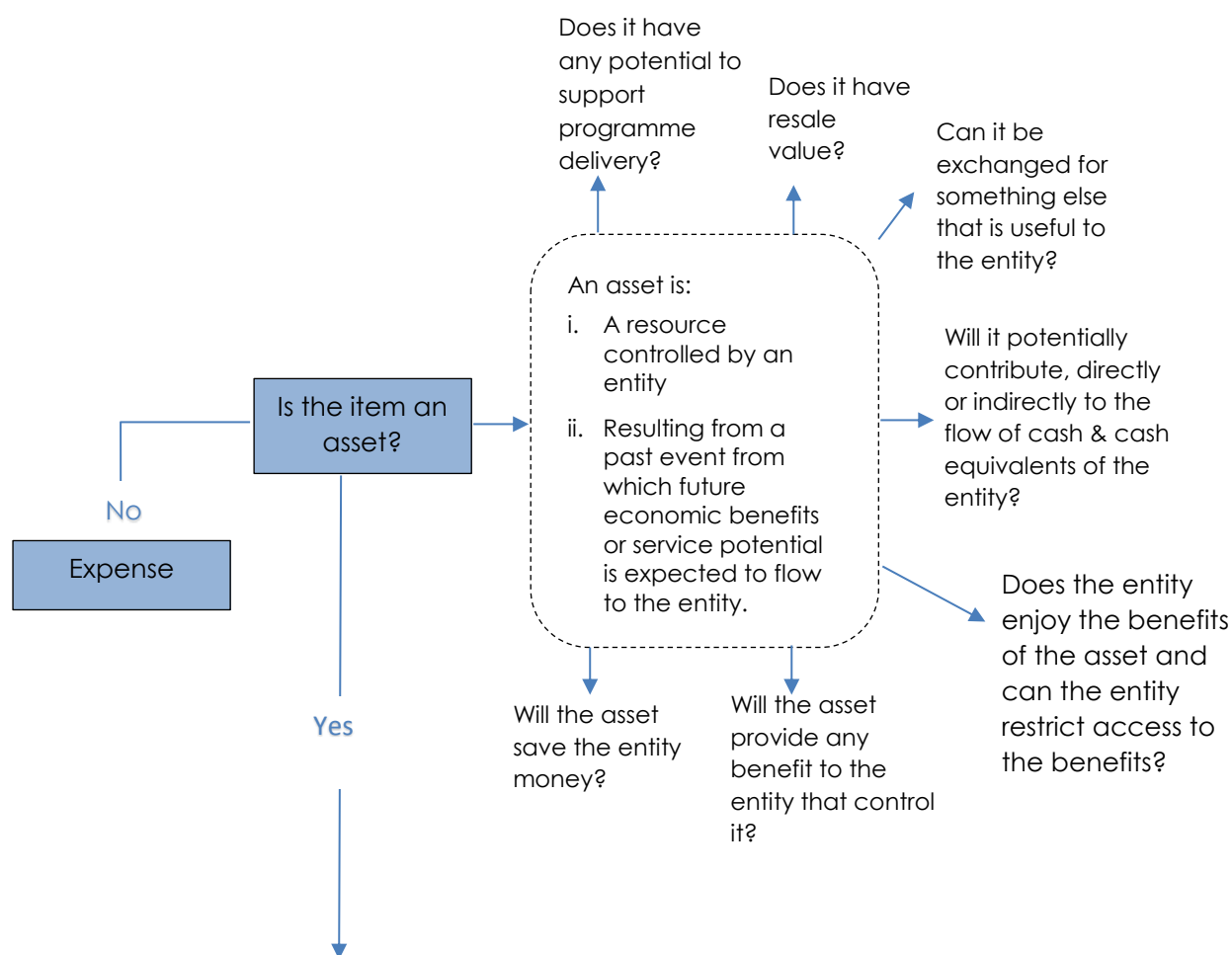
When the project capital asset is ready for use, the department accumulates the total capital works (i.e. capital work in progress of the previous year plus costs incurred to complete the project in the current year) in its asset register - The take-on of the "asset" is recorded as a non-cash addition. Once the contract is completed and final costing can be done the asset register is updated with payments made subsequent to the asset being ready for use e.g. retention payments and the amounts reflected under 'cash' in the note for additions as they will be current year expenditure. When the project is closed the asset with the updated cost will be reflected in the asset register.

- e) Accruals. (Received current not paid/paid current year received prior year) The cost per procurement documentation, of assets received before the end of the reporting period, e.g. 31 March, but not paid by that date should be included under this heading as an addition as it has already been included in the asset register.
  - i. Assets received prior to the current year, and only paid during the current year should be deducted under this column. These assets were included in the asset register as at the end of the prior year, but the cash payments are included under the 'Cash column' of the current year. Should the amount relating to these assets, not be deducted the additions for the current reporting period will be overstated and could be duplicated in the asset register if captured again.

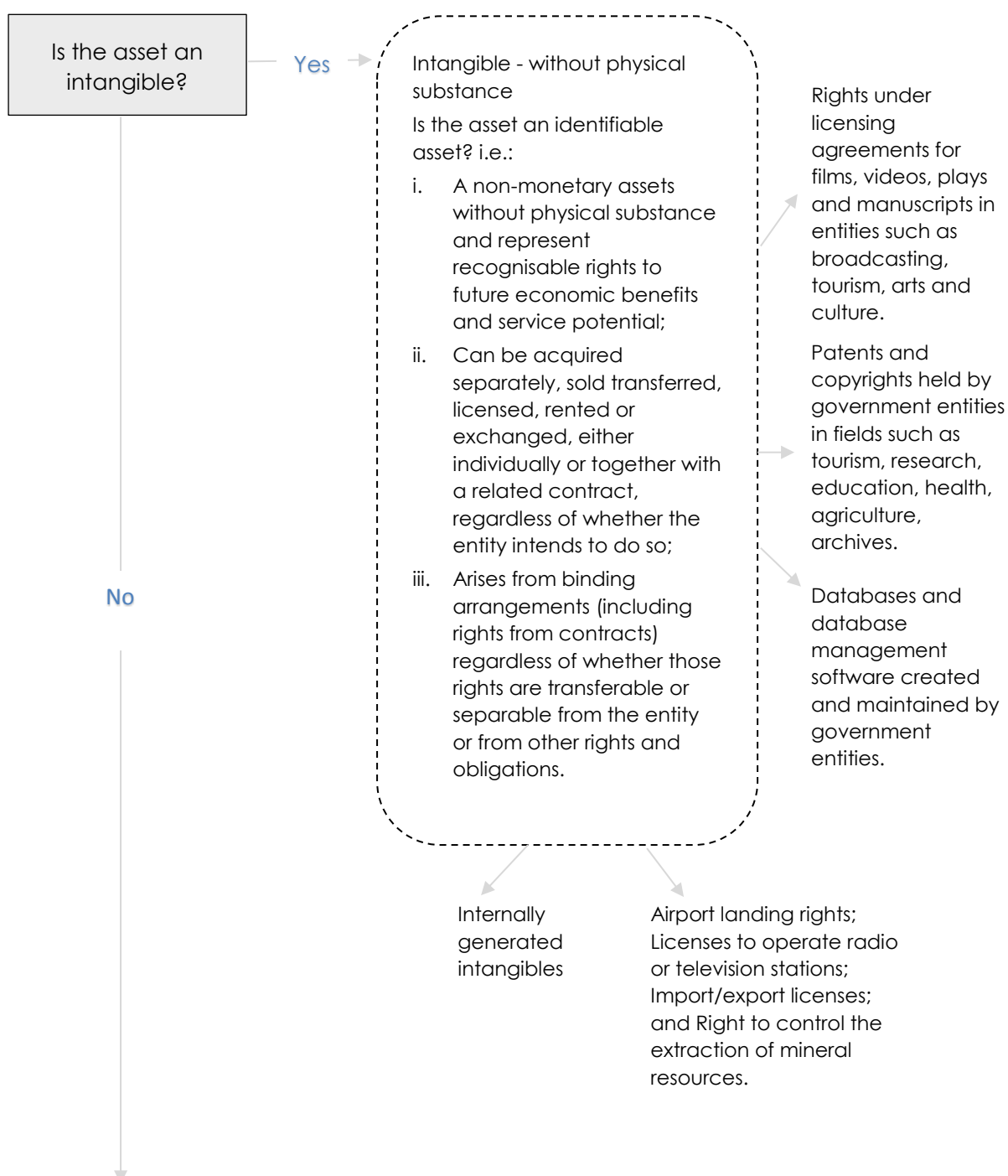
- ii. Where a difference between the procurement price and the payment has occurred, the comparative figures as well as the asset register must be updated to ensure that the actual amount paid for the asset is reflected in the asset register. The amount paid is deducted in this column and not the procurement value included in the prior year asset register as the former is the amount included under "cash".
- f) Disposals: An asset must be removed from the asset register and financial statements of the department upon disposal or when no future economic benefit or service potential can be derived from the asset. This means all assets sold, donated/transferred, scrapped, lost, damaged, etc. are derecognised.
  - i. The cost of all assets disposed of for cash and at no value during the current financial year, must be reported in this column. The disposals must agree to the total amount in the "DISPOSALS OF MOVABLE TANGIBLE CAPITAL ASSETS PER ASSET REGISTER FOR THE YEAR ENDED 31 MARCH.
  - ii. Sold for cash: The cost amount of assets as originally included in the asset register should be reflected in this column for all assets disposed of by selling for cash, during the current year. The manner in which the assets were sold is not important. The total amount in this column will not agree to any amount reflected in the statement of financial performance or any note thereto.
  - iii. Transfer out or destroyed or scrapped (Non-cash disposals) Transfer out - The cost amount as reflected in the asset register for all assets transferred to another government department or donated to any entity outside government should be reflected in this column. This implies that internal store transfers out are reflected in the asset register of the department's stores, but excluded when determining the transfer out amount for this disclosure note. The total amount in this column will not agree to any amount reflected in the statement of financial performance. Regarding interdepartmental transfers, PFMA section 42 must be followed or complied with and assets removed from the asset register when both parties have signed the section 42 documents and control has moved to the receiving department.

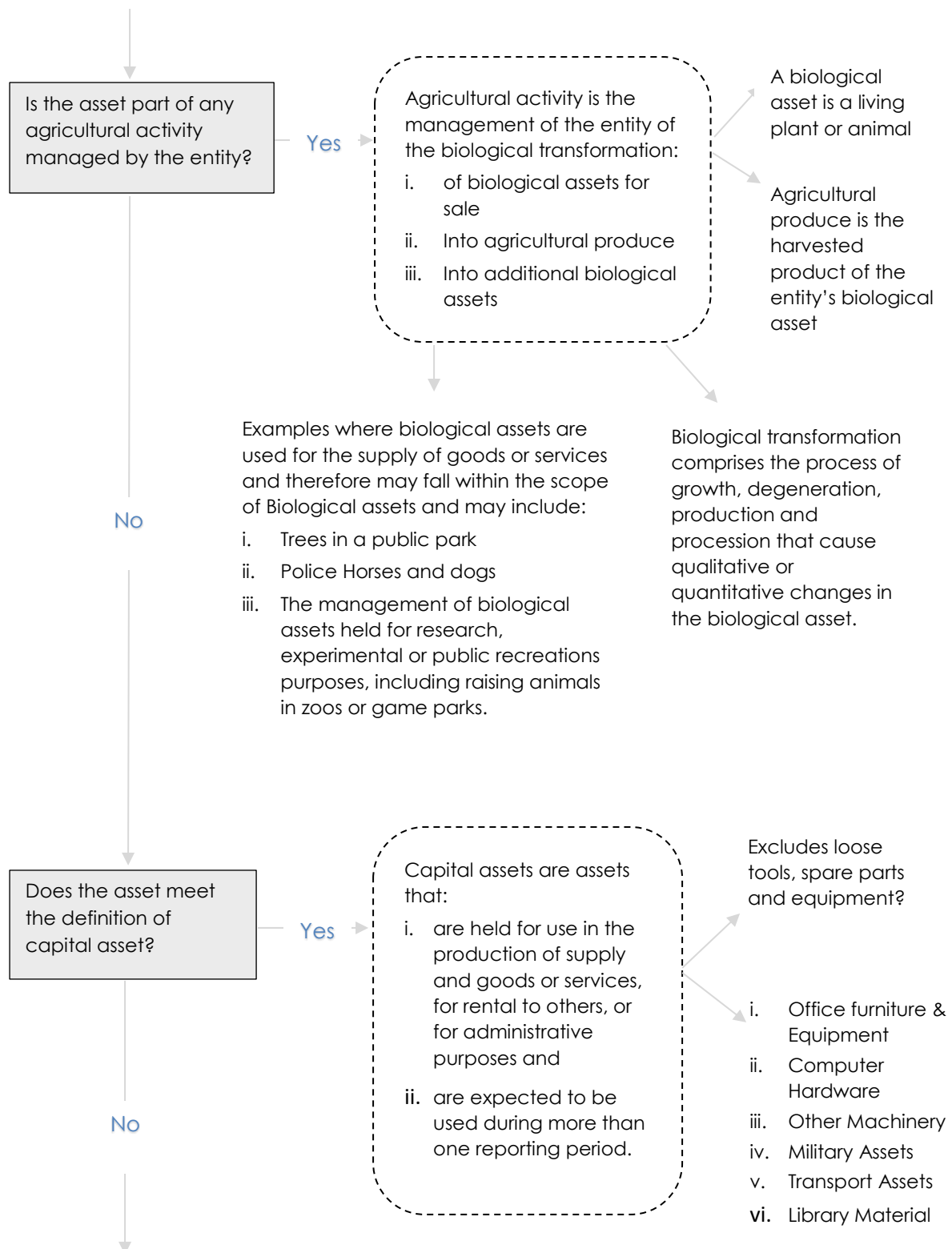
- iv. Destroyed or scrapped - The cost amount as reflected in the asset register for all assets destroyed or scrapped (including controlled dumping or other method of destruction and assets lost), should be reflected in this column. The total amount in this column will not agree to any amount reflected in the statement of financial performance.
  - g) All monies received from the sale of assets must be paid into the Provincial Revenue Fund in terms of section 13 (1) of the PFMA, Act No 1 of 1999. When items are sold as scrap the correct SCOA codes must be applied to ensure that the value of item disposed of as scrap can be accurately accounted for in the Annual Financial Statements.
  - h) Movable tangible capital assets - written off represent assets removed from the asset register during the financial year because they were lost, stolen, scrapped etc.
  - i) Closing Balance: This will be the value of the MAR as at 31 March of the financial year after a stock take has been undertaken, the physical quantities compared to the system quantities, corrections made to the system and any movements between the counting date and 31 March of the financial year „affected.
- 20.10 Assets that could not be found during the asset verification exercise should be documented in a loss control register. These discrepancies must be followed up and investigated. The outcome of the investigation will ascertain whether the asset has been disposed of (lost, stolen, sold or scrapped) and if it should be removed from the asset register. This write-off is disclosed in the note for Movable Assets written-off.
- a) This process should be completed by the time the annual financial statements are submitted for audit (i.e. by the 31 May or the actual date of submission if earlier).
  - b) The department must include a narrative with a summary of assets that could not be found. These assets will remain in the asset register until the investigation is complete and the outcome of that investigation will determine whether these assets should be removed from the asset register or not.
- 20.11 Departments will refer to the Specimen Annual Financial Statements for the illustrated disclosure requirements.

## ANNEXURE A: ASSET CLASSIFICATION AND RECOGNITION DECISION TREE

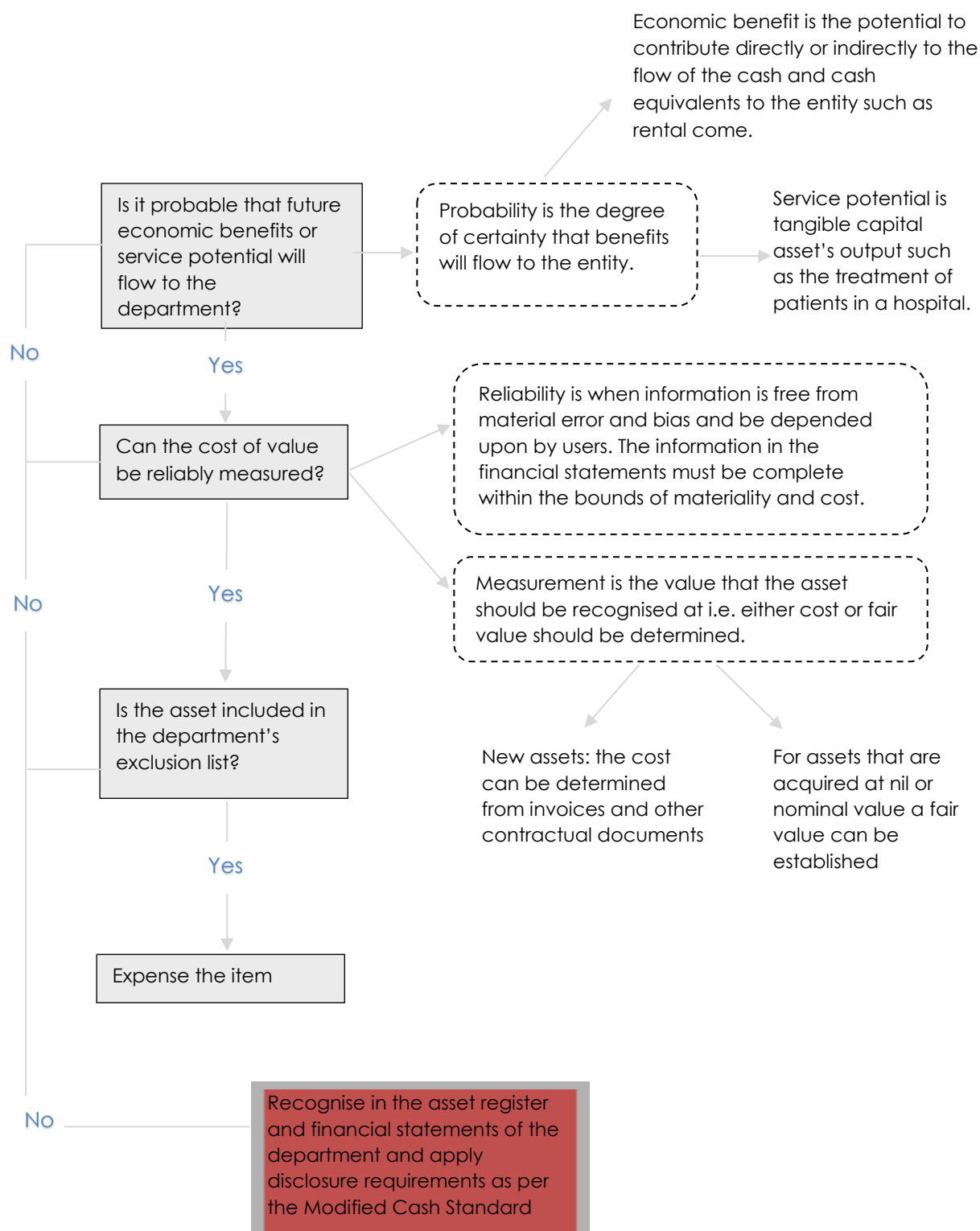


## 1. Nature of the asset





## 2. Testing the recognition criteria



## ANNEXURE B

### ASSET ACCOUNTING POLICY GUIDE ROLL-OUT PLAN

Activity	Responsibility	Due date
Issue circular	PT: Accounting	01-May-16
Workshop with FA Forum Members	PT: Accounting	To be confirmed
Workshop with Supply Chain Forum Members	PT: SCM	To be confirmed
Departments to review and align their Asset Accounting Policies in terms of AAPG	Departments	30-Jun-16
Departments to compile an Asset Exclusion list	Departments	30-Sep-16
Review departmental Asset Accounting Policies issued i.t.o consistency to AAPG	PT: Accounting/SCM/Systems	31-Aug-16
Assess Departmental asset exclusion lists against AAPG requirements	PT: Accounting/SCM/Systems	31-Oct-16
Departments to annually assess the cumulative effect of the excluded assets to determine materiality thereof.	Departments	31-Mar-17
Revise and update AAPG i.t.o latest developments	PT: Accounting/SCM/Systems	On-going