RESTORATION OF ESSENTIAL PUBLIC ASSETS POLICY

Version 1 Adopted on 24/02/2016 by Council Resolution 0216/005.

1. PURPOSE

The purpose of this policy is to provide Council with general guidance on how to account for the Natural Disaster Relief Arrangement associated activities – including Restoration Works, Betterment as well as Emergent Works on eligible public assets after a declared disaster event.

2. SCOPE

This policy applies activities and works associated with flood damage restoration and repairs to Council infrastructure. Maintenance expenditure can range from a few thousand dollars to repair road signage or clear table drains, too many thousands of dollars to restore the pavement (either gravel or sealed) to the road surface. In most cases, work undertaken is readily identified as maintenance and treated as an expense. However, at times the nature or intent of the work (or parts of the work) extends beyond restoring the asset to its original condition, capacity or function. In these cases, managers must decide whether the expenditure is most appropriately classified as "maintenance", or as a "capital outlay" that increases the value of the asset on which the expenditure is incurred.

Treating expenditure as maintenance (i.e. as an expense) affects the cost of Council's operating budget. Capital expenditure, on the other hand, has an impact on the value of Council's non-current assets and, subsequently, depreciation and community equity. Accounting for expenditure on assets in an appropriate and consistent manner will provide a more accurate indication of Council's output costs and of the value of its assets.

3. RESPONSIBILITIES

The administration of this policy is the responsibility of the Director of Corporate Services

4. DEFINITIONS

Council means Carpentaria Shire Council.
Commonwealth means Australian Federal Government
State means Queensland State Government

5. POLICY

When is maintenance work classified as a capital expenditure?
"Expenditure on assets must be capitalised (i.e. added to the carrying amount of the asset) when it improves the condition of the asset beyond its originally assessed standard of performance or capacity." in accordance with Queensland Treasury *Non-Current Asset Policies for the Queensland Public Sector – NCAP 1 Recognition of Assets*.

In general, work that includes upgrades, enhancements and additions to an asset would fall into the category of capital expenditure when it results in any of the following:

- an increase in the asset's useful function or service capacity
- an extension of its useful life
- an improvement to the quality of the service(s) delivered through utilisation of the asset
- a reduction in future operating costs
- the upgrade or enhancement becoming an integral part of the asset.

Conversely, work falls into the category of maintenance expenditure when it does not result in an improvement to the asset (i.e. it simply preserves the asset's original serviceability).

The Queensland Government Department of Housing and Public Work's *Maintenance, Management Framework* (MMF) defines "maintenance" as "work on existing assets undertaken with the intention of:

- re-instating physical condition to a specified standard
- preventing further deterioration or failure
- restoring correct operation within specified parameters
- replacing components at the end of their useful/economic life with modern engineering equivalents
- making temporary repairs for immediate health, safety and security reasons (e.g. after a major failure)
- assessing assets for maintenance requirements (e.g. to obtain accurate and objective knowledge of physical and operating condition, including risk and financial impact, for the purpose of maintenance)".

The Australian Accounting Standards Board's *Framework for the Preparation and Presentation of Financial Statements* defines "expenses" as "decreases in economic benefits during the accounting period in the form of outflows or depletion of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants".

It is the first part of this definition (i.e. "decreases in economic benefits… in the form of outflows or depletion of assets") that is relevant to this policy.

In the context of these two definitions, maintenance is a reflection of the consumption (through usage) of the asset. As this consumption results in a reduction in the value of the asset, it meets the definition of an expense. However, works undertaken in the course of maintenance may include activities that result in the expenditure being classified as capital

Restoration of Essential Public Assets (REPA) is classified either as:
a) Emergent works:
Activities necessary during the course of a disaster to protect eligible public assets or to restore essential public services and maintain public safety. Immediate post-disaster repairs to an eligible asset to enable it to operate/be operated at a reasonable level of efficiency – this would include clean-up costs, removal of silt/debris and / temporary repairs.

b) Restoration works:
For the restoration or replacement of eligible uninsured *essential public assets* damaged as a direct result of an *eligible disaster* to **their pre-disaster standard**. This may include restoration in accordance with current building and engineering standards if required by legislation or exceptional issues where reconstruction cannot occur without it while maintaining the same asset class.

Extension of useful life
Significant components within assets (e.g. road pavement, road sub-base, road base, drainage) are identified, recognised and depreciated separately. The useful life of each of these components is generally different to that of the asset and to each other.

Accounting Standard AASB 116: Property, Plant and Equipment defines "useful life" as:
"the period over which an asset is expected to be available for use by an entity; or the number of production or similar units expected to be obtained from the asset by an entity".

The *Non-Current Asset Policies for the Queensland Public Sector – NCAP 6 Depreciation and Amortisation* add that the useful life of an asset to one department may well differ from its useful life to another entity, or even differ between business units within the same entity.

Factors that influence the useful life of assets and their components include:

- physical wear and tear as a result of usage
- environmental conditions
- technical obsolescence
- commercial obsolescence
- legal compliance issues

- other limitations on the continued safe and legal use of the asset.

In the context of these factors, an extension of the useful life of an asset may result from work incorporating:

- a more robust material than that used in the original structure
- a component that benefits from an improved design (e.g. a new, more efficient compressor of the same capacity as the original).

As such, expenditure in these instances should be carefully reviewed with respect to its categorisation as either capital expenditure or expense (or a combination of both).

Reduction in future operating costs
Reductions in the future operating costs of assets may occur as a result of repairs that incorporate new materials, more efficient components, or new technology. For example, the integration of a polymer substance with gravel may serve to reduce future maintenance costs.

Even if these types of replacements are precipitated by maintenance requirements and fail to result in an increased output capacity or improvement in service quality, the expenditure should still be reviewed in terms of its capital content. In such cases, the intent of the work may be a relevant issue.

If the primary intent is to reduce future operating costs, the expenditure should be classified as capital.

However, replacement of an asset component purely for maintenance reasons – even if the replacement is made with a modern engineering equivalent that has the potential to reduce future operating costs – should be categorised accordingly unless there is a material change or enhancement in the physical characteristics of the asset.

Councils Treatment of REPA
Based on the conditions of funding from the Commonwealth/State Natural Disaster Relief and Recovery Arrangements (NDRRA), the Restoration of Essential Public Assets cannot be enhanced past their pre-disaster standard, which means that Council will provide the necessary “maintenance” works to restore the assets to their pre disaster standard and furthermore that Council will treat this work as an expense item within Councils operating budgets which will reflect through to Council’s Comprehensive Income Statement under Expenditure through the line item title Materials & Services which will be further expanded upon within the notes section of Council’s annual financial statements.

Exceptions
“Expenditure on assets must be capitalised (i.e. added to the carrying amount of the asset) when it improves the condition of the asset beyond its originally assessed standard of performance or capacity.” in accordance with Queensland Treasury *Non-Current Asset Policies for the Queensland Public Sector – NCAP 1 Recognition of Assets*.

Under the Queensland Disaster Relief & Recovery Arrangements Guidelines version dated October 2015, under Section 7.7 Betterment, Council would treat any approval under Betterment as capital and not under maintenance.

Betterment of an essential asset is the enhancement of an asset beyond a pre-disaster level of immunity, resilience, service or condition where legislation does not require current building and engineering standards, codes and guidelines be followed. For the purposes of this guideline, betterment costs means the difference between the cost of restoring or replacing an essential public asset to its pre-disaster standard, and the cost of restoring or replacing the asset to a more disaster-resilient standard.

According to the Determination (Guideline 7), Betterment is intended to limit the cost of rebuilding repeatedly damaged infrastructure by allowing essential public assets to be rebuilt to a more resilient standard where it is cost-effective to do so. In assessing the cost-effectiveness of a betterment proposal, both the financial and non-financial aspects of the proposal may be considered.

Betterment of an asset may be considered eligible if:

a) the asset is an essential public asset
b) the state and Australian Government are satisfied with the cost effectiveness of the proposal

c) the state and Australian Government are satisfied that the increased disaster-resilience of the asset will mitigate the impact of future natural disasters.

6. ASSOCIATED DOCUMENTS

- Queensland Disaster Relief & Recovery Arrangements – October 2015
- Australian Accounting Standards Board's Framework for the Preparation and Presentation of Financial Statements
- Queensland Government Department of Housing and Public Works – Maintenance Management Framework
- Australian Accounting Standard AASB 116: Property, Plant and Equipment
- Australian Accounting Standard AASB 136: Impairment Standard
- Carpentaria Shire Council – Annual Budget Document
- Carpentaria Shire Council – NDRRA Claim Submission/s

7. NEXT REVIEW

This policy will remain in force until otherwise determined by Council.

8. RESOLUTION.

Adopted on 24/02/2016 by Council Resolution 0216/005.

______________________ 24 / 02 / 2016

Bob Owen Date

Chief Executive Office