




LKAS 16 Property, Plant and Equipment

Presented by:


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The slide has a dark red background. In the top left corner, there is a small version of the CA logo and shield emblem. The main content is centered on the right side of the slide. It starts with the title 'LKAS 16 Property, Plant and Equipment' in a large, white, sans-serif font. Below the title, the text 'Presented by:' is written in a smaller, white, sans-serif font. Underneath that, the name 'Priyoshini Fernando' and the firm name 'PricewaterhouseCoopers' are listed in a bold, white, sans-serif font. A large, semi-transparent shield emblem with a scale of justice is positioned on the left side of the slide, overlapping the text area.


Overview

1. Introduction – Scope & definitions
2. Recognition
3. Measurement
4. De-recognition
5. Disclosures

Objective:
 prescribe the accounting treatment for property, plant and equipment (PPE) (i.e. recognition of assets, determination of their carrying amounts & depreciation charges and impairment losses)


Introduction – Scope & definitions

- Apply LKAS 16 when accounting for PPE, **except when another SLFRS / LKAS requires or permits a different accounting treatment.**
- LKAS 16 does **not** apply to:
 - (a) PPE classified as **held for sale** per SLFRS 5 *Non – current Assets Held for Sale and Discontinued Operations*
 - (b) **Biological assets** related to **agricultural activity** other than bearer plants (Refer LKAS 41 *Agriculture*)
 - (c) **Recognition & measurement of exploration and evaluation assets** (Refer SLFRS 6 *Exploration for and Evaluation of Mineral Resources*)
 - (d) **Mineral rights and mineral reserves** such as oil, natural gas and similar non – regenerative resources.

Introduction – Scope & definitions

Property, Plant and Equipment are **tangible** items that:

- are **held for use** in the **production or supply** of goods or services, for **rental** to others, or for **administrative** purposes; AND
- are expected to be used during **more than one period**

Investment property
under **cost model** – **LKAS 16**

Investment property
under **fair value model** -
LKAS 40

Recognition

Criteria for **recognition** of PPE

- It is **probable** that **future economic benefits** associated with the item will flow to the entity;
- AND**
- The **cost** of the item can be **measured reliably**

Cost of spare parts, stand – by equipment and servicing equipment that **satisfy** the **definition** of PPE are recognized per LKAS 16. If not, they are classified as inventory

Recognition

All costs incurred should be evaluated under the above **recognition principle** for assets, at the time such costs are incurred;

Cost of **day – to – day servicing** should **not** be capitalized

Recognition

- **Replacements :**

Parts of some items of PPE may require replacement – regularly, or at a lesser frequency.

Apply **recognition principle** above when recognizing replacements. **If recognition criteria are met**, recognize cost of the replacement part in the carrying amount of that item of PPE, when it is **incurred**.

The **remaining carrying amount** of those parts **replaced** is **derecognized** in accordance with the derecognition provisions of LKAS 16.



Recognition

- **Major inspections :**

Often a condition of continuing to operate item of PPE.

Apply **recognition principle** above when recognizing cost of each major inspection performed. **If recognition criteria are met**, recognize cost of that major inspection in the carrying amount of that item of PPE, when it is **incurred**.

The **remaining carrying amount** of the cost of the **previous inspection** is **derecognized**.



Recognition

Scenario 1:

Entity A, a supermarket chain is renovating one of its major stores. The store will have more available space for in – store promotion outlets after renovation, and will include a restaurant. Management is preparing budgets for the year after the store re – opens, which include cost of remodeling and the expectation of a 15% increase in sales resulting from the store renovations, which will attract customers.

Should cost of re-modelling the supermarket be capitalized?



Recognition

Scenario 2:

Entity B has an existing freehold factory property, which it intends to knock down and redevelop. During the redevelopment period, the company will move its production facilities to another (temporary) location. The following incremental costs will be incurred: set-up costs of CU 50,000 to install machinery in the new location, rent of CU 150,000 and removal costs of CU 30,000 to transport machinery from the old location to the temporary location.

Can these costs be capitalized into cost of new building?



Measurement at initial recognition

An item of PPE that **qualifies** for **recognition** as an asset shall be measured at its **cost**.

Elements of cost:

- **Purchase price**, including import duties and non – refundable purchase taxes, after deducting trade discounts and rebates,
- Any **costs directly attributable** to bringing asset to the location and condition necessary for it to be capable of operating in the manner intended by management,
- Initial estimate of the **costs of dismantling and removal** of item and restoring site on which it is located

Measurement at initial recognition

Which of the following costs would be included in the initial measurement of PPE?

Description of cost	Included?
Start - up and pre - production	
Operating losses prior to achieving planned performance	
Dismantling, removal and restoration	
Administrative and other general overheads	
Abnormal costs (repairs, wastage and idle time)	
Borrowing costs incurred during period of acquisition / construction / production of asset	

Measurement at initial recognition

Which of the following costs would be included in the initial measurement of PPE?

Description of cost	Included?
Start - up and pre - production	NO*
Operating losses prior to achieving planned performance	NO
Dismantling, removal and restoration	YES
Administrative and other general overheads	NO
Abnormal costs (repairs, wastage and idle time)	NO
Borrowing costs incurred during period of acquisition / construction / production of asset	YES (if LKAS 23 criteria is met)

Measurement at initial recognition

Which of the following costs would be included in the initial measurement of PPE?

Description of cost	Included?
Costs of opening a new facility	
Costs of introducing a new product (including advertising & promotional costs)	
Costs of conducting business in a new location or with a new class of customers (including training costs)	
Net off of Government grants received in connection with the acquisition of the PPE	
Fair value gains/losses on qualifying cash flow hedges relating the purchase of the PPE in a foreign currency	

Measurement at initial recognition

Which of the following costs would be included in the initial measurement of PPE?

Description of cost	Included?
Costs of opening a new facility	NO
Costs of introducing a new product (including advertising & promotional costs)	NO
Costs of conducting business in a new location or with a new class of customers (including training costs)	NO
Net off of Government grants received in connection with the acquisition of the PPE	YES
Fair value gains/losses on qualifying cash flow hedges relating the purchase of the PPE in a foreign currency	YES



Measurement at initial recognition

References to other accounting standards and interpretations:

- (i) IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*
- (ii) LKAS 23 *Borrowing Costs*
- (iii) LKAS 20 *Government Grants*
- (iv) LKAS 36 *Impairment*



Measurement after initial recognition

Accounting policy choice:

(1) Cost model

PPE is carried at cost less accumulated depreciation and accumulated impairment losses.



Measurement after initial recognition

(2) Revaluation model

- If fair value can be measured reliably, PPE is carried at **revalued** amount.
- **Revalued** amount = fair value as at date of revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses.
- Revaluations should be sufficiently regular to ensure carrying amount of PPE does not materially differ from that which would be determined using fair value as at end of reporting period.



Measurement after initial recognition

(2) Revaluation model

- If an item of PPE is revalued, entire class of PPE to which item belongs should be revalued.
- At the date of revaluation, asset is treated in one of the following ways:
 - (a) **Gross** carrying amount is adjusted in a manner that is **consistent** with the revaluation of the carrying amount of the asset. E.g. restatement proportionately to the **change** in carrying amount;
 - OR
 - (a) **Accumulated depreciation** is **eliminated** against the gross carrying amount of the asset.

Measurement after initial recognition

Example – Treatment of gross cost and accumulated depreciation when asset is revalued

Property, plant and equipment is revalued to C1,500 consisting of C2,500 gross cost and C1,000 depreciation based on observable market data.

Details of the property, plant and equipment before and after revaluation are as follows:

	Cost/Revalued cost C	Accumulated depreciation C	Net book value C
Property, plant and equipment before revaluation	1,000	(400)	600
Fair value			1,500
Revaluation gain			900
Gain allocated proportionately to cost and depreciation	1,500	(600)	900
Property, plant and equipment after revaluation	2,500	(1,000)	1,500

The increase on revaluation is C900 (namely, C1,500 – C600).

Measurement after initial recognition

Example – Treatment of accumulated depreciation when asset is revalued

Details of the property, plant and equipment before and after revaluation are as follows:

	Cost/revalued cost C	Accumulated depreciation C	Net book value C
Property, plant and equipment before revaluation	1,000	(400)	600
Property, plant and equipment after revaluation	1,500	-	1,500
Revaluation gain	500	400	

The increase on revaluation is C900 (namely, C500 + C400).



Measurement after initial recognition

- Accounting for effect of revaluation on an asset's carrying amount:

Increase	<ul style="list-style-type: none"> Recognized in other comprehensive income and accumulated in equity under revaluation surplus. Increase recognized in profit or loss to extent it reverses a revaluation decrease of same asset previously recognized in profit or loss
Decrease	<ul style="list-style-type: none"> Recognized in profit or loss. Decrease recognized in other comprehensive income to <i>extent</i> of any credit balance in revaluation surplus of asset.



Depreciation

- Depreciation* is the **systematic allocation** of the **depreciable amount** of an asset over its **useful life**.
- Each part of an item of PPE with a cost that is **significant** in relation to the total cost of the item shall be **depreciated separately**.
- Depreciation charge is recognized in profit or loss unless it is included in the carrying amount of another asset.
- Residual value, depreciation method** and **useful life** to be reviewed **at least** at each financial year end. If expectations differ from previous estimates, change(s) to be accounted for as a change in accounting estimate under LKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Depreciation

Example 01: Depreciation of separate components

An entity purchases a ship for CU 120 million. The ship (as a whole) has a useful life of 25 years. The engines, however, will need replacing after 7 years. The cost price of CU 120 million included CU 14 million in respect of the engines. Compute the annual depreciation charge.

Answer:

Depreciation charge on ship *excluding* engines

$$\begin{aligned}
 &= \frac{\text{Depreciable cost of ship excluding engines}}{\text{Estimated useful life}} \\
 &= \frac{106,000,000 \text{ CU}}{25 \text{ years}} \\
 &= \underline{\underline{4,240,000 \text{ CU}}}
 \end{aligned}$$

Depreciation

Example 01: Depreciation of separate components (contd)

Answer: (contd)

Depreciation charge on engines

$$\begin{aligned}
 &= \frac{\text{Depreciable cost of engines}}{\text{Estimated useful life}} \\
 &= \frac{14,000,000 \text{ CU}}{7 \text{ years}} \\
 &= \underline{\underline{2,000,000 \text{ CU}}}
 \end{aligned}$$

Total depreciation charge for the year

$$= \underline{\underline{6,240,000 \text{ CU}}}$$

Depreciation

Example 02: Change in depreciation estimates

An asset was purchased for CU 1,000,000 on 01 January 2013 and straight-line depreciation of CU 20,000 p.a. was charged (five year life, no residual value). A general review of asset lives is undertaken and for this particular asset, the remaining useful life as at 01 January 2015 is eight years. What should the annual depreciation charge be for 2015?

Answer:

Cost of asset	1,000,000 CU
Less: accumulated depreciation as at 01 January 2015	<u>(400,000) CU</u>
Carrying value as at 01 January 2015	600,000 CU
Remaining useful life as at 01 January 2015	8 years
Depreciation charge for 2015	<u>75,000 CU</u>

Derecognition

- An item of PPE is derecognized
on **disposal**;
OR
When **no future economic benefits are expected** from its use or disposal.
- Gains / losses arising from derecognition recognized in profit or loss when item is derecognized.
- Gains shall **not** be classified as revenue



Disclosure

Disclosures **include** –

- Reconciliation presenting carrying amount at commencement of year to that at end of the year (i.e. movement in year),
- Depreciation methods, useful lives and rates of depreciation used,
- Restrictions on title,
- Contractual commitments,
- Items pledged as security
- Disclosures on revalued assets (paragraph 77 to LKAS 16)
- Voluntary disclosures (paragraph 79 to LKAS 16)



THANK YOU