CA BUSINESS SCHOOL
EXECUTIVE DIPLOMA IN BUSINESS AND ACCOUNTING

SEMESTER 1

LKAS 16
PROPERTY, PLANT AND EQUIPMENT

M B G Wimalarathna

(FCA, FCMA, MCIM, FMAAT, MCPM)(MBA–PIM/USJ)

Objective

The objective of this standard is to prescribe the accounting treatment for property, plant and equipment so that users of the financial statements can discern information about an entity's investment in its property, plant and equipment and the changes in such investment.

The principal issues in accounting for property, plant and equipment are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognized in relation to them.

Scope

The standard shall be applied in accounting for property, plant and equipment except when another standard requires or permits a different accounting treatment.

This standard does not apply to:

a) Property, plant and equipment classified as held for sale in accordance with SLFRS 5; Non-current Assets held for sale and discontinued operations;
b) Assets related to agricultural activity (LKAS 41 Agriculture);
c) The recognition and measurement of exploration and evaluation assets; or SLFRS 6 Exploration for and Evaluation of Mineral Resources; and
d) Mineral rights and mineral reserves such as oil, natural gas and similar non-regenerative resources.

However, this standard applies to property, plant and equipment used to develop or maintain the assets described in (b) - (d) above.

Definitions

The following terms are used in this standard with the meanings specified:

Carrying amount is the amount at which an asset is recognized after deducting any accumulated depreciation and accumulated impairment losses.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration or, where applicable, the amount attributed to that asset when initially recognized in accordance with the specific requirements of other SLFRSs, e.g. SLFRS 2 share based payment.

Depreciable amount is the cost of an asset or other amount substituted for cost, less its residual value.

Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.

Entity-specific value is the present value of the cash flows an entity expects to arise from the continuing use of an asset and from its disposal at the end of its useful life or expects to incur when settling a liability.

Fair value is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arms’ length transaction.

An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.

Property, plant and equipment are tangible items that:

a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes;
b) are expected to be used during more than one period.

Recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

The residual value of an asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

Useful life is:

a) the period over which an asset is expected to be available for use by an entity; or
b) the number of production or similar units expected to be obtained from the asset by an entity.

Recognition

The cost of an item of property, plant and equipment shall be recognized as an asset if, and only if:

a) it is probable that future economic benefits associated with the item will flow to the entity; and
b) the cost of the item can be measures reliably.

Measurement at recognition

An item of property, plant and equipment that qualifies for recognition as an asset shall be measured at its cost.

Elements of cost

The cost of an item of property, plant and equipment comprises:

a) its purchase prices, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
b) 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.
c) the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purpose other than to produce inventories during that period.

Examples of directly attributable costs are:

a) cost of employee benefits (as defined in LKAS 19 Employee Benefits) arising directly from the construction or acquisition of the item of property, plant and equipment;
b) cost of site preparation;
c) initial delivery and handling costs;
d) installation and assembly costs;
e) costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any item produced while bringing the asset to that location and condition (such as samples produced when testing equipment); and
f) professional fees.

Examples of costs that are **not** costs of an item of property, plant and equipment are:

a) costs of opening a new facility;
b) cost of introducing a new product or service (including costs of advertising and promotional activities);
c) costs of conducting business in a new location or with a new class of customer (including costs of staff training); and
d) administration and other general overhead costs.

Measurement after recognition

An entity shall choose either the cost model or the revaluation model as its accounting policy and shall apply that policy to an entire class of property, plant and equipment.

Cost model

After recognition as an asset, an item of property, plant and equipment shall be carried at its cost less any accumulated depreciation and any accumulated impairment losses.

Revaluation model

After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period.

If an item of property, plant and equipment is revalued, the entire class of property, plant equipment to which that asset belongs shall be revalued.

If an asset's carrying amount is increased as a result of a revaluation, the increase shall be recognized in other comprehensive income and accumulated in equity under the heading of revaluation surplus. However, the increase shall be recognized in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognized in profit or loss.

If an asset's carrying amount is decreased as a result of a revaluation , the decrease shall be recognized in profit or loss. However, the decrease shall be recognized in other comprehensive income to the extent of any credit balance existing in the revaluation surplus in respect of that asset. The decrease recognized in other comprehensive income reduces the amount accumulated in equity under the heading of revaluation surplus.

Depreciation

Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately.

Depreciable amount and depreciation period

The depreciable amount of an asset shall be allocated on a systematic basis over its useful life. The residual value and the useful life of an asset shall be reviewed at least at each financial year-end and, if expectations differ from previous estimates, the change(s) shall be accounted for as a change in an accounting estimate in accordance with LKAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.

Impairment

To determine whether an item of property, plant and equipment is impaired, an entity applies LKAS 36 Impairment of Assets. That Standard explains how an entity reviews the carrying amount of its assets, how it determines the recoverable amount of an asset, and when it recognizes, or reverses the recognition of, an impairment loss.

De recognition

The carrying amount of an item of property, plant and equipment shall be de recognized:

a)on disposal; or

b)when no future economic benefits are expected from its use or disposal

The gain or loss arising from the de recognition of an item of property, plant and equipment shall be included in profit or loss when the item is derecognized (unless LKAS 17 requires otherwise on a sale and leaseback). Gains shall not be classified as revenue.

Disclosure

a) the measurement bases used for determining the gross carrying amount;
b) the depreciation methods used;
c) the useful lives or the depreciation rates used;
d) the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period; and
e) a reconciliation of the carrying amount at the beginning and end of the period showing:
    i. additions;
    ii. assets classified as held for sale or included in a disposal group classified as held for sale in accordance with SLFRS 5 and other disposals;
    iii. acquisitions through business combinations;
    iv. increases or decreases resulting from revaluations and from impairment losses recognized or reversed in other comprehensive income in accordance with LKAS 36;
    v. Impairment losses recognized in profit or loss in accordance with LKAS 36;
    vi. Impairment losses reversed in profit or loss in accordance with LKAS 36;
    vii. depreciation;
    viii. the net exchange differences arising on the translation of the financial statements from the functional currency into a different presentation currency, including the translation of a foreign operation into the presentation currency of the reporting entity; and
    ix. other changes.

The financial statements shall also disclose:

a) the existence and amounts of restrictions on title, and property, plant and equipment pledged as security for liabilities;
b) the amount of expenditures recognized in the carrying amount of an item of property, plant and equipment in the course of its construction;
c) the amount of contractual commitments for the acquisition of property, plant and equipment; and
d) if it is not disclosed separately in the statement of comprehensive income, the amount of compensation from third parties for items of property, plant and equipment that were impaired, lost or given up that is included in profit or loss.