

## Accounting for Assets – Property, Plant and Equipment

Identify the issues involved in the initial recognition and measurement of PPE and apply the relevant requirements of AASB 116

- PPE 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

### **Initial Recognition (AASB 116.7) and Measurement at Recognition (AASB 116.15-16)**

- Initially recognised at their cost of acquisition (historical cost)
  - As the economic benefits are 'consumed', the prepayment is recognised as an expense → depreciation expense & accumulated depreciation
  - Cost includes
    - Purchase price after deducting trade discounts and rebates
    - Any import duties and non-refundable purchase taxes
    - Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of performing its intended function AND
    - The initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located
- Assets comprised of identifiable components with different lives should be recognised as separate assets
- Journal entry
  - Debit – PPE
  - Credit – Cash/payables
  - (acquisition of PPE)

### **Depreciation (AASB 116.6&50&60)**

- Debit – depreciation expense
- Credit – accumulation depreciation
- (depreciation of PPE)

### **Derecognition (AASB 116.67-68)**

- Derecognition – removal of a previously recognised asset/liability from balance sheet
  - Occurs when an asset is disposed or when no future economic benefits are expected
- Derecognition requirements apply regardless of which model is used
- Recognised under profit/loss section (AASB 116.68)
  - Gain is not classified as revenue

Evaluate the role of revaluation in accounting for property, plant and equipment and apply the relevant requirements in AASB 116

- After being initially recognised, PPE must be measured using either the
  - Cost Model
  - Revaluation Model (AASB 116.29)
  - Note: these models differ in the carrying amount

- Consider the following when choosing between a cost and revaluation model
  - Relevance vs. reliability to users
  - Costs associated with revaluations
  - Effect on income statement (and management bonus plans)
  - Impact on debt/equity ratio
  - Public perception
- Once decided which model to use, all assets in the same class must be measured on the same basis (AASB 116.36)

### **Cost Model**

- Asset will be carried at the historical cost at all times
- i.e. Cost less any accumulated depreciation and/or accumulated impairment losses

### **Revaluation Model**

- Revalue the asset at the end of each period at its fair value
- Fair value – amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's-length transaction (AASB 116.6)
- If the fair value can be measured reliably
  - The asset shall be carried at a revalued amount
  - Revalued amount – fair value at date of revaluation less any subsequent accumulated depreciation and impairment losses (AASB 116.31)
- AASB 116 requires revaluations must be made with sufficient regularity so that the carrying amount does not differ materially from fair value at reporting date
- If you use the revaluation model, 1 of 2 things will happen
  - Increase in the carrying amount of an asset (revaluation increment)
    - Recognised in other comprehensive income (p/l) and accumulated in equity as a 'revaluation surplus' → increases equity
      - E.g. journal entry
        - Debit – asset
        - Credit – revaluation surplus
        - (to record the revaluation of asset)
      - If it reverses a previous revaluation decrement of the same asset previously recognised in the statement of comprehensive income, then it will be recognised in the p/l (AASB 116.39)
    - Decreases in the carrying amount of an asset (revaluation decrement)
      - Recognised in the statement of comprehensive income → ↓ profit
        - E.g. journal entry
          - Debit – revaluation expense
          - Credit – asset
          - (to record the revaluation of asset)
        - To the extent of any credit balance in the revaluation surplus relating to that asset the decrement shall be debited directly to the revaluation surplus (AASB 116.40)
    - Sale of a PPE asset under this model
      - Derecognition – revaluation surplus is transferred to retained earnings
      - Accumulated depreciation treatment

- Net method – accumulated depreciation of the asset to be revalued is closed to the asset account before revaluation
- Under the net method, we must close of accumulated depreciation first before dealing with any revaluation stuff