Fixed Assets Policy FA-1

Capitalisation Policy

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Version 2.0

Aurora Energy

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2 INTRODUCTION

2.1 The objective of this policy is to prescribe the accounting treatments for property, plant and equipment. This policy is set up in compliance with accounting standard AASB116- Property, Plant and Equipment and AASB 138 Intangible Assets.

2.2 This policy has been developed to specify the capitalisation criteria that expenditure needs to meet in order to qualify as capital and therefore be recognised in the carrying amount of an item of property, plant and equipment.

3 DEFINITIONS

3.1 For the purpose of this policy unless otherwise stated the definitions used within this policy are taken to be the same as in AASB Glossary of defined terms.

4 SCOPE

4.1 This policy shall apply to the accounting for cost incurred in the replacement, alteration, construction and purchase of plant, property and equipment by the Company.

4.2 This policy applies to both capital works (constructed assets) and purchased assets.

4.3 This policy should be read in conjunction with the policies referenced in Section 8.

5 POLICY STATEMENTS

Asset Recognition

5.1 The capitalisation threshold for expenditure on an asset is a value greater than $1,000, unless the asset is covered by the Attractive Assets Policy. All assets that meet this threshold are to be capitalised in accordance with AASB 116 and AASB 138.

5.2 An asset should be recognised in the statement of financial position when and only when:

a) It is probable that any future economic benefits associated with the item will flow to or from the entity; and

b) The asset has a cost or value that can be measured with reliability.

Asset Cost

5.3 The cost of an item of plant, property and equipment (purchased or constructed) comprises mainly:

- The purchase price;
- Import duties and non refundable taxes (i.e. GST is excluded from the cost);
- Initial delivery and handling cost (including freight);
- Cost of site preparation;
- Installation and assembly cost;
- Professional fees (e.g. design, architectural and engineering);
- Cost of testing to bring the asset into service (this should be net of any proceeds that may be generated from the testing process);
- Borrowing cost capitalised (see below);
- Direct material cost;
- Systematic allocation of direct labour and overheads attributable to bringing the asset to its working condition. The cost of an internally constructed asset should use the full absorption costing basis. As such overheads attributable to the costs of construction of the asset would be included in the capitalised cost.

5.4 In addition to the above, retirement/restoration cost should also be included in the cost of an item of property, plant and equipment to the extent it is recognised as a provision under AASB 137 Provisions, Contingent Liabilities and Contingent Assets. In brief, such cost should be significant, can be accurately measured, specific to the asset and is probable to occur at the end of the service life of the asset.

5.5 The following costs may not be capitalised as assets:

- Costs of relocating or reorganising an asset, or entity's operations;
- Costs of opening a new facility, or conducting a business in a new location (including the cost of staff training);
- Costs of introducing a new product, including advertising or promotional costs;
- Administration costs, and general overhead costs including (training, establishing policies and procedures, hiring and redundancy costs);
- Initial operating losses post commercial commissioning; and
- Repairs and maintenance of an asset. Repairs involve the day-to-day servicing and maintenance of an asset and ensure that it is maintained at its full productive capacity, and do not increase the previously estimated useful life. Refer section 6 and examples in Appendix 1.

Initial Spares

5.6 Spare parts and servicing equipment are usually carried as inventory and recognised in profit or loss as consumed. However, major spare parts and stand-by equipment (capital spares) qualify as property, plant and equipment when it is expected that they will be used for more than

one period. Similarly, if the spare parts and servicing equipment can be used only in connection with an item of property, plant and equipment, they are accounted for as property, plant and equipment.

Capitalised Interest

5.7 Borrowing costs, such as interest, is to be capitalised as part of the cost of the asset on all projects when the following conditions are satisfied:

i. The borrowing costs are attributable to the acquisition, construction or production of a qualifying asset as defined under AASB 123; and

ii. The project is funded from external borrowing not internal funds.

5.8 The capitalisation of borrowing costs, as part of the cost of a qualifying asset shall commence when:

i. Expenditure for the asset are being incurred;

ii. Borrowing costs are being incurred; and

iii. Activities that are necessary to prepare the asset for its intended use or sale are in progress.

5.9 Capitalisation of borrowing costs shall cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

5.10 Where funds are borrowed specifically for a project the amount can be determined by the actual borrowing costs, however where funds are borrowed generally and used for the purpose of obtaining qualifying assets, the rate of interest used as the capitalisation rate is to be equivalent to the weighted average borrowing costs of Aurora.

6 DISCUSSION OF POLICY STATEMENTS

Repairs v Refurbishment/ Replacement

6.1 One of the difficulties is determining whether expenditure on an asset is a repair or refurbishment.

6.2 The key difference is that repairs involve day-to-day maintenance of an asset, aimed at restoring the asset to its original working condition. Repairs do not extend the useful life or increase the future economic benefits of an asset. Examples include: regular maintenance checks, replacement of tyres and small parts.

6.3 Refurbishments or replacements are expenditure, which increase the estimated useful life of an asset, and provides significant increased future economic benefits through improved quality of output, increased capacity, improved efficiencies or economy of operation. Examples include a major overhaul, replacing the interior of a building, planned

replacement of major components of an asset to improve function, office fit-outs or refurbishments and system upgrades.

Cancelled Projects

6.4 If at any stage a project does not proceed, or it is deemed that the project will not provide any future economic benefits, as soon as the decision is made that the project has ceased, all the accumulated costs that relate to that project must be expensed to the business area responsible.

Work In Progress

6.5 Assets are set up as capital projects in the Navision system via capital jobs. These jobs sit in capital work in progress account until the completion of the job, at which time the cost will be capitalised to asset shells and form part of property plant and equipment on the Balance Sheet, and commence depreciating from this date.

Capital Works Job Review

6.6 Operating Business Units are to regularly review their capital jobs sitting in work in progress for completed jobs to ensure they continue to comply with the capitalisation policy, to write off expenditure no longer satisfying criteria for being carried as an asset and transfer completed jobs to asset shells.

Decommission/ Derecognising an Asset

6.7 The gain or loss arising from the decommission/derecognising of an asset should be included in profit and loss when the item is derecognised.

6.8 The decommissioning cost of an existing asset should not form part of the cost basis of a new asset created to replace it, except were the decommissioning costs are not material and are difficult to separately identify from the installation or construction costs of the new assets.

6.9 An example is the replacement of poles and equipment as a result of bushfires. The value associated with the remaining useful life of the assets, which have been replaced, is written off, and does not form part of cost base of the new assets to replace them. The asset which has been replaced must also be written out of the Regulated Asset Base (RAB), at the same time the new asset is introduced to the RAB, otherwise the RAB will be overstated.

Impairment of assets

6.10 At each reporting date Aurora is required to review the carrying amount of its assets, and determine whether an indication of impairment exists. This will be undertaken in line with AASB 136 and will be authorised by the CFO.

Intangible Assets

6.11 Where there is expenditure incurred in creating an internally generated intangible asset, it needs to be determined whether the expenditure meets the definition of research or development expenditure as defined in AASB 138 Intangible Assets.

6.12 Research expenditure is the original planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and shall be expensed to the income statement as incurred.

6.13 Development expenditure is the application of research findings to plan or design a product, process, systems or services before the start of commercial production or use. Any costs incurred during the development phase must be expensed unless it can be demonstrated that the criteria in AASB 138 are met.

6.14 All expenditure on research and development, regardless of whether capitalised or expensed needs to be identified for each project for taxation purposes.

7 PROCEDURAL ISSUES

Breach of Policy

7.1 Significant breaches of this policy will be reported to the Chief Financial Officer and Compliance Manager.

Periodic Review of this Policy

7.2 This Policy will be reviewed every two years unless circumstances change that require earlier review. The next review of this policy is scheduled for January 2013.

8 REFERENCES

- Fixed Assets Manual (Group Finance)
- Minor Fixed Stocktake Policy
- Attractive Asset Policy

APPENDIX 1 EXAMPLES OF CAPITAL AND OPERATING EXPENDITURE

Distribution Assets

Whether expenditure is capital or operating is determined by considering the facts in each case. The following examples are provided to assist with the application of this policy.

Note: Where there is a replacement of an asset, which forms part of our regulated asset base (RAB), the impact on RAB as part of the replacement must be considered to ensure that RAB is not overstated.

Unit of Property (UOP)	Expenditure	Capitalisation Criteria	Accounting Treatment
DISTRIBUTION ASSETS			
Feeder (overhead)	Repair a wooden pole as a consequence of car accident with either a wooden pole or a concrete pole as being the modern day equivalent	Repair	Operating
	Complete replacement of poles (eg due to car accidents, bush fires, or programmed)	Extend the life of the original asset Note: the asset, which has been replaced, must be written out of RAB, at same time as the new asset introduced to the RAB. Debit income statement with the remaining useful life value of asset that is replaced.	Capital
	Replacing conductor for all HV and LV feeders	Increase in capacity	Capital

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Note: Where there is a replacement of an asset, which forms part of our regulated asset base (RAB), the impact on RAB as part of the replacement must be considered to ensure that RAB is not overstated.

Unit of Property (UOP)	Expenditure	Capitalisation Criteria	Accounting Treatment
DISTRIBUTION ASSETS			
	over 2 spans with larger conductor to increase capacity		
	Programmed replacement HV and LV conductors that have reached the end of their serviceable life	Extend the life of the original asset	Capital
	Repairing a transformer (eg. rewiring as part of maintenance program)	Repair	Operating
	All additions and extensions to overhead HV and LV feeders over 2 spans including switchyards	Creates a new asset	Capital
	Installing larger capacity transformer and associated equipment	Increase in capacity	Capital
	Installing additional transformer and associated equipment, reclosers, sectionalisers and air break isolators	Creates a new asset	Capital

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Note: Where there is a replacement of an asset, which forms part of our regulated asset base (RAB), the impact on RAB as part of the replacement must be considered to ensure that RAB is not overstated.

Unit of Property (UOP)	Expenditure	Capitalisation Criteria	Accounting Treatment
DISTRIBUTION ASSETS			
Feeders (Underground)	Installing additional HV and LV underground cables, including fittings	Creates a new asset	Capital
	Installing HV and LV underground cable to replace overhead line	Creates a new asset	Capital
Substations	To upgrade an existing earthmat due to meet safety requirements	Additional functionality	Capital
	Installing new substation, including HV and LV switchgear, transformers and enclosure	Creates a new asset	Capital

Meter Assets

METER ASSETS	Expenditure	Capitalisation Criteria	Accounting Treatment
Domestic Residential Meters	Cost of meter and Installation to customer's residence	Creates a new grouped asset	Capital
Demand Meters	Cost of meter and Installation to customer's residence	Creates a new grouped asset	Capital
Domestic Electronic LV Meter (Intelligent metering system)	Cost of meter and Installation to business and key customer's premises	Creates a new grouped asset	Capital
Polyphase 3 phase HV Meter (Intelligent metering system)	Cost of meter and Installation to business and key customer's premises	Creates a new grouped asset	Capital
Prepayment LV Meter (domestic)	Cost of meter and Installation to customer's residence	Creates a new grouped asset	Capital

Other Assets

OTHER ASSETS	**Expenditure**	**Capitalisation Criteria**	**Accounting Treatment**
Minor Corporate Application Systems	Increases in the functionality of a computer system for example, improving the quality of output, speed or security	Additional functionality	Capital
Major IT Projects	Installing new systems eg BIRT reporting/ upgrades and enhancements to current systems eg WASP, Frontline/ Navision.	Searching for possible alternative products/ services.	Operating
		All costs incurred prior to obtaining project approval	Operating
		All costs incurred in the development and implementation phases, including project management.	Capital
		Where it becomes evident that it is not probable future economic benefits will eventuate from project	Operating
Facilities/Property	Refurbishments/ office fit-outs eg workstations/ refurbishment to café area	Creates an asset with separate useful life or increases future economic benefits of existing asset.	Capital
	Upgrades to various Depot locations i.e. truck wash, vehicle shelters/ toilet upgrades etc	Where major works are carried out, which extend useful life, improve functionality or create a new asset	Capital