Capitalisation Policy

January 2023

Version 4.0

Contents

1. Policy Overview

Capitalisation is the application of accounting rules to determine whether business expenditure is to be treated as an asset or expensed. TasNetworks recognises that a failure to comply with the Australian Accounting Standards can have significant adverse impacts on its reputation and its shareholders.

2. Who does this Policy apply to?

This policy applies to all costs incurred in the replacement, alteration, construction and purchase of property, plant and equipment (refer section 6) and intangible assets (refer section 7). The policy applies to both constructed and purchased assets.

3. The Purpose

The purpose of this document is to ensure that capital expenditure (Capex) is accounted for in a logical and cost-effective manner which is compliant with relevant Australian Accounting Standards. This policy is to provide staff involved in budgeting and expenditure decisions guidance when classifying expenditure in the TasNetworks financial system. It establishes the capitalisation criteria at the point of recognition of an asset.

4. Asset Recognition

Accounting standards distinguish between expenditure that is consumed immediately in operations (or within one financial year) and expenditure on assets that will provide service over more than one financial year. The recording of expenditure as an asset means that it is recorded in the TasNetworks balance sheet asset registers. Such expenditure on assets is referred to as capital expenditure, and the process of transferring assets to the asset register is referred to as capitalisation.

Where applicable, the capital expenditure that is capitalised in the fixed asset register will also be included in the Transmission or Distribution Regulatory Asset Bases (RAB) which impacts TasNetworks Regulatory asset values and future revenue streams.

These processes are subject to reviews by TasNetworks external auditors.

The minimum capitalisation threshold is $500, this is applied to the combined components that make up the identifiable unit of property. All expenditure above the threshold shall be capitalised when recording the asset.

Attractive assets that are less than $500 are also capitalised. Items that are considered to be an attractive asset and less than $500 are also capitalised in the asset register. All other expenditure shall be expensed.

As per Australian Accounting Standards, an asset should be recognised in the statement of financial position when:

- It is probable that any future economic benefits associated with the item will flow to or from the entity beyond the year it was acquired; and
- The asset has a cost or value that can be measured with reliability.

5. Commencement of Capitalisation of Costs

Capitalisation will usually commence once:

- the asset to be capitalised has been identified and approval has been obtained to build or purchase the asset; and
- there is reasonable certainty of the project going ahead and economic benefits being realised.

When there are several choices or options being considered as to which asset to invest in, capitalisation will commence from when the high level functional requirement of the project has been scoped and a preferred solution has been decided that establishes a line of sight to the eventual asset. Expenditure incurred up to that point is not to be capitalised as part of the asset.

TasNetworks Gated Investment Framework provides guidance on the process the business uses to determine when this point in time occurs for investment activities and either aligns to Decision Gate 2 (preferred option approval) or Decision Gate 3 (financial approval)

6. Capitalisation of Property, Plant and Equipment

The following expenditure incurred in the purchase or construction of an item of property, plant and equipment **are normally capitalised** as part of an asset.

- The purchase price;
- Import duties and non-refundable taxes (GST is excluded from the costs);
- Initial delivery and handling costs (including freight);
- Cost of site preparation;
- Installation and assembly costs;
- Professional fees (e.g. design, architectural and engineering);
- Cost of testing to bring the asset into service;
- Direct material costs;
- Direct labour attributable to bringing the asset to its working condition;

- The CAM (Cost Allocation Methodology) which applies overhead costs attributable to bringing the asset to its working condition; and
- Restoration costs should be included in the cost of the asset to the extent it is recognised as a provision under AASB 137 Provisions, Contingent Liabilities and Contingent Assets. Such costs should be significant, easily measured, specific to the asset and probable to occur at the end of the service life of the asset.

Labour costs should only be capitalised when an employee is dedicated to work on a project and the allocation of time (whether full time or on a pro-rata basis) has been agreed to by the project manager. Resources provided to support a project on an adhoc basis from a business as usual perspective should not be costed to the project.

When an employee's has been seconded to a project and that position has been backfilled, the cost of backfilling that position is treated as business as usual expenditure and should not be costed to the project.

The following costs **should not be capitalised** as part of an asset:

- Expenses incurred in decommissioning an existing asset should not form part of the cost of a new asset, unless it forms an integral part of the site preparation costs required to install an asset at the same location;
- Costs of day-to-day servicing including labour and consumables, which may include the cost of small parts. This is often described as repairs and maintenance, see 6.2 below;
- Costs involved in the process of determining which asset to construct or purchase up to the point when the preferred option is decided;
- Costs of relocating or reorganising an asset or operation;
- Administration costs including establishing policies and procedures, hiring and redundancy costs, meal entertainment, celebration events and work related clothing; and
- Costs of abnormal amounts of wasted material, labour, or other resources incurred in constructing an asset.

6.1. Capitalisation of Purchased assets

Purchased assets (e.g. Motor Vehicle, Personal Computer) are capitalised when the assets are received and ownership has transferred to TasNetworks. These assets are capable of being used when received.

6.2. Capitalisation of Initial Spares

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 (strategic spares) qualify as property, plant and equipment and are capitalised when the assets are received and ownership has transferred to TasNetworks.

7. Capitalisation of Intangible Assets (Software)

A separate Accounting Standard applies to the capitalisation of Intangible Assets, AASB 138 Intangible Assets.

For expenditure on a project relating to software development to be capitalised, the project must be able to satisfy ONE of the following criteria:

- Creating or using a new module of a software product; or
- Amending an existing module of a software product and creating additional or significantly improved functionality; or
- Development of a substantive model that will be used on a repeatable basis in future years (with a future benefit of greater than 1 year) and usually where the software used is not part of the Standard Operating Environment (SOE). Examples include data modelling or conversion tools. This includes the effort to develop or purchase data models to support significant data conversion and load activities, but not the on-going maintenance of the models.

Given the inherent nature of these types of projects, the accounting treatment of software development activities will be considered on a case-by-case scenario prior to the project commencing and will be assessed based upon the nature of the activity and tasks.

The portion of software licenses that represents the cost of ongoing upgrades to hardware and software products is to be capitalised.

In a cloud- based software arrangement the right to access hardware or software does not generally result in any title transfer or licence being granted. The cost of a cloud software license agreement can only be capitalised if the following principles are met:

- TasNetworks has the contractual right to take possession of the software at any time during the hosting period without significant penalty; **and**
- It is feasible for TasNetworks to run the software on our own hardware or another party unrelated to the current host vendor.

Where there is expenditure incurred in creating an internally generated intangible asset **(e.g. software),** it needs to be determined whether the expenditure meets the definition of research or development expenditure as defined in AASB 138 Intangible Assets. Research expenditure is not able to be capitalised. This includes the majority of expenditure prior to the initiation phase of a project. Expenditure incurred in creating a new asset is deemed to be development phase expenditure (compared with expenditure incurred in making the decision to create an asset, which is research expenditure). Any costs incurred prior to the point of the approval of the preferred function option are operational in nature.

Once it has been identified that a capital project exists, the Intangibles Capitalisation Guide will assist in applying the correct treatment of expenditure for the asset/ project.

8. Expenses incurred post commissioning (Repairs v Replacement / Refurbishment)

Once an asset has been capitalised, it may in time incur further expenses. These are typically either a repair or refurbishment/replacement. This distinction is important as replacement or refurbishment expenditure is capitalised, whereas repair expenditure is not.

A repair is expenditure required to address the day-to-day wear and tear of an asset, aimed at maintaining the asset to perform its functional operation. Repairs are not intended to substantially extend the useful life or increase the future economic benefit of an asset.

Refurbishment or replacement is expenditure that increases the estimated useful life of an asset, usually through increased capacity, improved efficiencies or economy of operations or significant increase future economic benefits.

9. Project Cancellation

In the event of a project being cancelled at any point prior to completion, all expenditure on that project will immediately be expensed. Rejection of a business case might suggest a project has been cancelled, however if the business case is re-submitted, then only that portion of the expenditure relating exclusively to the previous submission (if any) will be expensed. Expenditure attributable to the successful business case may be capitalised.

10. Capital Work in Progress Reviews

Capital projects often take time to finish however require completion to ascertained the final cost and allow for depreciation to begin. Works still in progress are regularly reviewed to ensure that they still comply with this capitalisation policy. Where expenditure no longer satisfies the criteria for being carried as an asset, is to be expensed.

11. Roles and responsibilities

11.1. Executive Finance, Finance

The Executive Finance, Finance is responsible for approving this Policy.

11.2. Head of Finance

The Head of Finance is responsible for:

- Maintenance of this policy;
- Ensuring the establishment of relevant procedures, processes and electronic systems which enable TasNetworks to meet its obligations; and
- Managing compliance with this policy.

11.3. Financial Accounting and Tax Team

The Financial Accounting, Treasury and Tax Team are responsible for:

- Developing and documenting relevant procedures and processes which assist TasNetworks to meets its obligations in a timely and accurate manner;
- Ensuring that management is adequately informed about its obligations so that they can appropriately address any significant issues in their day-to-day business decisions.
- The day-to-day application of this policy and administration of capitalisation matters across all areas of financial management;
- The maintenance of asset registers;
- Maintaining up-to-date skills by annual attendance at relevant training courses and updates; and
- Assisting with the development of this policy and enforcing day-to-day compliance.

11.4. Leaders, team members and contractors

Line managers, employees and contractors acting as TasNetworks agents are responsible for:

- Adherence to any directions and/or guidance relating to capitalisation matters as are deemed necessary for the effective and efficient operations of TasNetworks; and
- Adhering to this policy.

All TasNetworks **Leaders** and **Team Members** have a responsibility for advancing the Capitalisation Policy under these existing policies and principles.

12.References

Australian Accounting Standards – www.aasb.gov.au

13.Compliance

Breaches of this policy will be treated seriously and may if necessary result in disciplinary action being undertaken. Depending on the circumstances of the case, this may include an apology, counselling, training, demotion or termination of employment. Behaviour that is not a breach of this Policy may still be found to be inappropriate or unreasonable. For example, it may be a breach of the TasNetworks Code of Conduct. In this instance, disciplinary action may still result.

Public Interest Disclosure Statement ("Whistle blowers")

If an individual is concerned about consequences associated with reporting a serious breach of this Policy, that individual should refer to the Public Interest Disclosure (Whistle blowers) Policy available on The Zone or talk to their Leader.

14.Need to know more or have a question?

All Team Members will have access to (this policy) on The Zone. Support and further information is available from your Finance Business Partner or Financial Accounting and Taxation Team.

15.Administration of this Policy

This policy is administered by Head of Finance and will be reviewed on a biennial basis and updated where applicable.

Authorisations		
Action	**Name**	**Date**
Prepared by		
Reviewed by		
Authorised by		

Document control		
Date	**Version**	**Description**
September 2015	1.0	Issued to AER
May 2016	2.0	Issued to AER
February 2020	3.0	New format
January 2023	4.0	Update Group Structures, minor wording. Issued to AER

16.Glossary

Asset	A future economic benefit controlled by the entity as a result of a past transaction or other past event. All combined components that create a single asset are recognised by TasNetworks at the lowest unit of property.
Acquired Assets	Those assets which are purchased from an external supplier, including those installed by TasNetworks employees. The primary difference between acquired and constructed assets is the scope of work required for the asset to be ready for use. Contrast the purchase of new corporate IT infrastructure (an acquisition) with the construction of a new transmission line (construction).
Carrying amount	The value of an asset under Australian Accounting Standards.
Constructed Assets	Those assets which are internally generated by TasNetworks. Compared with Acquired Assets, Constructed Assets may include the cost of materials, but the asset's value is generated through its construction
Development	The application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.
General Assets	Those assets held by TasNetworks which are not energised as part of the transmission network (generally Minor Assets, but also Land and non-substation Buildings).
Impairment	Accounting recognition that an asset's carrying amount has decreased to a greater degree than that allowed for by depreciation (e.g. as a result of change in market conditions).
Intangible Assets (or Intangibles):	General, non-physical assets (e.g. computer software).
Minor assets	General, portable assets (e.g. motor vehicles and computers).
Research	Original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.
Software	The programs used to direct the operation of a computer, as well as documentation giving instructions on how to use them.
Attractive Assets	Are generally non consumable items that are susceptible to theft or loss due to their portable nature and attractiveness to personal use or resale. E.g. Laptop computers, mobile phones, digital cameras, motion tablets, etc.