

CAPITALISATION AND DEPRECIATION POLICY

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Drafted by	J Rakadrudru	Approved by Board on	
Responsible person	M Usumaki	Scheduled review date	31/01/2020

Summary

All assets meeting the definition of a fixed asset shall be considered a long-term asset and shall be recorded in the Church's Fixed Assets Register (FAR). Harbour City Harvest Church (the church) and its related entities are responsible to account for all long-term assets under its jurisdiction. Such assets shall be systematically and accurately recorded; properly classified; and adequately documented in the FAR. All entities shall establish an internal control structure over fixed assets that provides reasonable assurance of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations.

Asset Valuation

Fixed assets shall be recorded at historic cost or, if the cost is not readily determined, at estimated historic costs. Cost shall include applicable ancillary costs. All costs shall be documented, including methods and sources used to establish any estimated costs. In the case of gifts, the fixed asset should be recorded at fair market value at the date of receipt.

1. Purchased Assets – The recording of purchased assets shall be made on the basis of actual costs, including all ancillary costs, based on vendor invoice or other supporting documentation.
2. Constructed Assets – All direct costs (including labour) associated with the construction project shall be included in establishing the asset valuation.
3. Donated Assets – Fixed assets acquired by gift, donation, or payment of a nominal sum not reflective of the asset's market value shall be assigned cost equal to the fair market value at the time of receipt.

Asset Salvage Value

The salvage value of an asset is the value it is expected to have when it is no longer useful for its intended purpose. In other words, the salvage value is the amount for which the asset could be sold at the end of its useful life. This value can be based on (1) general guidelines from some professional organizations such as AASB, (2) internal experience, or (3) professionals such as engineers, architects, programmers, etc.

Asset Classification

Fixed assets should be categorized into the following:

- Land
- Land improvements and infrastructure
- Buildings/Facilities
- Equipment, library books, and artwork
- Works in Progress (WIP)
- Intangible Assets (IP)

General Policy for Capitalisation

Fixed assets should be capitalised as follows:

- All land acquisitions
- All buildings/facilities acquisitions and new construction
- Facility renovation and improvement projects costing more than \$10,000
- Land improvement and infrastructure projects costing more than \$10,000
- Equipment costing more than \$1,000 with a useful life beyond a single reporting period (generally one year)
- Purchases of equipment and facilities acquired through a debt financing arrangement meeting the capital lease criteria under AAS-17 Leases (AASB) should be considered for capitalisation. In general, for equipment, any such lease arrangement in excess of \$1,000 regardless of whether individual items under lease arrangement do not qualify as a fixed asset based on the \$1,000 threshold.
- Capitalised interest incurred on new construction, rehabilitation or improvement projects costing in excess of \$10,000
- Computer software costing more than \$1,000 with a useful life beyond a single reporting period
- Intangible assets of internally generated computer software and all other intangible assets costing more than \$100,000
- All library books and artwork
- Works in Progress (WIP) for capital projects with a budget in excess of \$20,000

Land Acquisitions

The recorded cost of land includes (1) the contract price; (2) the costs of closing the transaction and obtaining title, including commissions, options, legal fees, title search, insurance, and past due taxes; (3) the costs of surveys; and (4) the cost of preparing the land for its particular use such as clearing and grading. If the land is purchased for the purpose of constructing a building, all costs incurred up to the excavation for the new building should be considered land costs. Removal of an old building, clearing, grading and filling are considered land costs because they are necessary to get the land in condition for its intended purpose. Any proceeds obtained in the process of getting the land ready for its intended use, such as salvage receipts on the demolition of the old building or the sale of

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cleared timber, are treated as reductions in the price of the land. Capitalisation of land costs include, but are not limited to, the following:

- Original contract price
- Brokers' commissions
- Legal fees for examining and recording title
- Cost of title guarantee insurance policies
- Cost of real estate surveys
- Cost of an option when it is exercised
- Special paving assessments
- Cost of excavation, grading or filling of land and razing of an old building
- Cost of cancellation of unexpired lease
- Payment of noncurrent taxes accrued on the land at date of purchase, if payable by purchaser

Buildings & Facilities

Capitalisation of facilities costs include, but are not limited to, the following:

- Original contract price of asset acquired or cost of design and construction
- Expenses incurred in remodelling, reconditioning, or altering a purchased building to make it available for the purpose for which it was acquired.
- Expenses incurred for the preparation of plans, specifications, blueprints, etc.
- Cost of building permits
- Payment of noncurrent taxes accrued on the building at date of purchase, if payable by purchaser
- Architects' and engineers' fees for design and supervision
- Costs of temporary facilities used during the construction period

Each building or addition of square meters to an existing building acquired or constructed is divided into 10 major building components. The components are as follows:

1. General construction
2. Site preparation (this component is classified as land on the financial statements)
3. Roof and drainage
4. Interior construction
5. Plumbing
6. Heating, ventilation, and air conditioning
7. Electrical
8. Fire protection
9. Elevators
10. Miscellaneous

The total cost of the building or additional square meters is then allocated among the 10 major building components. Projects such as building construction included in the fixed asset value of the building, the cost of professional fees (architect and engineering), permits and other expenditures necessary to place the asset in its intended location and condition for use should be capitalised.

Furthermore, the cost of interest incurred during building construction should be capitalised as described below under capitalised interest costs.

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Building Renovations

A building renovation is defined as enhancements made to a previously existing building component. Any renovation to a building must at a minimum meet the following criteria to qualify as a fixed asset:

1. The total project cost must be more than \$10,000
2. The renovation must extend the useful life or productive capacity of the asset

Building Improvements

An improvement to a building is defined as adding a new component where one did not previously exist. The improvement must cost more than \$10,000 and have an initial useful life extending beyond a single reporting period (generally one-year).

Land Improvements and Infrastructure

Land improvements include items such as excavation, non-infrastructure utility installation, driveways, sidewalks, parking lots, flagpoles, retaining walls, fencing, outdoor lighting, and other non-building improvements intended to make the land ready for its intended purpose. Land improvements can be further categorized as non-exhaustible and exhaustible. Expenditures for land improvements that do not deteriorate with use or passage of time are additions to the cost of land and are generally not exhaustible, and therefore not depreciable.

Infrastructure assets are defined as long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets. Examples of infrastructure assets include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems.

Improvements to infrastructure or land improvements which extend the useful life or capacity of the asset and meet capitalisation thresholds will be capitalised as a separate asset/component and depreciated over its estimated useful life

Equipment

- Equipment qualifying as a capital asset is defined as a single item with an acquisition cost of \$1,000 or more and has a useful life beyond one year. Capitalisation of equipment costs include but are not limited to, the following:
 - Original contract or invoice cost
 - Freight, import duties, handling and storage costs
 - Specific in-transit insurance charges
 - Sales, use and other taxes imposed on the purchase
 - Costs of preparation of foundations and other costs in connection with making a proper site for the assets
 - Installation charges
 - Costs for reconditioning used equipment to make it usable for the purpose it was purchased

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Improvements to existing equipment assets which extend the useful life or capacity of the asset and meet capitalisation thresholds will be capitalised as a separate asset/component and depreciated over its estimated useful life.

Leased Equipment and Facilities

Leased equipment and facilities should be capitalised if the lease agreement meets any one of the four criteria below. Also, a contractual lease obligation for a facility, that at its inception, meets any of the following four criteria, should be capitalised:

- The lease is a non-cancellable lease
- The lease transfer ownership of the property to the Church by the end of the lease term.
- The lease contains a bargain purchase option.
- The lease term is equal to 75 percent or more of the estimated economic life of the leased property.
- The present value of the lease payments at the inception of the lease, excluding executory costs, equals at least 90 percent of the fair value of the leased property.

Leases that do not meet any of the above requirements should be recorded as an operating lease.

Capitalised Interest Costs:

The Church will capitalise interest costs based on the criteria outlined in AASB-123 Borrowing Costs. The objective of capitalising interest is to obtain a measure of the acquisition cost that more closely reflects the Church's total investment in the asset.

The amount of interest capitalised should theoretically be the amount of interest charged during the assets acquisition period that could have been avoided if the assets had not been acquired, or had not been acquired without incurring debt. As required under AASB 123 (12) involving borrowings, interest costs will be offset by interest income. As such, the amount of interest cost capitalised is all interest cost of the borrowing less any interest earned on related interest-bearing investments acquired with proceeds of the related borrowing from the date of the borrowing until the assets are ready for their intended use.

The capitalisation period begins when the following three considerations are present:

- Expenditures for the capital asset have been made.
- Activities necessary to get the capital asset ready for its intended use are in progress.
- Interest costs are being incurred.

The amount capitalised should be an allocation of the net interest cost incurred during the period required to complete the asset. The interest rate for capitalisation purposes is to be based on the rates on the Church's outstanding borrowings. If a specific new borrowing can be identified with the asset, the rate on that borrowing should be used as the basis for allocating the interest cost for the asset. A weighted average of the rates on other borrowings is to be applied to expenditures not covered by specific new borrowings.

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Computer Software

Purchased computer software costing more than \$1,000 with a useful life beyond a single reporting period (generally one-year) should be capitalised.

Intangible Assets

Intangible assets are those that lack physical substance, are non-financial in nature and have an initial useful life extending beyond a single reporting period. Intangible assets must be identifiable, meaning they are either capable of being separated by means of sale, transfer, license or rent, or they arise from contractual or other legal rights.

Intangible assets acquired or developed by the Church could include licensed software, internally generated computer software and church owned websites or portals. Other examples include patents, copyrights and trademarks, permits and licenses, easements, and land use rights (e.g., water, timber or mineral rights).

The value of certain intangible assets, such as land use rights or easements, may already be included in the reported value of the associated real property asset. In these instances, although the individual rights associated with the property are separable and intangible in nature, collectively they represent the ownership of a tangible asset. Therefore, the value of the individual rights should remain aggregated and reported as a tangible capital asset, not separately as an intangible asset (i.e., easements on Church/Other Party owned land should not be reported separately, but be included in the reported land value).

Current policy requires purchased computer software costing greater than \$1,000 to be capitalised by the Church (i.e., entered in the Fixed Assets Register). The additional recognition requirements for intangible assets apply to internally generated computer software. In this regard, the activities involved in creating (and/or significantly modifying commercially available) software need to be evaluated to determine if the internal costs meet the criteria for capitalisation.

The software must be acquired, internally developed, or modified solely to meet internal needs and there must not be a substantive plan to market the software externally to other organizations. Software development generally involves three phases. These phases and their characteristics are as follows:

- Preliminary project phase - when conceptual formulation of alternatives, the evaluation of alternatives, determination of existence of needed technologies and final selection of alternatives is made.
- Application development phase - Design of chosen path including software configuration and software interfaces, coding, installation of computer hardware and testing, including parallel processing phase.
- Post-implementation/operation phase - training and application maintenance activities.

Costs associated with the preliminary project and the post-implementation/operating phases should be expensed as incurred. Internal and external costs associated with the application development phase should be capitalised. Costs to develop or obtain software that allows for access or conversion of old data by new information systems should also be capitalised. Costs incurred during the application development phase should be capitalised as an in progress asset until the software is

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placed in service. When the project is completed, the asset should be reclassified as an intangible asset and should be capitalised and depreciated. General and administrative costs and overhead expenditures associated with software development should not be capitalised as costs of internal use software.

Upgrades and enhancements are defined as modifications to existing internal-use software that result in the ability for the software to perform tasks that it was previously incapable of performing. In order for costs of specified updates and enhancements to internal-use computer software to be capitalised, it must be probable that those expenditures will result in additional functionality, increased efficiency, or the extension of the estimated useful life. If the modification does not result in any of these outcomes, the costs should be considered routine maintenance and be expensed as incurred.

Library Books

Purchased library books should be recorded at cost. Generally, library books acquired by contribution would be recorded at fair market value. The Church uses a “layered” depreciation procedure for library books, where an annual layer for books/volumes purchased/donated is maintained. Although not maintained in the fixed asset accounting system, the useful life of library books, reference materials and information sources other than library books will be 10 years. As such, a 10 percent charge would be applied to gross / historical cost balance of each layer (year). When books are disposed of, no gain or loss would be recognized, even if cash were received. The disposal will be recorded as a reduction of the gross library book value and the related accumulated depreciation balance.

Additions in the current year will be grouped by a layer and the total gross asset value would be depreciated over the established average useful life (10 years in this example). In the initial year of library book additions, the Church will take one-half year worth as a depreciation charge.

Example:

Assume the Church purchased \$20,000,000 in library books during the year. The entry to record depreciation on that layer only ($\$20,000,000/10 \times 1/2$) would be:

Depreciation Expense -Library Books 1,000,000

Accumulated Depreciation-Library Books 1,000,000

Works in Progress (WIP)

A WIP asset reflects the cost of construction work undertaken, but not yet completed. For work in progress assets, no depreciation is recorded until the asset is placed in service. When construction is completed, the asset should be reclassified as building, building improvement, or land improvement and should be capitalised and depreciated.

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Depreciation

Depreciation is the process of allocating the cost of tangible property over a period of time, rather than deducting the cost as an expense in the year of acquisition. Generally, at the end of an asset's life, the sum of the amounts charged for depreciation in each accounting period will equal original cost less the salvage value.

Information Needed to Calculate Depreciation

To calculate depreciation on a fixed asset, the following five factors must be known:

- the date the asset was placed in service
- the asset's cost or acquisition value
- the asset's salvage value
- the asset's estimated useful life, and
- the depreciation method.

Estimated Useful Life

Estimated useful life means the estimated number of months or years that an asset will be able to be used for the purpose for which it was acquired. Eligible fixed assets should be depreciated over their estimated useful lives. The Church has established a table of useful lives that is reflected in the FAR. When an asset is added to the system, depending upon the sub-category of fixed assets selected, a corresponding estimated useful life would be assigned.

Depreciation Method

The Church has adopted the straight-line method for depreciating all fixed assets. Depreciation will begin in the month the asset is placed in service with the exception of library books. Under the straight-line depreciation method, the cost of the asset is written off evenly over the useful life of the asset. The amount of annual depreciation is determined by dividing an asset's cost reduced by the salvage value, if any, by its estimated life. The total amount depreciated can never exceed the asset's historic cost less salvage value. At the end of the asset's estimated life, the salvage value will remain.

Library books will be depreciated using the straight-line method based on the half-year convention. Under the half-year convention, library books purchased during the fiscal year will be treated as though they were placed in service on the first day of the seventh month of the fiscal year. One-half of a full year's depreciation will be taken for the library books in the first year they were placed in service.

HCHC FAR Useful Life Schedule

The Asset Type Code is an identifier used in the FAR to properly classify the asset or asset component.

Building and Building Components:

Asset Type Code	Description	Useful Life (in years)
0	General Construction	50
1	Site Preparation	Unlimited*
2	Roof	25
3	Interior Construction	30
4	Plumbing	30
5	HVAC	30
6	Electrical	30
7	Fire Protection	25
8	Elevators	25
9	Miscellaneous	25
10	Land Improvements and Infrastructure	20

Environmental removal costs – Qualifying costs not included as a component listed above, will be identified as a separate component and depreciated using a 30-year life.

* - Classified as Land

Capital Equipment, Furniture, Fixtures, etc.:

Asset Type Code	Description	Useful Life (in years)
11	Food Service	10
12	Auto/Vehicle	6
13	Furniture	6
14	General Office Equipment	5
15	Printing & Related	5
16	Electronic Data Processing	5
17	Telecomm Equipment	5
18	Audio/Visual	7
19	Music Instr/Equipment	7
20	Library Book and Reference Materials	10

Asset Disposal

Retiring an entire asset or building component – remove the entire asset and related accumulated depreciation from the fixed asset file. Any undepreciated balance will be reported as a disposal expense, net of any value received.

Authorisation

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Chairman

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Date