

ACCOUNTING STANDARD AASB 116

DEFINITION OF RESIDUAL VALUE

Submission by

**DG & AB MAXWELL
Consulting Accountants**



INTRODUCTION

AASB 116 *Property, Plant and Equipment* paragraph 6 contains the following definition of *the residual value* of an asset:

"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. "

THE ISSUE

In some instances this is being interpreted as requiring a cash receipt of the proceeds of sale (or deduction from a cash payment made for the acquisition of the replacement asset as with an item traded-on).

This submission argues that for certain not-for-profit entities (specifically for local governments) such an interpretation is unduly limiting and, we would suggest, does not reflect the intention of the Standard. We suggest that the strict interpretation is in fact reading the Standard more closely than it is intended to be read.

The following simple example illustrates our point.

Example

An open surface road was constructed on the natural surface on level ground. The wearing surface construction (sheeting) was of 200 mm thick crushed gravel of 8 metre width for a 1 kilometre length. (The 1600 cubic metres of gravel required for the construction was carted from a nearby pit, and graded, compacted and rolled on site.)

The wearing surface is now in poor condition, has reached the end of its useful life and the road will be re-surfaced. (The road is seriously pot-holed and is showing the natural ground surface, particularly in the "channels" where vehicles tend to track, and many of the pot-holes have joined up. Despite this, there is a certain amounts of the previous sheeting remaining in the areas where pot-holes have not developed.)

In the process of reconstructing the wearing surface, the remnant sheeting from the original construction was graded up and mixed with additional gravel from the nearby pit, and graded, compacted and rolled as in the original construction.

The new wearing surface is in all respects identical to the original wearing surface when that was originally completed.

However, due to the salvaged materials from the original wearing surface, it was only necessary to cart 1050 cubic metres of new gravel from the nearby pit.

We contend that the residual value of the original wearing surface is the cost saving realised (or expected to be realised) from the re-use of salvaged materials, less the cost of salvage.

In our example, this would be the cost of carting 550 cubic metres of new gravel from the pit, less the cost of grading up the salvaged material.



There are many other common examples in a local government environment:

- Previous road seal materials mixed with the pre-existing road base, graded, compacted and rolled prior to a new bitumen seal being applied.
- The replacement of a timber bridge with a concrete span, retaining and re-using the old bridge abutments.
- Re-use of "soft-fall" surface materials and other components in the re-design and refurbishment of playgrounds, parks, etc.
- A 150 mm cast iron gas pipe becomes porous resulting in leakage throughout its length. A 100 mm flexible pipe is threaded through and service connections transferred from the old pipe to the new, avoiding re-trenching and relaying of the supply pipe throughout its length, which would be a much more expensive exercise.

RECOMMENDATION

We recommend that an additional "Aus" paragraph be added applicable to not-for-profit entities to the effect that where an asset is replaced, cost savings arising from the salvage and re-use of materials in the construction of the replacement, net of costs of salvage, form part of the residual value.

