

Component:	Assets / Property plant and equipment (IAS 16)
Short title:	Major replacements/ overhauls to components of plant and equipment such as "pot lining"

### Issue

It is common in the metals industry that major components of some items of property, plant and equipment are replaced or subject to major overhauls at regular intervals. For example, the "lining" of an aluminium smelter's kiln is typically replaced every four years or so. The rest of the fixed asset last considerably longer. How should this expenditure be accounted for?

### Solution

Components, such as pot lining, are accounted for as separate assets because they have useful lives different from those of the larger items of plant and equipment of which they are a part. The expenditure incurred in replacing or renewing the component is accounted for as the acquisition of a separate, new asset and the replaced asset is written off according to IAS 16 R.27.

The costs of a major inspection or overhaul should be expensed as incurred except if:

- a) the components which are being replaced or restored have already been previously identified and depreciated so as to reflect the consumption of the economic benefits provided by them;
- b) it is probable that future economic benefits will flow from the asset being inspected or overhauled; and
- c) the cost of the major inspection or overhaul can be measured reliably.

Therefore, if these three criteria are met, the expenditures should be capitalised as a component of the asset.

Management should identify the components of plant and equipment (such as pot lining) that will need a major overhaul and replacement at the time of acquisition of the asset. These components are recognised as separate assets. The initial cost of the equipment should be apportioned between these components and the remainder of the asset. The components subject to overhaul and replacement should be depreciated over the period to the next overhaul. The remainder of the cost of the equipment is depreciated to its residual value over the full useful life.