

Component:	Assets / Property plant and equipment (IAS 16) and Expenses (IAS 16)
Short title:	Accounting for expenditures after the initial commissioning of an asset – expense vs. capitalise

Issue

It is common in the metals industry for companies to have complex capital projects involving long installation processes with modifications and improvements continuing after the initial commissioning and use of the asset. The issue is whether the subsequent expenditures should be capitalised or expensed.

Solution

IAS 16 R.16 requires that the cost of an item of property, plant and equipment should include the directly attributable costs of bringing the asset to working condition for its intended use.

Subsequent expenditures may be recognised in the carrying amount of a fixed asset if they meet certain recognition criteria [IAS 16 R.12-14]. The cost of an item of property, plant and equipment is recognised as an asset if it is probable that future economic benefits will flow to the entity and the cost can be measured reliably.

Subsequent expenditure is capitalised if it extends the useful life of the asset or expands its capacity.

For an illustrative example please refer to the Appendix 2 "Accounting for expenditures after the initial commissioning of an asset – expense vs. capitalise".

Appendix 2 "Accounting for expenditures after the initial commissioning of an asset – expense vs. capitalise"

The following example serves to illustrate the appropriate accounting.

In the second half of the year a company continued expenditures for the reconstruction of an electrolysis shop; the launch having taken place in the beginning of the year. These expenditures were as follows:

Type of expense	Amount US\$`000	Comments
Periodic maintenance costs	300	Maintenance services were provided to production equipment installed in the new electrolysis shop to restore the original standard of performance.
Installation of new electrolytic cells	2,200	Initially 200 electrolytic cells were installed. To increase output management decided to install 50 more cells.
Pilot production costs	200	Cost of producing samples to ensure the proper work of the newly installed electrolytic cells.
Reconstruction of metal floor coating	1,800	Removal of 20 year old, fully depreciated metal floor coating and covering with a new metal floor coating. This increases the useful life of the building which houses the shop by 20 more years.
Window glass fixing shop premises	700	Old, fully depreciated windows were replaced with new ones in accordance with the original plan of replacement.
Installation of new electricity cables	1,100	Upgrade of electricity system was performed to supply new electrolytic baths with electricity power
Total	6,300	

The following conclusion can be reached in the example above:

- Installation of new electrolytic cells, pilot production costs and installation of new electricity cables for the amount of US\$ 3,500,000 will allow future economic benefits associated with these items to flow to the company and costs were measured reliably. Recognition principles were met, therefore expenditures should be capitalized.
- Reconstruction of metal floor coating and window glass fixing for the amount of US\$ 2,500,000 were incurred to increase the useful life of shop premises and therefore additional future economic benefits will flow to the company. Recognition principles were met, therefore expenditures should be capitalized.
- Periodic maintenance costs should be expensed when incurred as these do not meet the recognition criteria.