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Distinctions between private and public sector management in Australia are diminishing. Public sector managers now need to develop approaches and skills formerly considered to be the hallmarks of their counterparts in the private sector – strategic thinking, business acumen, a customer (or user) focus and the capacity to take considered risks.

This part of the Asset Management Series will assist public sector managers to apply these skills in managing public assets effectively and accountably.

It sets out the operational policies and practices for asset management that apply to all Victorian Government departments and agencies wholly or partly funded through the State budget, and provides assistance for asset managers to interpret policy requirements in the light of their particular situation. It was developed in line with the principles and key activities set out in Part 1 of the series, and in the context of applicable legislation and Government and administrative policy (see Appendices 2A and 2B).

Part 2 is concerned with ‘what to do’, not ‘how to do it’, and is intended for use by:

- › managers (at all levels) who are responsible for at least some asset management activity;
- › staff who make decisions about assets; and
- › staff of central agencies with responsibilities that affect asset management.

For ease of reference (except where its use may mislead or confuse), the term ‘entity’ has been used throughout this part to refer to all Victorian Government departments and agencies that are wholly or partly funded through the State budget, and that, under the provisions of an Act, are required to report to Parliament.

Policy statements

Statements of Government policy are identified by a crest icon. Details of policy documents from which these statements have been derived are at Appendix 2B.

Below is an example of a typical footnoted policy statement.



Secretaries of Departments and heads of statutory bodies are accountable for the planning, management and performance of service delivery assets under their control.¹

Any policy in this document not identified as Government policy should be interpreted as an administrative policy.

References and contacts

Publications, other information sources, and details of contacts who can provide further information, are identified by an information icon, as in the following examples:



Financial Management Act 1994
Financial Management Regulations 1994

Department of Treasury and Finance,
Budget and Resource Management
Division
Telephone 61 3) 9651 1234

Only organisational names and units have been listed. Unless otherwise indicated, all contacts are Victorian organisations. It should also be noted that the area code of all telephone numbers listed in this part does not include the zero digit.

¹ Budget Sector Asset Management Principles
Budget and Expenditure Review Committee, 1993

*Out of intense complexities
intense simplicities emerge.*

Winston Churchill

Today's manager of public assets faces many new challenges. Technology is advancing rapidly and social changes are diversifying community needs.

Demands for new or improved assets are mounting, while the capital funds available to acquire them are limited.

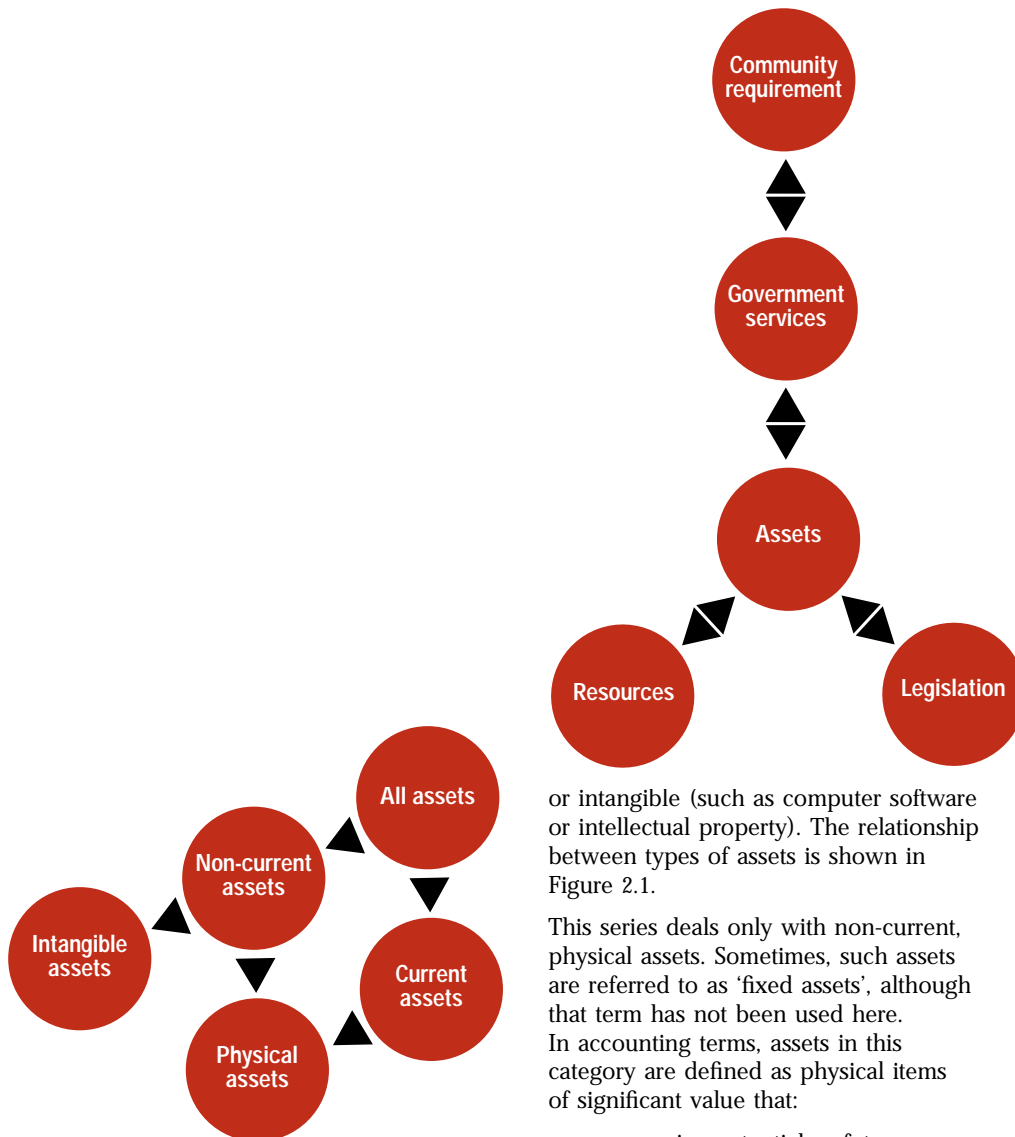
Pressures to conserve finite resources and improve the quality of life continue, together with a sharpening focus on commercial principles in the operations of the public sector.

Management of public assets requires a comprehensive approach. A diversity of processes and activities is involved, as is the consideration of a number of strategic, operational and financial issues.

This section has been designed to help the reader to see asset management in context and to understand some of its fundamental concepts.

An asset is an item of value – something that is ‘worth having’. Some assets have an expected short life or are readily turned into cash, such as investments or inventory – these are known as ‘current assets’. Others have a potential service life longer than one year, and are known as ‘non-current assets’.

Non-current assets may be either a physical item (such as land or buildings)



or intangible (such as computer software or intellectual property). The relationship between types of assets is shown in Figure 2.1.

This series deals only with non-current, physical assets. Sometimes, such assets are referred to as ‘fixed assets’, although that term has not been used here.

In accounting terms, assets in this category are defined as physical items of significant value that:

- › possess service potential or future economic benefits;
- › are controlled by an entity;
- and
- › originate as a result of past transactions or events.

This definition typically includes such items as land, buildings, infrastructure, plant and equipment, cultural collections, and natural resources.

Figure 2.1
Types of assets

What assets are for

The role of assets is to support the delivery of a government service to the public. They combine with other resources of government (such as funding and human resources) to make the delivery of a community service possible. (see figure 2.2). If it does not contribute effectively to such a service, an asset should not be held in or used by the public sector.

Figure 2.2
Assets and service delivery

Decisions about assets must therefore be service driven. The need for services may vary depending on such factors as population distribution, and will alter over time as the characteristics of populations change. As the need for services changes, the demand for different types of assets will also change.

Classes of assets

Assets vary considerably in their size and nature, and it is useful to classify them into logical groupings for management control and financial treatment.

Classifications

may also be imposed by external reporting requirements. Typical of these is the classification:

- › land;
- › buildings;
- › infrastructure;
- › plant and equipment;
- › cultural collections; and
- › natural resources.

This classification is used in the Chart of Accounts for balance sheet reporting and is normally employed in annual financial statements. Classes may be broken down even further for management purposes. For example, the 'plant and equipment' class could be divided as follows:

- › furniture and fittings;
- › information technology assets (computing equipment);
- › office machines;
- › kitchen equipment; and
- › vehicles.

Managers need to distinguish between classes of assets, and exercise judgment and discretion in applying the policies and practices outlined in this part. For example, the maintenance approach adopted for personal computers or a suite of office furniture will be different to that required for a major item of sophisticated machinery or a school. Similarly, the planning input required for the construction of a new hospital would obviously be more comprehensive than that required for the acquisition of a new vehicle. The accounting treatment of various classes of assets may also differ considerably in areas such as applicable depreciation rates, the frequency and precision of revaluation, and the approach to condition assessment and stocktaking.

1.2 The asset life cycle

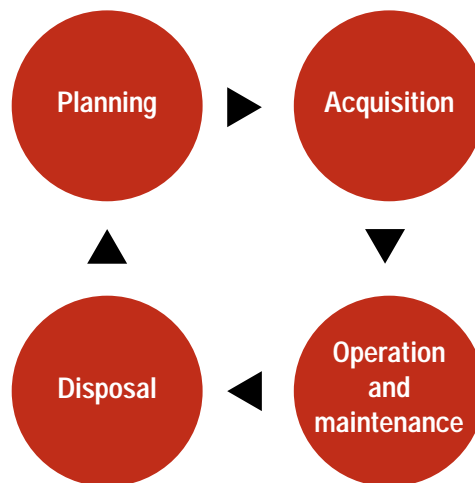
In determining the approach most suited to the class of asset, managers should consider their responsibility to account for the effective and efficient management of the item(s) in question, and the risks and benefits attached to differing levels of record-keeping and accountability.

Non-current physical assets typically have a long life. They consume resources to acquire or create them and to keep them in operational condition over the whole of that life. Many decisions about assets are enduring, and have long-term implications. Because of these characteristics, it is helpful to consider the use of assets in terms of their life cycle.

The phases through which an asset passes during its life are:

- the identification of need, where the requirement for a new asset is planned for and established;
- the acquisition phase, where the asset is purchased, constructed or otherwise created;
- the operation and maintenance phase, where the asset is used for its intended purpose. This phase may be punctuated by periodic refurbishment or major repair, requiring the asset to be taken out of service for periods of time; and
- the disposal phase, initiated when the economic life of the asset has expired, or when the need for the service provided by the asset has disappeared.

The asset life cycle is shown diagrammatically in Figure 2.3.



Decisions taken about an asset in one phase can affect its performance in others. As an example, seeking minimum capital cost solutions in the acquisition phase can have adverse effects on long-term operating costs. Inadequate attention to maintenance can accelerate the need for major repairs, or shorten the operational life of the asset. It can also prejudice the achievement of maximum returns on disposal. Conversely, careful management of existing assets can extend their effective life and avoid or defer the need for new acquisitions.

The concept of 'the asset life cycle' is aimed at encouraging an understanding of these effects, and at helping managers to reach decisions about assets in a whole-of-life context. Economic evaluation tools such as discounted cash flow are often useful in assessing the long-term effects of individual decisions about assets.

Entities should consider whether the asset management responsibilities of their managers reflect a life cycle approach. Limiting the responsibility of managers to a single phase (such as acquisition, or operation and maintenance) will not lead to sound long-term decisions about assets. Asset managers should be accountable for the life cycle effects of their decisions.

Figure 2.3
The asset life cycle

The principal objective of asset management is to enable an entity to meet its service delivery objectives efficiently and effectively. It involves guiding the acquisition, use and disposal of assets, and managing the related risks and costs over all phases of the asset life cycle.

To be effective, asset management needs to be considered as a comprehensive and multi-disciplinary activity that takes into account a range of factors such as:

- technical adequacy and commercial viability;
- external or market factors (commercial, technological, environmental or industry implications);
- the competing demands of stakeholders (in some instances); and
- the need to rationalise operations to improve service delivery or to enhance cost-effectiveness (in some instances).

Managers responsible for assets have recourse to a range of techniques to assist them. These include value management, demand management, economic appraisal, life cycle costing and risk management (see Glossary for definitions). Risk management is particularly important as it underpins many of the key decisions made about assets.

- the asset life cycle and asset management principles;
- the needs of the users of the asset;
- the policy and legislative environment;
- the entity's corporate management and planning framework;

Entities

Assets must be controlled by an entity. In this part, an entity is defined as a Victorian Government department or agency that is wholly or partly funded through the State budget and that is required to report to the Victorian Parliament.

Managers in reporting entities are expected to use financial and asset reports to guide them in evaluating and making decisions about the allocation of resources.

The policies and practices outlined in this part apply to all Victorian Government entities as defined above.

Control

An entity is deemed to control an asset if it has the capacity to enjoy the service potential or future economic benefits of the asset, and can deny or regulate the access of others to those benefits.

However, the entity that is responsible for the control of a public asset may not necessarily be the entity that 'owns' it.

All public assets are owned by the Crown, although there are a number of ways in which this 'ownership' may be expressed. An asset may be:

- › deemed to be 'owned' in the right of the State of Victoria; or
- › 'owned' in the name of a Minister on behalf of the Crown, or by a body corporate set up for that purpose.

A Minister in whose name an asset is 'owned' may not be the Minister to whom the entity responsible for using that asset reports. Heads of entities who control assets have to account for their proper management. 'Ownership' is not the appropriate measure by which to establish responsibility in the public sector.



¹ Budget Sector Asset Management Principles
Budget and Expenditure Review Committee, 1993

Accountability

Accountability involves mechanisms (including rewards and sanctions) to ensure that a person or entity performs to an agreed standard. As an example, financial accountability involves an obligation to demonstrate that expenditure has been efficient, effective, ethical and in accordance with the law.

Entities that control assets are accountable for their management. Accounting standards contain indicative tests to determine whether an entity has control of an asset, and whether it should be accounted for in the entity's annual financial statements.

Secretaries of departments and heads of statutory authorities are accountable for the planning, management and performance of assets under their control.¹

Managers who are uncertain about their asset management responsibilities should use the information in this section to consider:

- whether they utilise the services of assets, as defined above, in the course of discharging their responsibilities;
- the nature of the organisation to which they belong. If it is a Victorian Government entity as defined in this section, then this series provides the appropriate guidance; and
- which of the assets they use are under the control of the entity (as opposed to being hired from another organisation).

These considerations will enable managers to compile a list of assets for which they are accountable.

As a first step in fulfilling their responsibilities, managers must develop an appropriate asset register, if it does not already exist. Assets must be identified, classified and valued as set out in Section 7, Asset Recording, Valuation and Reporting, and entered in the register.

This will assist in meeting statutory reporting obligations. Further steps can then be taken to strengthen the management of the assets as set out in other sections of this part.

*There is commonly less money,
less wisdom, and less good faith,
than men do account upon.*

Francis Bacon

Financial management and accounting conventions provide a disciplined and consistent framework for recording and reporting much of the information needed for asset management. Accounting conventions and reporting obligations influence all phases of the asset life cycle.

This section collects and explains the key financial and accounting concepts that affect asset management.

Traditional accounting conventions previously used in government were based on cash and commitment accounting and did not yield all the information needed for asset management purposes.

Accrual accounting, coupled with improved financial management information systems, can provide the comprehensive and timely information that is necessary. These approaches require the maintenance of complete and accurate asset registers, and regular revaluations and appraisals of asset holdings. The true cost of owning and operating assets can then be readily determined.

Financial accounting is not an end in itself, and the managers of assets will require other information to gauge some aspects of asset performance such as functionality and utilisation. There is a close correspondence between financial management and other records associated with asset performance, and managers need to have a good understanding of the fundamental financial management and accounting concepts that apply.



Recognition of assets

An asset should be recognised in the financial statements of an entity if it meets all of the following criteria:

- The asset has service potential for the entity.
- The entity has the capacity to control the service potential of the asset.
- An event giving the entity control over the service has occurred.
- It is probable that the service potential will be used.
- The asset has a cost or value that can be reliably measured.
- The estimated value of the asset is above the entity's recognition threshold.

Accrual Accounting Manual

Chapter 4 – 'Asset Management Recording' Department of Finance (Victoria), 1994

Asset Management Principles

Victorian Government, 1994

Recognition and Valuation of Non-current Physical Assets

Department of Finance (Victoria), 1995

Statement of Accounting Concepts 4 – Definition and Recognition

of the Elements of Financial Statements
Australian Accounting Research Foundation, 1992

Department of Treasury and Finance,
Accounting and Financial Reporting
Division

Telephone 61 3) 9651 2187

Service potential

The concept of 'service potential' relates to the fundamental nature of an asset – it exists or is acquired to support a service. Typical 'services' may be the provision of filtered water, accommodation for administrative workers, the clinical treatment of patients, or the processing and transfer of information.

The term 'potential' is used because the asset itself does not provide the service – it only contributes to the delivery of the service. Also, the capacity of the asset



to support the delivery of services may not be fully utilised. Service potential is a measure of the ability of the asset to fulfil its role in service delivery.

Decline in the service potential of an asset typically occurs over time through:

- › physical wear and tear; and/or
- › technical or functional obsolescence; and/or
- › commercial obsolescence.

Financial recognition of the decline in service potential over the life of an asset is through the use of depreciation, which is discussed below. A decline in service potential can be arrested or reversed by enhancing or refurbishing the asset. When this occurs, the asset should be revalued.

Service potential is also referred to as 'future economic benefit'.

Depreciation

Depreciation recognises the cost of consuming the service potential of an asset over time, and provides a means of accounting for the cost of an asset over its useful life.

The recognition of depreciation charges is necessary for the valuation of assets and costing of services, and is also used for resource allocation and asset performance assessment. Depreciation is not normally funded and does not provide cash for the replacement of an asset.

Depreciation can be calculated in several ways. Some methods are arithmetical, such as the straight-line or reducing balance techniques. Others are designed to reflect the actual condition or capacity of the asset as realised over time (such as the production unit method, or 'condition-based depreciation'). The method chosen should match the pattern of service potential yielded by the asset as closely as possible, and the depreciation charge will then be a realistic reflection of the cost of providing the services by using the asset.

Depreciation rates must be reviewed annually and, if necessary, adjusted to reflect the most recent assessments of the asset's useful life (see the section on useful life below for issues to be considered in making this assessment).



Accrual Accounting Manual,
Chapter 7 'Depreciation of
Non-current Assets'
Department of Finance (Victoria), 1994

*Australian Accounting Standard 4 –
Depreciation of Non-current Assets*
Australian Accounting Research
Foundation

Department of Treasury and Finance,
Accounting and Financial
Reporting Division
Telephone 61 3) 9651 2187

Useful life

An asset's useful life is the period over which it is expected to provide the entity with service. Depending on the nature of the asset, useful life can be expressed in terms of time (years) or output (production or service units).

Useful life must be realistically assessed. Entities should consider the following:

- Over what period does the entity expect to gain service potential from the asset?
- Has the asset been acquired for a specific project, or can it be redeployed within the entity over time?
- What has been the past experience of such assets in use?
- Is the past experience an appropriate benchmark, given the technology embodied in the asset?
- Has an independent adviser assessed the condition of the asset or its life expectancy?
- What is the opinion of the user or relevant expert about the asset's useful life?
- What is the net amount expected to be recovered on the asset's disposal?

Consideration of these factors will enable the expected life of an asset to be assessed realistically. Useful life is an important determinant of the rate of depreciation.

Valuation

Improved financial and asset information is needed for the implementation of accrual accounting in the public sector. The Victorian *Financial Management Act 1994* requires that all assets controlled by the Victorian Government be recognised and valued.

Australian Accounting Standards provide

the overall framework for all accounting in the budget sector. *Australian Accounting Standard 29, Financial Reporting by Government Entities*, is particularly applicable. *The Accrual Accounting Manual*, issued by the Department of Finance, provides further detailed guidance on the accounting treatment of asset valuation, depreciation and revaluation issues.

The Department of Finance publication, *Recognition and Valuation of Non-current Physical Assets*, establishes a framework for valuing such assets. The document also covers depreciation and revaluation.

The implementation of these measures is a core element of the Government's reform of financial management in Victoria.

Australian Accounting Standard 10 – Accounting for Revaluation of Non-current Assets
Australian Accounting Research
Foundation

Australian Accounting Standard 29 – Financial Reporting by Government Entities
Australian Accounting Research
Foundation

Financial Management Act 1994
Recognition and Valuation of Non-current Physical Assets
Department of Finance (Victoria) 1994

Department of Treasury and Finance,
Accounting and Financial
Reporting Division
Telephone 61 3) 9651 2187

Office of the Valuer-General
Telephone 61 3) 9603 8200



2 Budget Information Paper No. 1
Public Sector Capital Works, 1994-95
Victorian Government

Enhancement and refurbishment

Assets are often modified during their life. There are two main types of modification:

Enhancement: where works are carried out on the asset that increase its service potential. Works of this kind may be extensions, or modifications to improve functionality such as installing computer cabling or increasing the speed of a lift. Enhancements normally increase the service potential of the asset, and result in an increase in value; and

Refurbishment: where major works are carried out to bring or restore the asset to acceptable condition. Refurbishment works do not necessarily extend functionality or the life of the asset, but are necessary for the planned life to be achieved. In such cases, the value of the asset is not affected.

If the refurbishment extends the useful life of an asset, the service potential (and value) of the asset is increased accordingly.

Types of asset expenditure

Expenditure on assets may be incurred using capital or recurrent funds.

The acquisition of new assets is a capital expense. In addition, expenditure on an existing asset is treated as capital expenditure if it:

- › extends the asset's economic life; and/or
- › improves the asset's service potential; and/or
- › adds attributes not previously part of the asset.

Any expenditure on an existing asset that falls outside this definition is classified as an operating expense and met from recurrent funds. An example of this is maintenance expenditure. By comparison with capital expenditure, maintenance expenditure enables an asset to last its expected useful life but does not extend its service potential. (Expenditure on minor repairs and cyclical maintenance, such as on painting and cleaning guttering, are

examples of maintenance expenditure.)

3.0 Asset planning and budgeting

2

The capital charge

A capital charge applies to all entities in order to distribute part of the centrally funded annual cost of capital. This gives entities greater incentive to increase the performance of their asset base by encouraging maintenance, rather than inefficient replacement; redeployment rather than retention; and completion of construction and acquisition on time and according to specification.²

The capital charge on funds reflects the cost of these funds, which are derived from a mix of external borrowings at commercial rates and funds generated from taxes. The capital charge is the means used to measure the cost of capital that entities have invested in the assets under their control.

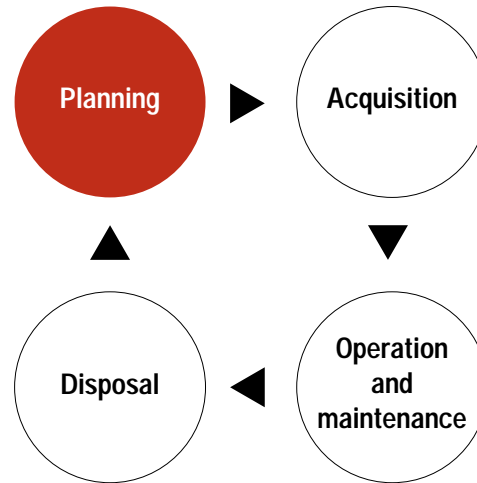
The essential features of the capital charge are as follows:

- It applies to all entities and to the Parliament.
- The Department of Treasury and Finance advises on the rate to be used.
- It applies to assets controlled by entities, and to capital grants to private organisations.
- A credit for the capital charge will be given on disposal of the asset.

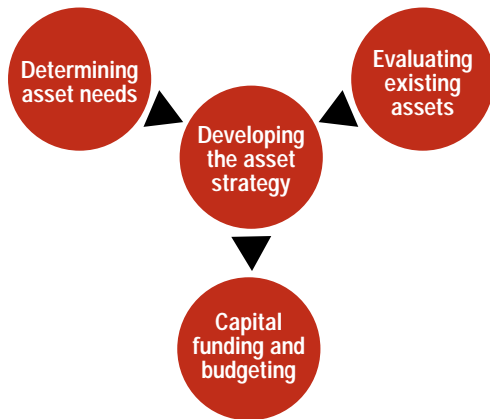
The capital charge must be taken into account when calculating the full cost of an asset for pricing purposes. It will form part of the core cost that should be recovered (except in special circumstances where assets are provided at minimal or no cost – see Section 8).

Budget Information Paper No. 2 – Budget Performance and Outlook
Victorian Government, 1994

Department of Treasury and Finance,
Budget and Resource Management
Telephone 61 3) 9651 5344



3.1 Determining asset needs



*Without counsel plans go wrong,
but with many advisers they succeed.*

Proverbs 15:22

Asset planning is fundamental to the effective management of an entity's business, being the first phase in the asset life cycle (see Figure 2.4).

Matching the asset requirements of an entity to its service delivery strategy should result in assets with the necessary capacity and performance. Asset planning also leads to specific actions to acquire any new assets that may be needed, to dispose of assets that are surplus and to operate and maintain existing assets effectively.

This section describes a model asset planning framework (illustrated in Figure 2.5) within which entities are required to undertake planning and budgeting for asset acquisition, operation and disposal.



Figure 2.4
Asset life cycle: the planning stage



Figure 2.5
Asset planning framework

Asset management decisions regarding acquisition, use and disposal are to be made within an integrated service and financial planning framework, and in the context of the Government's overall resource allocation policies and priorities.³

The need for assets is directly linked to the provision of services. Asset planning involves the assessment of existing assets and planned acquisitions against service delivery requirements. Proposals for new assets must be justified by a thorough evaluation of all service delivery options, and, as part of the Government budgetary process, be the subject of a comprehensive appraisal or investment evaluation.



⁴ Budget Sector Asset Management Principles
Budget and Expenditure Review Committee, 1993



Service delivery strategy

All entities are responsible for developing a service delivery strategy within the context of their objectives and corporate plan. The strategy is based on a needs analysis and a review of how services are currently being provided. It should:

- › define the scope, standard and level of services to be provided;
- › assess the methods of service delivery and the resources needed, including requirements for the use of assets; and
- › consider methods of containing demand by using demand management techniques. This may involve reducing the need for the service (for example, by combining it with another service, or by dealing with the situation that causes the service to be sought). It may also involve a review of pricing policies (see Section 8.2).

Service options need to be evaluated on financial, economic, social and environmental grounds.

Non-asset options

Service delivery options that reduce or contain a requirement for the entity to use assets should be considered. Devising non-asset options should challenge traditional concepts and assumptions about the delivery of services, and enable innovative methods to be developed.

Three broad types of non-asset solutions should be considered:

- › redesigning the service to reduce the need for assets (eg home-based medical care);
- › increasing the utilisation of existing assets (eg the conduct of evening TAFE courses in school buildings) so that the acquisition of a new asset can be avoided; and
- › using private sector contractors to provide parts or all of the service. Assets may still be required for the service, but they will be controlled and operated by the contractor rather than being controlled by the entity.

Once the service need is determined and the service strategy devised, those services that need to be supported by an

5 [Budget Sector Asset Management Principles](#)
Budget and Expenditure Review Committee, 1993

asset-based solution can be determined, as can the performance requirements of those assets over the planning period.

The evaluation of existing assets determines whether their performance is adequate to support the selected service delivery strategy.

Program evaluations are to include the evaluation of asset performance. Asset performance is to be reviewed regularly against best practice benchmarks to identify assets that are under-performing, or costly to own or operate. It is also possible to over-invest in assets. The evaluation should reveal assets that provide more than their required capacity, or are surplus to requirements.

Assets that have been inadequately maintained may pose potential safety or health risks, disrupt essential services, or incur unforeseen expenditures for the correction of defects.⁴

Evaluating asset performance

All assets currently being used to deliver the service under consideration need to be identified and registered. How effectively these assets support service requirements also has to be determined. As part of this process, the following aspects need to be assessed:

Physical condition: Is the asset adequately maintained? Is there a maintenance backlog that requires attention? Are major replacements or refurbishments likely to be required during the planning period?

Utilisation: How intensively is the asset used? Could it be used more productively by extending its working hours, or by accommodating additional functions?

Functionality: How well suited is the asset to the activities and functions it supports?

Financial performance: Are the asset's operating costs similar to those for other comparable assets? (Use benchmarking to establish this wherever possible.) Are the energy, cleaning and maintenance costs reasonable? Are user charges being made, and how do they relate to the total operating costs of the asset (including the cost of capital)?

These measures for assessing asset performance are discussed in more detail in Section 5.1.

Assessing the Condition of Constructed Assets

Department of Planning and Development, Office of Building, 1995

Department of Planning and Development, Office of Building
Telephone 61 3) 9651 5800

Current or committed projects

The assessment of existing assets must include those assets in the process of being acquired or that are committed (such as facilities under construction, or those incorporated in an authorised capital works program).

The result of evaluating existing and anticipated new assets is a statement of the assets available, or expected to be available, to support the selected delivery strategy.



3.4 Capital funding and budgeting

Entities are to establish systems and processes to support the preparation of five-year forward asset strategies covering acquisition, maintenance, refurbishment, redeployment and disposal, together with the attendant capital and operating costs.⁵

An integrated approach towards asset planning and management will enable entities to deliver quality asset based services efficiently and effectively.

By integrating asset planning with its overall planning processes, an entity is better able to make the most appropriate decisions about its asset profile, particularly when responding to such factors as:

- new or changing service delivery requirements;
- different methods of service delivery; and
- evolving technology.

Comparison of existing and required assets

Strategic planning begins by comparing assets that are needed with those that exist or are committed to come into service. Entities must carry out this analysis for all services for which they are responsible, and establish which assets are:

- capable of meeting service delivery requirements (with or without modification);
- surplus to needs; or
- not available, and have to be acquired.



The analysis needs to consider the options in terms of service outcomes, financial implications and risk. This analysis may involve some rationalising or sharing of assets that support different services within the same portfolio.

The asset strategy

The asset strategy should consider various ways of achieving the desired results within the portfolio, and include an evaluation of the costs, benefits and risks associated with each. It should also consider the possible methods and benefits of private sector involvement

in all phases of the asset life cycle.

⁷ **Budget Sector Asset Management Principles**
Budget and Expenditure Review Committee, 1993

The individual plans that constitute the asset strategy are described below:

Acquisition plan

Assets to be acquired may be purchased (either on the open market, or from another government entity), or custom developed for their purpose. They may also be leased or hired. The asset acquisition plan should define the type and timing of asset requirements, and set out the proposed method of acquisition and financing.

Operations plan

The operations plan defines operating policies (ie in respect to working hours, security, cleaning, energy management and similar) and the resources required to manage the asset. The operational management of individual assets should be assessed to determine whether this function can be contracted out in whole or in part.

Maintenance plan

The maintenance plan defines maintenance standards, describes how the work is to be carried out, and forecasts the necessary maintenance expenditure for the planning period.

Modifications or enhancements are work that is required because of a change in the use of the asset, or a need to improve its functional performance. Works of this nature normally increase the service potential of the asset and are then treated as capital expenditure.

Disposal plan

Disposal options include transfer for alternate use, rental, sale and/or lease-back, and demolition (see Section 6.1).

Funding plan

Entities controlling assets should consider the options available for funding both capital and operating expenditures for assets.

New assets may be funded in whole or in part:

- from the disposal of unused assets;
- by leasing or other form of private investment; or
- from borrowings, including appropriated funds.

Revenues to support borrowing or leasing charges, or to supplement operating expenses, may be obtained from user charges or levies (see Section 8.1).

The funding plan should be based on an analysis of all available possibilities, including utilising private sector funding wherever appropriate.

Risk management plan

Entities should prepare a risk management plan which describes the risk management strategies and actions to be implemented for the assets under their control.

They are to be:

- aimed at effective and timely outcomes;
- geared to meeting the quality standards of industry; and
- determined in line with best practice.⁸

Entities must continue to monitor and evaluate the effectiveness of their risk management measures. If necessary, these measures should be redefined.



⁸ Budget Information Paper No. 1
Public Sector Capital Works, 1994–95
Victorian Government

Insurance

To be managed effectively, assets must be protected against theft or fraudulent use and other hazards such as fire.

The consequences of not having the asset available for service delivery must be carefully considered.

Assets must therefore be adequately insured to minimise financial loss to the Government.

Department of Treasury and Finance,
Budget and Resource Management
Telephone 61 3) 9651 5344

Department of Treasury and Finance,
Managed Insurance Fund
Telephone 61 3) 9651 2187

The budget sector capital works process enables the Government to consider asset acquisition and enhancement options effectively and to establish priorities. Capital funds can then be applied to new projects and investments to satisfy government objectives, and to obtain best value for money for the State.

Sources of capital funding

If it is determined that public sector capital funding is appropriate for an asset, funds are obtained from a range of sources, such as those referred to below:

Commonwealth programs

Commonwealth programs may provide capital funding to States in order to fulfil particular Commonwealth–State objectives. In these cases, the same evaluation criteria apply as for all State-funded investment proposals, ensuring that Commonwealth-funded projects complement State capital investments, and enhance them where possible.

State dedicated funds

Some capital investment projects are funded from State dedicated funds.

Annual capital works allocations

All investment proposals not eligible for Commonwealth funding or State dedicated funding are considered for commitment against the normal annual allocations estimated to be available for future capital works.

Securing funding for an asset

All proposals to acquire new assets, enhance existing assets or develop increased private sector capacity to provide public services must be evaluated in accordance with evaluation guidelines and methodologies endorsed by the Department of Treasury and Finance, and must identify:

- › the full costs associated with the proposal;
- › all impacts on future budget supported expenditure and receipts;
- › the net impacts on service delivery capacity, quality, range and efficiency; and
- › the arrangements and timetable proposed for implementation.⁷

Where asset plans involve capital expenditure (for either new projects, or enhancements to an existing

4.0 Asset acquisition

asset), an investment proposal for each individual proposal must be prepared for consideration by the appropriate Government committee.

Requirements of each investment proposal

Soundly based investment proposals demonstrate clearly that their benefits exceed their costs. They will be based on the asset strategy and will detail the links between the proposal and both the service delivery strategy and the entity's corporate plan. They will also show that relevant asset and non-asset based service options have been considered.

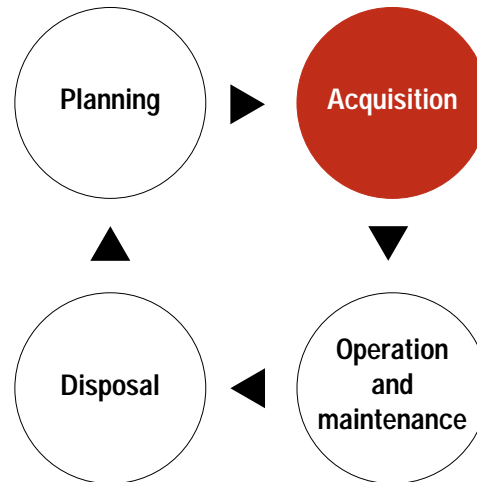
Advice on the required contents of a capital investment proposal is issued by the Department of Treasury and Finance.

Proposals must address the evaluation criteria, indicate the preferred funding source and set out the full costs, benefits and risks. Proposals must also address the ongoing operating and maintenance cost implications, and identify the recurrent funding needed for this purpose. This information should be used by the entity to support the logic underpinning the ranking of proposals.

Ranking and evaluation of investment proposals

In ranking and prioritising investment proposals, entities must take into account the role that the proposed assets will play in service delivery, and the relative importance of the services themselves.

The entity must then submit its proposals, in ranked order, to the Department of Treasury and Finance, irrespective of the proposed source of funds. (Projects to be supported from dedicated and external fund sources must also be fully evaluated and prioritised according to the particular processes that apply to those funds sources.)



Consideration of investment proposals

All submissions requiring approval for capital funding are made to the Budget and Expenditure Review Committee (BERC).⁸

The Department of Treasury and Finance will assess investment proposals for subsequent consideration by BERC.

The Department of Treasury and Finance reviews the investment proposals lodged by each entity, and applies 'across Government' criteria. This will result in the proposals being ranked in a whole-of-government context (eg the first three proposals ranked by one entity may be deemed to have a higher priority than the proposal ranked first by another entity).

The criteria considered by the Department of Treasury and Finance include:

- › the impact on service delivery and productivity;
- › the financial effects, including costs, savings, revenues and offsets;
- › the economic costs, benefits and risks (including environmental and social effects);
- › other risks to Government that might be involved; and
- › the capability of the entity to implement the proposal successfully.

The Department of Treasury and Finance then forwards the proposals, ranked in whole-of-government priority order, to BERC for its consideration and approval. BERC formally assesses all proposals, including any recurrent

4.1 Acquisition of assets



financial impacts.

Assessing the Condition of Constructed Assets

Department of Planning and Development, Office of Building, 1995

Budget Information Paper No. 1 – Public Sector Capital Works, 1994–95
Victorian Government, 1994

Budget Information Paper No. 2 – Budget Performance and Outlook, 1994–95

Victorian Government, 1994

Infrastructure Investment Policy for Victoria

Department of Treasury (Victoria), 1994

Investment Evaluation Guidelines (forthcoming)

Department of Treasury and Finance, (Victoria)

Department of Planning and Development, Office of Building
Telephone 61 3) 9651 5800

Department of Treasury and Finance, Budget and Resource Management
Telephone 61 3) 9651 5344

Department of Treasury and Finance, Project Finance and Evaluation
Telephone 61 3) 9651 5771



Riches do not consist in the possession of treasures, but in the use made of them.
Napoleon Bonaparte

Figure 2.6
Asset life cycle: the acquisition stage



Asset acquisition is the next stage in the asset life cycle after the planning phase (see Figure 2.6).

This section outlines the practices that entities are to follow to acquire assets. These practices may vary according to what the asset is, namely:

- › land (both improved and unimproved);
- › building and related works, and other public construction (ie assets that are constructed); or
- › other assets, including capital equipment (ie such as those recorded in an asset register, regardless of funding source).



Asset acquisition decisions are to be made within an integrated service and financial planning framework.⁹

The acquisition of assets is a key asset management activity. It is imperative, therefore, that acquisition decisions be taken within an integrated planning framework that takes account of service delivery needs, corporate objectives, financial and budgetary constraints, and the Government's overall resource allocation objectives.

Options for acquiring assets include purpose-design and construction, purchasing or financial leasing. As part of the acquisition process, an entity needs to consider:

- › the nature of the assets to be acquired (ie whether they are specialised assets or common items);
- › the market conditions and the implications for the acquisition cost (ie whether it is a buyers' or a sellers' market);
- › the industry capacity (ie the number of potential contractors or suppliers – based both locally and overseas – capable of supplying the assets);
- › the industry standard (ie how the assets are normally procured in the industry); and
- › the suitability of contractors or suppliers (ie whether the contractors or suppliers engaged need government endorsement of the Victorian Government Purchasing Board (VGPB)).

Minimising the exposure to risk

Acquisition decisions require thorough examination and economic appraisal. As outlined in Section 3.3, any potential risks as well as the consequences of acquiring an asset should be examined before any action is taken.

The involvement of the private sector in the acquisition process should also be considered, where appropriate. (Further information is contained in the Victorian Government publication, *Infrastructure Investment Policy for Victoria* (1994)).

In accounting for private involvement in public investment, however, the entity should arrange for an appropriate sharing of risk. This approach is consistent with the Government's drive towards a more commercial focus in the management of its entities. Legal expertise should be engaged to assist in preparing contracts to minimise exposure to risk.

Some of the issues which may be applicable and need to be considered and clarified in contracts with contractors and suppliers include:

- › the type of contract;
- › ownership and control;
- › performance criteria to be met;
- › rights over the intellectual property developed as a result of the contract;
- › responsibility for maintenance;
- › responsibility for testing, inspection and installation; and
- › responsibility for post-completion testing.

Purchasing ethics and principles

Officers involved in purchasing and supply management in the public sector shall maintain the highest ethical standards, and seek best value for money.

The following principles should be observed:

- › Public money should be spent efficiently and effectively, and in accordance with Government statutes, regulations and policies, including the supply policies of the VGPB and the Minister responsible for building and construction matters.
- › Confidentiality is to be maintained at all times.
- › Gifts or favours from current or potential contractors or suppliers that might compromise their integrity as a delivery/purchasing agent should not be accepted.
- › Purchasing should be carried out without favour or prejudice.
- › Purchase orders for identical goods or services must not be split in order to circumvent established procurement delegation limits.
- › All potential contractors and suppliers are to be provided with adequate and identical information on which to base their tender, proposal or quotation.





Procedures are to be established and maintained to ensure that:

- fair and equal consideration is given to each tender or quotation received; and
- selection is based on fitness for purpose and on the lowest total cost complying bid.

Infrastructure Investment Policy for Victoria

Department of Treasury (Victoria), 1994

Project Development and Construction Management Act 1994, Ministerial Direction No. 1

Department of Planning and Development, 1995

Supply Policies and Guidelines

Victorian Government Purchasing Board, 1995

Department of Planning and Development, Office of Building
Telephone 61 3) 9651 5800

Department of Treasury and Finance,
Project Finance and Evaluation
Telephone 61 3) 9651 5771

Victorian Government Purchasing Board
Telephone 61 3) 9651 3008

Acquisition of land

Land, for the purposes of this publication, encompasses both improved and unimproved land. It generally also includes all improvements of a permanent nature constructed on it.

Legislation governing the acquisition of land by entities for public purposes is contained in various Acts of Parliament. For example, the Acts listed below govern the acquisition of land within the stated portfolios:

- Conservation and Natural Resources
Conservation Forests and Lands Act 1987
Crown Land (Reserves) Act 1978

- Education

Education Act 1958

- Finance

Financial Management Act 1994

- Planning and Development

Planning and Environment Act 1987

Project Development and Construction Management Act 1994.

Generally, the Crown or an entity acquires land either by agreement or by compulsory acquisition:

- Purchase by agreement can be achieved by negotiation and entering into a common law contract of sale.
- Where necessary, the acquiring entity is empowered under legislation to acquire land compulsorily. If agreement on the compensation to be paid cannot be reached, the matter is determined by the Administrative Appeals Tribunal or by the Supreme Court.

Entities uncertain about whether or not they have the capacity to enter a contract for the sale/purchase of land are encouraged to seek further legal advice.

Department of Planning and Development, Planning Division
Telephone 61 3) 9628 5307

Department of Treasury and Finance,
Victorian Government Property Group
Telephone 61 3) 9651 2496

Construction of assets

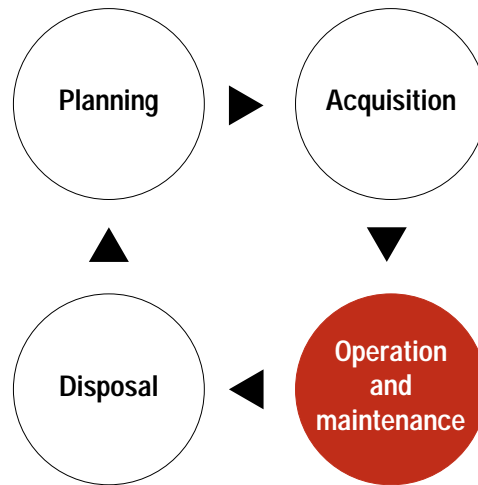
This section relates only to the construction of assets, not the acquisition of existing assets.

The *Project Development and Construction Management Act 1994* provides the Minister responsible for the Act with powers to set standards for public construction, and provides for empowerment of entities and Ministers to facilitate development projects.

Other Acts provide for land development, and for building and other construction works for various public purposes (ie residential subdivisions, public housing, roads, transport facilities, water supply etc).

Contracting methods

Choosing an appropriate contract method is fundamental to the feasibility, development and ultimate success of the procurement. Entities are responsible for choosing the most appropriate method on a project-by-project basis and for identifying, assessing and allocating potential risks to optimise investment return.



The method used to acquire assets should enable:

- appropriate allocation of risks and obligations to relevant parties;
- definition of the respective roles of the various parties involved; and
- definition of the required outcomes of the acquisition process.

The choice of a method is made by considering costs, financial benefits, funding options, risks, delivery times and the period for which the asset is needed.

Lump sum contracts

Lump sum contracts involve the design and documentation of the project. Tenders are then invited and a contractor appointed to construct the works as documented in return for an agreed lump sum payment, paid as the work progresses. A project manager undertakes the management role for the delivery of the project within the specified time, and to meet specified cost and quality targets. The project manager may be an architect or other building professional.

Design and construct contracts

A design and construct contract involves a single supplier or contractor undertaking both the design and construction processes. The contractor engages consultants to design and document the project, generally with the close involvement of the customer.

This type of contract may include warranted or guaranteed maximum price, subject to allocation of risks.



Build-own-operate-transfer (BOOT)

The BOOT process involves private construction of a public asset at the expense of the private owner in return for the right to operate the facility and charge users a fee. At the end of the contract period, the facility reverts to the State. This process can be modified to suit particular needs (eg Build-own-transfer), depending on the requirements for ownership and operation.

Building Act 1993

Code of Practice for the Building and Construction Industry

Department of Planning and Development, Office of Building, 1994

Housing Act 1983

Project Development and Construction Management Act 1994

Ministerial Direction No. 1

Department of Planning and Development, 1995

Transport Act 1983

Department of Planning and Development, Office of Building
Telephone 61 3) 9651 5800

Department of Planning and Development, Office of Major Projects
Telephone 61 3) 9651 5255

Department of Planning and Development, Urban Land Authority
Telephone 61 3) 9628 5111

Department of Transport,
Public Transport Corporation
Telephone 61 3) 9619 6666

Department of Treasury and Finance,
Project Finance and Evaluation
Telephone 61 3) 9651 5771

Acquisition of other assets

The acquisition by entities of assets other than land and those that are constructed is governed by the *Financial Management Act 1994* and by the policies and guidelines of the VGPB.

The supply guidelines issued by the VGPB currently define the Government acquisition requirements for entities.

After accreditation by the VGPB, departments will be able to develop and implement their own acquisition arrangements.

The VGPB will issue practice statements from time to time to assist entities in implementing policies.

Financial Management Act 1994

Supply Policies and Guidelines

Victorian Government Purchasing Board, 1995

Victorian Government Purchasing Board
Telephone 61 3) 9651 3008

Assuming control of an asset

There are a number of ways by which an entity may assume control of an asset, and these are briefly described below.

It should be noted, however, that not all these means apply to all classes of assets, or are available to all entities.

Acquisition with funds from appropriations

An asset that is purchased, constructed or developed by an entity using appropriation funds is controlled by that entity,

unless it explicitly does so on behalf of another entity and an agreement between the entities specifies this.

Acquisition with funds from non-appropriation sources

An asset that is purchased, constructed or developed by an entity using funds from non-appropriation sources (eg user charges, grants, revenues, proceeds of sale of other assets) is controlled by that entity, unless it explicitly does so on behalf of another entity and an agreement between the entities specifies this.

Acquisition with Commonwealth funds

An asset that is purchased, constructed or developed by an entity with Commonwealth funds is deemed to be controlled by that entity unless the funding agreement specifies otherwise.

Acquisition by finance lease

Entities that lease assets under a finance lease are deemed to control those assets.

Acquisition by joint venture

An asset that is purchased, constructed or developed as part of a joint venture (eg private sector investment in public infrastructure and/or contracting-out arrangements) is deemed to be under the control of the entity accountable for the venture, unless an agreement between the joint ventures specifies otherwise.

Transfer

An asset that is transferred from another entity is deemed to be controlled by the entity to which it is transferred.

Vesting

An asset that is vested in an entity is deemed to be controlled by that entity.

Consignment of control

An entity will assume control of Crown land through a system of consignment, which will ratify existing control of the land and will be used for the future transfer of control of Crown land.

Entities that currently control Crown land will need to ensure that the terms and conditions of their control are evidenced in writing in the instrument of consignment.

The system of consignment is subject to further guidelines produced by the Department of Conservation and Natural Resources.

Department of Conservation and Natural Resources

Telephone 61 3) 9412 4678

Donation/gift/bequest

An asset that is donated, given or bequeathed to an entity is deemed to be controlled by that entity unless any restrictions exist that prevent the entity having control of it.

Sovereignty

An asset over which the Crown has asserted sovereignty is deemed to be controlled by the entity using the asset or holding it on behalf of the Crown.

Seizure

Some entities have control over, and are accountable for, the collection of revenues on behalf of the Crown. Assets seized by those entities where customers default on payment are deemed to be controlled by the entity.

Contingent control

Some arrangements, such as private sector investment in infrastructure, afford an entity the right to take control of an asset.

Compulsory acquisition

Some Acts afford an entity the right, on behalf of the Crown, to take control



of an asset.

Crown Land (Reserves) Act 1978

Directions of the Minister for Finance
under the *Financial Management
Act 1994*

Land Act 1958

*Project Development and Construction
Management Act 1994*

*Recognition and Reporting of Crown
Land by Government Entities*

Public Sector Accounting Centre of
Excellence, 1995

*Recognition and Valuation of Non-
current Physical Assets*

Department of Finance (Victoria), 1995

Supply Policies and Guidelines

Victorian Government Purchasing Board,
1995

Accounting

Department of Treasury and Finance,
Accounting and Financial Reporting
Division

Telephone 61 3) 9651 2187

Construction of assets

Department of Planning and
Development, Office of Building

Telephone 61 3) 9651 5800

Land

Department of Conservation
and Natural Resources,
Crown Land and Assets Division
Telephone 61 3) 9412 4406

Department of Treasury and Finance,
Victorian Government Property Group
Telephone 61 3) 9651 2496

Other assets

Victorian Government Purchasing Board
Telephone 61 3) 9651 3008

11 | **Budget Sector Asset Management Principles**
Budget and Expenditure Review Committee, 1993

...for the animals, hedges, trees, buildings and other things of the estate hath each a natural allotment of days; just as we too have an allotment of days. Good management of the estate in accordance with this order of things rests, therefore, in thy possessing a knowledge of the parts so that each may be upheld for the duration of its allotted time and then left to pass. For the wholeness of an estate is not ours alone but also of they who follow and we shall be thanked, not for wonton and untimely outlaying, but for the exercise of good husbandry.
Sir Hugh Platt, 1594

Service delivery needs are recognised in Part 1 of this series, Asset Management Principles, as being fundamental in guiding asset practices and decisions. This section focuses on the performance of assets in meeting these needs and the role that operation and maintenance – the third key stage in the asset life cycle – play in sustaining performance levels (see Figure 2.7). Particular issues addressed are performance assessment and the planning of maintenance requirements.

Figure 2.7
Asset life cycle: operation and maintenance stage



Entities shall establish and maintain management processes to regularly monitor and assess the assets under their control.¹⁰

Protecting service delivery potential and addressing health and safety concerns are priorities when making decisions about asset use and maintenance. It is very important, therefore, that asset performance be appropriately reviewed and evaluated to verify that required outcomes are being achieved.

The results of any performance assessment need to be reported to management to:

- › identify any actions to be taken; and
- › comply with the ongoing reporting requirements of Government, as well as with those forming part of the corporate, business and asset planning processes.

In addition to observing the reporting requirements covered elsewhere in this part, the entity shall comply with the requirements of any legislation that may apply specifically to its operations.

There are a number of measures used to assess asset performance: the asset's physical condition, its utilisation, its functionality and its financial performance. These measures are described below (see also Section 3.2).

Physical condition

An asset should be able to be used safely and effectively. This means that it needs to be maintained in a condition that is adequate for the purpose for which it is intended, and that it complies with the relevant health and safety standards. If this is not the case, the asset's ability to deliver services to the level and standard required will be compromised.

A proper condition assessment of an asset will involve:

- › setting the required condition of the asset relative to its service delivery requirements and value (criteria should include those relating to operational efficiency, public health and safety, and amenity);
- › inspecting the asset and comparing its condition with that required; and
- › forecasting the future condition of the asset.

Condition assessments provide important inputs for compliance with legislation and in planning for asset maintenance.

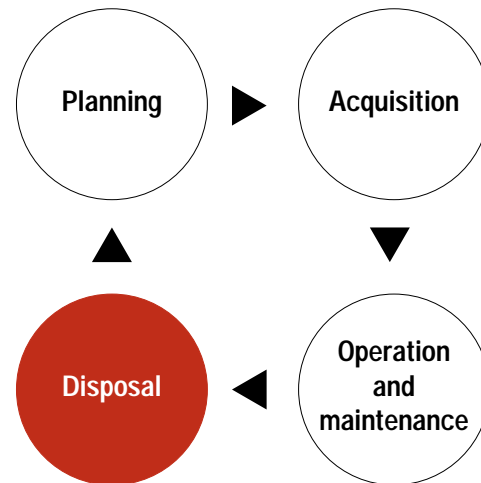
Utilisation

Asset utilisation is a measure of how intensively an asset is being used to meet the entity's service delivery objectives, in relation to the asset's potential capacity.

To assess utilisation, criteria and benchmarks appropriate to the services being delivered and to the class of asset being considered firstly need to be established. The criteria should have regard to:

- › the value of the asset's unit of service potential that is being used relative to the units of service being delivered (eg the future economic benefits of a TAFE college that are consumed relative to the number of students enrolled);
- › the physical measures of asset capacity relative to the units of service being delivered (eg floor space per student place relative to the type of educational or training activity, or to the hours of classroom use per student enrolment); and
- › the use being made of the asset relative to the optimal availability for the type of asset (eg the number of computer hours used relative to the number of

operational hours available on a mainframe computer).



The utilisation criteria should be based, wherever appropriate, on best practice data as well as on the results of analyses undertaken either by the entity or elsewhere in the private and public sectors.

Underutilised assets should be identified, and the reasons for this examined. It may be, for example, that the asset is no longer effective in performing the activities required of it or that it is in less than optimum condition. It may also be that the need for the services it delivers or supports has reduced. The following examples illustrate some of the reasons for underutilisation:

- » physical constraints, such as poor lighting for night-time use;
- » technological obsolescence; and
- » management constraints, such as the hours worked by security or caretaking staff.

Action should be taken either to improve the asset's utilisation or to redeploy it (provided that service delivery needs can be met by alternative means).

Where asset utilisation is low, entities should consider whether the cost of holding the asset exceeds the cost of transferring the services it delivers, and whether there is a more economical way of delivering the services. Alternative or additional uses of assets should also be considered (eg an underutilised group of classrooms may appropriately house a health clinic).



The utilisation of each asset should be reviewed annually.

Functionality

The functionality of an asset is a measure of the effectiveness of the asset in supporting the activities to be carried out.

To monitor and assess functionality, the entity needs to determine:

- the role that the asset plays in achieving service delivery outcomes; and
- the functional characteristics required of the asset to support the specified activities (for example, the functional brief requirements prepared for constructed assets).

The functionality of assets should be regularly reviewed. This will enable any significant impacts on services to be identified. It will also allow timely changes to be made to improve both service delivery and functional standards. Furthermore, the results of regular functionality reviews are used in the formulation of asset strategies.

Financial performance

The financial performance of an asset must be evaluated to determine whether or not it is providing economically viable services.

To do this, the entity needs to monitor and assess:

- operating expenses; and
- current and projected cash flows, including capital expenditures.

This information is then used to determine the current and projected economic return of the asset or portfolio.

Discounted Cash Flow analysis can be used to provide a measure of the Net Present Value and the internal rate of return for assets.

The Department of Treasury and Finance sets a level for charge on capital and hurdle rates against which return on investment is measured.

When assessing project viability, these rates should be used as one of the criteria set for ranking proposals in priority order.

Another important aspect of an asset's financial performance which must be assessed is the maintenance of equity. This measure provides a basis for evaluating the performance of both assets and entities. It is also a major consideration in establishing approaches to service pricing and revenue.



12 | Budget Sector Asset Management Principles
Budget and Expenditure Review Committee, 1993

Asset maintenance

Entities are responsible for developing five-year asset management strategies for the assets under their control.

The strategies are to cover maintenance, refurbishment and energy management and include all operating costs.

They shall also detail the systems and processes to be established to monitor asset performance.¹¹

The usefulness of an asset depends on how effectively it meets its purpose. For many types of asset, this may depend on the regularity and appropriateness of its maintenance. Regular maintenance may also help to preserve an asset's value.

Planning for asset maintenance enables targeted action to be taken in a timely and cost-effective manner. This, in turn, helps to ensure that the entity's asset portfolio can remain appropriate and productive for the lowest possible long-term cost.

As a first step, the entity must determine which of its assets need to be maintained (ie it must assess the materiality of its assets).

Some assets may, for example, have low or little value and have a relatively short expected life; others may be of a type that normally requires little or no regular maintenance effort (eg furniture). Entities controlling such assets may elect to exclude these from the formal maintenance planning process, and rely on regular condition assessments or inspections (eg in conjunction with stocktakes).

For each of those assets or groups of assets that are to be regularly maintained, the entity should develop a maintenance strategy.

Maintenance strategy

A maintenance strategy is a comprehensive plan that:

- defines the asset, the performance required of it, and the level to which it is to be maintained;
- describes the systems and procedures to be used to plan and manage the maintenance work;
- specifies the types of maintenance to be

carried out, and why;

- nominates the means of resourcing and implementing maintenance;
- indicates any requirements for inhouse plant, equipment or spare parts; and
- outlines the projected costs of routine (and corrective/preventive) maintenance, as well as forecasting major replacements for the next 5–10 years.

In developing a maintenance strategy, two considerations are particularly important: the level of maintenance required for the asset, and maintenance priorities.

Level of maintenance: The level of maintenance required for an asset, and the performance expected of it, should be clearly established. The level set should:

- be consistent with the role that the asset will play in the delivery of services, relative to other like assets in the portfolio of the entity;
- reflect obligations for compliance with statutory requirements for occupational health and safety, fire, environmental management and the like;
- be realistically attainable, given the age, condition and expected life of the asset;
- be capable of being achieved within planned resource availability; and
- be agreed with the users of the asset.

The level of maintenance should specify the extent to which the performance of the asset is operationally critical and to which visual appearance is important. It should also stipulate the necessary response times in the event of failure.

Maintenance priorities: Higher priority maintenance tasks (such as those that affect health and safety or that are operationally critical) should be identified in the maintenance strategy. This will enable maintenance effort to be focused on these areas if resources fall below the planned levels.



Maintenance plan

Once a maintenance strategy has been developed for an asset, it must be translated into annual maintenance plans that set out, in detail, the maintenance tasks to be performed each year.

The maintenance plan provides a basis for managing the work and for monitoring maintenance performance. It should

set out the maintenance requirements of assets, broken down into individual components, systems or elements when necessary. It should also include a statement of resources, which details such information as:

- › the resources required to undertake the maintenance function, including its planning and management;
- › the expected number and type of maintenance contracts and suppliers; and
- › the expected funds sources for both capital and recurrent costs over the period (sources of funds could include recoveries from user charges and other sources as well as funds appropriated in the budget).

Maintenance data need to be captured as work is performed, with records being kept of maintenance history for planning purposes. As appropriate, such data should also be used to prepare the annual maintenance plan.

Criteria for assessing maintenance performance

The outcomes of effective asset maintenance include:

- › a long-term reduction in life cycle costs;
- › better asset performance and service;
- › the optimisation of asset life; and
- › improved public perception of the asset's service and safety standards.

These outcomes can generally be monitored and reported through the use of performance measures.

Typical indicators can be derived from such measures as the asset's availability, its operational performance in relation to service delivery, its energy consumption, its operating costs, and user satisfaction. Many of these indicators can be benchmarked against other like assets.

Assessing the Condition of Constructed Assets.

Department of Planning and Development, Office of Building, 1995

Department of Planning and Development, Office of Building
Telephone 61 3) 9651 5800



7.1 Asset information requirements

Property is necessary, but it is not necessary that it should remain for ever in the same hands.

Rémy de Gourmont

Figure 2.8
Asset life cycle: the disposal stage

Decisions to dispose of an asset require thorough examination and economic appraisal. Like acquisition decisions (see Section 4), they must be taken within an integrated planning framework that takes account of service delivery needs, corporate objectives, financial and budgetary constraints and the Government's overall resource allocation objectives.

Disposal options, which include alternative use, rental, sale, or sale and lease-back, should be considered as part of the acquisition strategy.

Asset disposal terminates control of a particular asset, but may generate the need for a replacement to support the continuing delivery of services.

Disposal is therefore a crucial component of the asset management life cycle (see Figure 2.8).



Entities are to:

- evaluate the effectiveness of their redeployment/disposal strategies in maintaining an asset portfolio that best meets service needs; and
- establish arrangements for the decommissioning of assets and for underperforming or surplus assets as efficiently as possible, prior to redeployment or disposal.¹²

Asset disposal decisions are to be made within an integrated service and financial planning framework. The following guidelines are provided to help entities dispose of their assets in an accountable manner. Entities should:

- establish and maintain an asset information system, which records all relevant information, to assist in asset planning and management;
- prepare and evaluate proper costing to support the selection of the most cost-effective disposal methods;
- identify those areas most susceptible to fraud or risks, and introduce appropriate preventive measures;
- identify and communicate the preferred arrangements for disposals to relevant staff;
- engage experts to develop the terms of contract and to assist in preparing the contract (particularly for complex and non-standard disposals) to minimise the exposure to risk;
- provide clear instructions to the agent engaged to undertake the disposal; and
- monitor and evaluate disposal performance regularly for achievement, fair dealing, cost-effective choice of disposal methods and for compliance with the Government's disposal policies and objectives.

Different disposal methods will be needed for different types of assets. Auctions, for example, may not be appropriate to dispose of some classes of assets. Before deciding on a particular disposal method, the following matters should be considered:

- the nature of the asset (ie a specialised asset or a common item);
- its potential market value;
- other intrinsic value of the asset (ie cultural/heritage aspects etc);

- its location (with respect to its transportation or access);
- its volume;
- its trade-in value;
- its ability to support wider Government programs;
- environmental considerations;
- market conditions; and
- the asset's life.

Appropriate means of disposal may include:

- public auction;
- public tender;
- transfer to another entity;
- sale to another entity;
- sale to staff;
- trade-in; and
- controlled dumping (for items that have a low value or are unhygienic).

Professional valuations play an important role in asset disposal (see Section 7). They can help managers to select the most appropriate selling method. They also

help to set realistic expectations for the sale. If they are required, valuations must be obtained from experienced agents who have a knowledge of the type of asset(s) for sale and the current market trends. The Office of the Valuer-General can offer advice in this respect.

Supply Policies and Guidelines

Victorian Government Purchasing Board, 1995

Department of Treasury and Finance,
Victorian Government Property Group
Telephone 61 3) 9651 2496

Victorian Government Purchasing Board
Telephone 61 3) 9651 3008



Disposal of land

As indicated in Section 4, land includes all improvements of a permanent nature (ie buildings, infrastructure etc) constructed on the land. Laws and procedures relating to the disposal of land will therefore also cover the disposal of such improvements.

Crown land

Only the Minister for Finance may dispose of Crown land. Disposal must be in accordance with the provisions of the *Land Act 1958*. Where improvements in which the Crown has no financial interest are constructed on Crown land (eg a local Water Board residence), the practice has been to share the proceeds of sale between the Crown and the entity that has the financial interest in the improvements.

Other land (freehold land)

Land, other than Crown land, must be sold in accordance with the relevant legislative requirements. For example, the Acts listed below govern disposal of assets by entities within the portfolios stated:

Conservation and Natural Resources
Conservation Forests and Lands Act 1987

Education
Education Act 1958

Equity in any land improvements established under such arrangements as joint venture, licence or lease must be considered when disposing of land. For example, the following issues may be applicable:

- *Joint venture*: The partner's costs may need to be reimbursed.
- *Licence*: The licensee may be required to remove all improvements.
- *Lease*: The lessee may have to make good or restore the site to its pre-leased state.

Conservation Forests and Lands Act 1987
Education Act 1958
Government Employee Housing Act 1981
Housing Act 1983
Land Act 1958
Project Development and Construction Management Act 1994
Transport Act 1983
Urban Land Authority Act 1979

Various other Acts with development and building provisions.

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Disposal of other assets

With the exception of land and constructed assets, the disposal of assets by entities is governed by the *Financial Management Act 1994*.

The Regulations and Directions that currently apply essentially require each department to establish a Board of Survey to recommend on asset disposal and to prescribe the approval processes to be followed (based on the value of the assets to be disposed of).

Financial Management Act 1994

Supply Policies and Guidelines
Victorian Government Purchasing Board,
1995

Victorian Government Purchasing Board
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Relinquishing control of an asset

An entity ceases to be responsible for managing an asset when it relinquishes control of that asset. This may occur in a number of ways:

- » in some instances, an entity may elect to do so;
- » in others, it is unable to exercise any discretion in the matter.

For example, an entity may choose to sell or transfer the asset or to give it away. On the other hand, an asset may be lost or stolen, accidentally destroyed (eg in a fire), forfeited, or resumed by the Commonwealth.

Not all of these means of relinquishing control of an asset apply to all classes of assets, or are available to all entities.

Directions of the Minister for Finance under the *Financial Management Act 1994*

Project Development and Construction Management Act 1994

Recognition and Reporting of Crown Land by Government Entities
Public Sector Accounting Centre of Excellence, 1995

Recognition and Valuation of Non-current Physical Assets
Department of Finance (Victoria), 1995

Supply Policies and Guidelines
Victorian Government Purchasing Board, 1995

Accounting
Department of Treasury and Finance,
Accounting and Financial Reporting
Division
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Construction of assets
Department of Planning and
Development, Office of Building
Telephone 61 3) 9651 5800

Land
Department of Conservation and Natural
Resources, Crown Land and Asset
Division
Telephone 61 3) 9412 4406

Department of Treasury and Finance,
Victorian Government Property Group
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Department of Planning and
Development, Office of Building
Telephone 61 3) 9651 5800

Other assets
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*Knowledge is of two kinds. We know
a subject ourselves, or we know where
we can find information upon it.*

Samuel Johnson

Entities must make informed decisions about the assets they control if they are to be properly accountable for the physical and financial performance of those assets. They cannot do this effectively if they do not have ready access to the necessary information.

Accurate recording, valuation and reporting procedures are therefore needed so that decisions to modify, rehabilitate, find an alternative use for, or dispose of an asset can be soundly based. Some information has to be kept to meet statutory requirements, while additional data should be kept as part of good asset management practice.

Comprehensive information about assets can generate large amounts of data. Entities must define their minimum information requirements, and implement an effective information management strategy to ensure that information needed (and only that information) is generated, and that the necessary controls are in place.

Comprehensive, accurate and up-to-date information on assets is vital to effective asset planning. Good information is necessary to:

- » support sound decisions about assets relating to service delivery capacity, acquisition, maintenance and disposal; and
- » comply with statutory financial reporting obligations.

Information generated about assets must match the decision-making purpose (see below) for which it is required:

Strategic decisions: These generally require small amounts of information about a range of issues and asset characteristics related to trends, rather than specific data about individual assets. In this situation, the level of accuracy is of less importance than completeness. Approximations or proxy information are often acceptable for these decision-making purposes.

Tactical decisions: These require a broader range of information, and at a greater level of detail. The level of accuracy of the data required depends on the criticality of the decisions to be made.

Operational decisions: These tend to require source data with high levels of accuracy as the information supports day-to-day decisions by individual staff in the field. Operational data are the prime sources of aggregated information for tactical and strategic purposes.



Asset information systems

Entities are to maintain asset registers in accordance with the Department of Treasury and Finance guidelines in order to facilitate the implementation of appropriate portfolio and risk management strategies across the budget sector.¹³



Asset information systems use a database of asset information known as an 'asset register'. For a register to fully support effective decision-making about asset utilisation, it must:

- › be comprehensive, and include all assets under the control of the entity;
- › be structured in a way that allows different classifications of assets to be distinguished, and treated appropriately. For example, assets such as buildings and plant may have a long life and complex maintenance requirements. These may be recorded in a specialised section of the asset register which contains more information than the section used to record furniture and office equipment;
- › capture details of all transactions affecting the assets, as they occur;
- › have associated procedures, controls and audit trails to maintain the integrity of the information;
- › identify the individual or organisational unit accountable for the asset and the location of the asset; and
- › carry the financial information needed for statutory reporting.

Information in the asset register must be readily accessible to individuals who are accountable for the control and management of a nominated asset or group of assets, preferably on a 'real-time' basis.

Entities may elect to use separate asset registers for different classes or categories of assets. If this course is taken, common data standards should be employed so that consistent consolidated reports on assets can be readily prepared for the entity as a whole.

Asset performance data

Asset registers should have provision for recording performance data for individual assets. As examples, useful performance data may include:

- › measures of the operational performance of the asset in relation to its service delivery objectives (as revealed by performance indicators for the quality of the service delivered by using the asset);
- › measures of how intensively the asset is utilised (to disclose any surplus capacity that could be taken up for other purposes); and
- › operating costs (to include, for example, cleaning and energy costs and maintenance expenditure).

The information should be appraised by entities against best practice data to establish whether assets are being managed effectively.

Asset Management Catalogue of Reference.

Victorian Government, 1995

Asset Management Principles

Victorian Government, 1995

Australian Accounting Standard 29 – Financial Reporting by Government Departments

Australian Accounting Research Foundation

Financial Management Act 1994

Department of Treasury and Finance,
Accounting and Financial Reporting
Division

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Responsibilities

Within entities, accountability for assets will normally be devolved to the business units responsible for the delivery of the service that the asset supports. Asset details should be captured and reported at this level. Individual managers may then monitor and manage the utilisation and maintenance of the assets assigned to their control.

Details of individual assets must be capable of being consolidated and summarised

for financial reporting purposes, and for co-ordinated portfolio management.

If more than one asset register is used within an entity, common data standards should be employed to assist in consolidating the data.

Recording threshold

Entities are required to set a minimum monetary threshold for the recording and financial reporting of assets. Effort on these activities is then limited to those assets whose value is of significance to service delivery objectives and is above the threshold. This approach can achieve significant administrative savings.

The principal consideration in setting a threshold is whether the omission of those assets whose value is below the threshold would materially affect the quality and usefulness of the information derived. In the absence of a conscious decision to the contrary, entities must maintain an asset register for all non-current physical assets that have a value above a threshold level of \$1,000.

Entities may elect to use a higher threshold to meet their individual requirements, but must be prepared to justify their decision.

Portable and/or attractive assets

Some items whose value falls below the threshold level but which otherwise qualify as significant assets should be recorded and tracked either for control or security reasons, or to meet other management requirements. Such items may be classified as 'portable and/or attractive'.

They are recorded in the asset register but excluded from the entity's annual financial statements. (This exclusion does not mean that they are less important to the entity, but only that full accounting treatment is not warranted.)

Core and non-core assets

The terms 'core assets' and 'non-core assets' are used to distinguish assets that are central to the obligations of Government from those that are not.

An asset is classified as 'core' where it is:

- necessary for the ongoing delivery of a service required by Government; and
- publicly owned, and not readily replaced with a private sector alternative; or
- retained for heritage or conservation reasons.

An asset is classified as 'non-core' where it is:

- intended not to be replaced if lost because it is not required for the long-term service output of the entity; or
- identified as surplus and awaiting disposal or redeployment.

Grouping of assets

Recording of assets should generally be on an asset-by-asset basis. In some cases, however, it may be more appropriate to record a group of interrelated assets (of which some or all of the components may have a value below the recording threshold). Examples include a major piece of machinery with a number of sub-assemblies, or an infrastructure asset such as a services network. The asset register should record the grouped asset, and identify the individual components.

Unlike assets that are aggregated for convenience (see below), a group of assets attracts particular value because it represents a complete collection (eg a suite of furniture, a set of crockery, or a services network). Loss or removal of one item would significantly diminish the value of the group or collection by making it incomplete. This would apply even if the value of the particular item were relatively low. (This contrasts with an aggregation of assets where the loss or removal of one item may have negligible effect on the total value of the aggregated assets.)

Aggregation of assets

Some entities have large numbers of homogeneous assets which have complementary values (such as library books, or a collection of scientific material). In such cases, the assets may be recorded in aggregate. As for assets that are grouped, this approach will be useful where the value of the components of an individual asset may fall under the recording threshold, but the aggregate value of the 'asset' is above the threshold.

Aggregation should not be used for assets that have fundamentally different characteristics as this will result in inconsistent assumptions about useful life and depreciation.



8.2 Charging for the use of assets

Asset data must be kept up to date. Data on transactions affecting assets should be captured as the transactions occur, and entered in the asset register. Wherever possible, data transfers should take place electronically, and not rely on discretionary actions or anecdotal evidence.

Asset data at acquisition

Records for newly acquired assets should be captured from the purchasing system at the time of purchase or acquisition, and the initial valuation of the asset should be taken as the cost of acquisition.

In this context, 'cost of acquisition' means the actual purchase price, plus any costs incidental to the acquisition.

All costs attributable to the purchase or construction activity should be capitalised and included in the acquisition cost. This includes such costs as design fees, agent's commission, the cost of import licences, freight and the like.

Expenditure on existing assets

Expenditure on an existing asset that increases its service potential is treated as capital expenditure, and must be recorded either as:

- an addition to the value of the existing asset; or
- a new asset, linked to the existing asset.

Normal maintenance expenditure must also be recorded as an operating expense. Maintenance work should be initiated by a 'Work Order' or equivalent, and used to collect the costs and to prepare a history record of work completed. The asset register or a specialised maintenance management system may be used for the purpose.

Maintenance history is important for forward maintenance planning and budgeting purposes, and care should be exercised to identify and retain appropriate data.

Stocktaking

Stocktakes of assets must be carried out at periodic intervals – normally annually – with the results being reconciled with the records in the asset register.

The stocktake frequency may be modified or supplemented by a sampling approach at the discretion of the entity controlling the assets.

Barcoding, or similar optical recognition techniques, may be utilised for stocktaking purposes to introduce higher levels of accuracy and to reduce asset management costs.

The valuation of assets is undertaken for a number of purposes. For example, the valuation of an asset may be used to:

- generate the information needed for internal control, resource allocation and performance assessment;
- establish the basis for asset realisation;
- determine insurance cover and risk exposure; and
- meet requirements for external financial reporting.

Choice of an appropriate valuation method depends firstly on the purpose of the valuation, and secondly on the nature of the asset involved. The initial valuation is applied at the time of acquisition, and generally corresponds to the cost of acquisition. Subsequent revaluations are undertaken at periodic intervals with a frequency chosen to reflect the nature of the class of assets concerned.

Valuation methods used should be in accordance with the guidelines issued by the Department of Finance publication, *Recognition and Valuation of Non-current Physical Assets*.

A description of the approach to be taken to depreciation is provided in Section 2 of that publication.

Valuation of core and non-core assets

It is necessary to distinguish between core and non-core assets in determining valuations.

A non-core asset is to be valued at its net realisable value, which is the current market value net of all costs involved with disposing or redeploying the asset.

A core asset should, in general, be valued at the cost of replacing the service potential remaining in the asset. If a viable market exists for the asset, a core asset



is to be valued at its current market price. If a market for the asset does not exist, a core asset is to be valued at its written-down replacement cost.

Valuation of heritage/cultural assets

True valuation may be difficult to obtain for assets retained for heritage or conservation purposes.

Heritage assets have two components of value: a market-related value and an aesthetic or social value. The aesthetic or social component will probably not be reflected, in part or in full, in the asset's current market value.

Entities should refer to Section 9.8 of the *Accrual Accounting Manual* issued by the Department of Treasury and Finance for guidelines on how to value heritage or cultural assets. A note to the entity's annual financial statements should mention that the asset's true worth to the State is probably only partly reflected in its reported value.

If an entity has difficulty in establishing a reliable measure of a heritage or cultural asset's value, it must notify the Department of Treasury and Finance. Insurance and risk management issues must be considered. Entities must also provide narrative information in the notes to their financial statements on heritage assets.

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Asset revaluation

Entities must establish a program to revalue assets every five years and to review these annually. The review should include consideration of the asset's current condition, required maintenance and estimated remaining useful life.

Australian Accounting Standard 10 – Accounting for Revaluation of Non-current Assets
Australian Accounting Research
Foundation

Recognition and Valuation of Non-current Physical Assets
Department of Finance (Victoria), 1995

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We must look at the price system as... a mechanism for communicating information if we want to understand its real function.

Friedrich August von Hayek

Entities must know the full costs of assets that they control. This information is needed to review the performance of the asset itself, and to compute the costs of the service to which the asset contributes.

Pricing determines the charges to be made when an asset is used to support provision of a service to others, either within the entity or externally.

The policies and practices in this chapter are set in the context of the Government's move to manage its entities according to commercial principles.

Knowledge of costs incurred in using assets is critical to their effective management. Asset costs are used to:

- › set operational budgets and targets for management control;
- › monitor asset and program performance;
- › evaluate capital projects; and
- › set a basis to establish prices – the charges to be made to others for the use of the asset.

Costing systems

Asset costs and corporate systems

The costing of assets should take place in concert with the costing of other components of service delivery. Corporate costing systems should be designed with this in mind, and be able to capture the costs of assets on a whole-of-life basis, as well as the full costs of the service to which they contribute. This may require the ability to attribute portions of indirect and corporate overhead costs to individual assets.

Entities should apply an activity-based costing approach so that specific services and components of the services can have realistic costs ascribed to them.

Full costs and depreciation

Most physical assets – other than land – deteriorate with time and use.

Depreciation recognises this as a cost, even though it may not immediately incur a cash expense. In accounting terms, the use of an asset results in a progressive loss of 'service potential', and has to be recorded as a cost.

The benefit obtained from the use of the asset is recognised in each accounting period by a depreciation expense.

The full costing of services that use assets must include this expense, in addition to the other operational costs of asset use.

Life cycle costs

Life cycle costing is used to establish the full costs of controlling and operating an asset over its life, or for the period it is controlled by the entity.

Life cycle costs have three basic components:

- ▶ *Capital costs:* These include the costs associated with the initial acquisition of an asset, either by way of purchase, construction or commissioning, as well as enhancement costs.
- ▶ *Ongoing or recurrent costs:* These include all costs incurred in the course of holding and operating the asset (such as management, finance refurbishment and operating costs such as energy and maintenance).
- ▶ *Salvage and disposal costs:* These costs are reflected as offsets against asset sale value and translate to 'residual value'.

Depreciation needs to be computed in a way that recognises the initial capital cost, the expected life, and the residual value at the end of the asset's useful life. All costs over the whole-of-life cycle need to be considered when evaluating the full costs of an asset, since continuing operational costs can accumulate to exceed the initial capital costs in a relatively short time.

Life cycle costing provides a profile against which alternatives to owning and constructing assets can be examined.

It also provides a means of monitoring actual cost performance, and can assist entities in making future decisions on asset design and acquisition.

Many of the life cycle costs incurred or to be incurred by an asset can be found in the entity's accounting system, but some items (such as projected future maintenance costs) may require separate studies, estimates or approximations. Opportunity costs should be included where relevant.

Asset costs

Several types of cost must be recognised and measured in order to determine the full cost of an asset. The use of accrual accounting allows all costs incurred to be measured, even though the associated cash transactions may not have taken place.

Three types of costs can be identified:

Direct costs: These costs can be specifically assigned, and are directly attributable to a particular asset. Examples include depreciation, utility costs, maintenance charges, statutory charges and taxes, cleaning and finance costs.

Indirect costs: These costs are attributable only to the total asset base, to a specific group of assets, or to the asset indirectly. Wherever possible, indirect costs need to be allocated to individual assets in a meaningful way.

The attribution of indirect costs requires a causal relationship between the cost and the asset. For example, the capital charge may be allocated in proportion to the value of the asset, or rental costs may be allocated according to the floor space occupied. Other indirect costs, for instance, are regional management service charges, insurance costs and other expenses associated with the management and operation of assets or asset groups.

Overhead costs: These costs are generally related to the assets but cannot be identified with a specific asset or asset portfolio (eg the corporate overhead associated with an entity). If an asset is controlled by a particular region, it may be appropriate to apportion the overhead costs of that region but not those of the head office.

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Charging for asset use brings a number of benefits:

- » The level of pricing can be used to modify or suppress demand for the service that the asset supports, or for the asset itself. Realistic pricing can also encourage the search for more efficient solutions to the service requirement.
- » Resources are allocated more effectively.
- » Some or all of the costs of operating the asset can be recovered (depending on the pricing policy).
- » More realistic costs are available, for comparison with other sources of the service.
- » Benchmarking and comparisons with the private sector become possible.

The price set when an asset is to be used by another party should, in most instances, reflect at least the full cost of the asset (or the services it provides). This cost should reflect the capital charge attributable to the asset, the operating and maintenance expenditure, and depreciation.

Entities may hire or lease assets (or the services they provide) under a number of different circumstances. Assets may, for example, be provided for use to another party within the public sector or to a private sector party, as well as to users within the entity itself.

In allowing other parties to use assets for which it is responsible, the entity must develop suitable charging arrangements. Generally, all charges should be set to recover full costs, and the same charge should be applied for all users. An entity does, however, have a number of options for cost components when setting charges – these are described in ‘Pricing Models’ below.

In setting charges, the entity needs to understand the total cost structure of the asset and the service that it supports. Such information will clearly highlight issues such as cross-subsidisation in the provision of services. It will also help the entity to develop policies for use of the asset in different circumstances.