Constructed Assets

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The cost of a capital asset includes direct construction or development costs (such as materials and labour) attributed to the acquisition, construction, or development of the asset. There are four stages related to acquisition/construction of assets: preliminary, pre-acquisition, acquisition or construction and in-service.

Preliminary Stage

During the preliminary stage activities include exploration of various opportunities for acquisition or construction of an asset, i.e. business case, feasibility studies.

All related costs (direct and overhead) of the preliminary stage should be expensed.

Pre-acquisition Stage

During the **pre-acquisition** stage some of the activities and costs may be similar to those incurred during the preliminary stage except, in the pre-acquisition stage they occur after it is probable that the asset will be acquired or constructed (approval has been received, funds committed).

Directly identifiable asset costs related to the pre-acquisition stage should be capitalized. All other related costs should be expensed.

Directly identifiable costs would include:

a) ***Incremental direct costs*** of asset pre-acquisition activities incurred in transactions with independent third parties. i.e. consultant fees, design and engineering fees, survey costs.
b) Certain costs directly related to pre-acquisition activities performed by the NBCC component for the specific asset. Those costs include **only** payroll, related payroll benefits and travel costs of employee(s) who devote time to the asset's pre-acquisition stage activity, to the extent of time the employee(s) spent directly on that activity and in proportion to the total hours employed.
c) Incremental direct costs of asset pre-acquisition activities **does not** include rent, depreciation and other occupancy costs associated with the physical space occupied by employees. *These costs should be expensed*.

Capitalized pre-acquisition stage costs should be included in the cost of the specific asset upon its acquisition. If it becomes no longer probable that the asset will be acquired, the pre-acquisition stage costs previously capitalized related to this asset should be reduced to the lower of cost or fair market value less cost to sell. A presumption exists that the fair value of those pre-acquisition stage costs is zero (that is, the costs of the asset would be charged to expense), unless management, having the authority to approve the action, has committed to a plan to sell the asset and the proceeds can be reasonably estimated.

Acquisition or Construction Stage

The third stage, the **acquisition or construction** stage, begins at the time the NBCC component obtains ownership of the asset (asset is received by the NBCC component or legal ownership of the asset has passed from the seller to the NBCC component) or obtains the right to use the asset through an agreement (i.e. lease). Activities include planning for construction or installation once ownership, or the right to use, has been acquired; constructing or installing the asset, costs incurred to get land in condition for its intended purpose, assumption of any liens and supervising the construction or acquisition of the asset.

Directly identifiable asset costs related to the acquisition or construction stage should be capitalized. All other related costs should be expensed.

Directly identifiable costs would include:

a) ***Incremental direct costs*** of acquiring, constructing, or installing the asset incurred in transactions with independent third parties for the specific asset.

b) Certain costs directly related to specified activities performed by the NBCC component for the acquisition, construction, or installation of the specific asset, that are necessary to get the asset ready for its intended use. Those costs include only:

   i. Payroll, related payroll benefits and travel costs of employees who devote time to an asset's acquisition or construction stage activity, to the extent of time the employee spent directly on that activity and in proportion to the total hours employed;

   ii. Depreciation of machinery and equipment used directly in the construction or installation of an asset, to the extent of time the machinery and equipment is used directly in that activity as a percentage of its expected useful life, and incremental costs (such as fuel for machinery) directly associated with the utilization of that machinery and equipment; and

   iii. Inventory (including spare parts) used directly in the construction or installation of the asset.

c) Incremental direct costs of asset acquisition-or-construction stage does not include rent, depreciation and other occupancy costs associated with the physical space occupied by employees. *These costs would be expensed.*

When the asset is substantially complete (97% complete) and ready for its intended use, all expenses associated with the asset should be recognized in operations as they accrue and depreciation should begin.

Proceeds obtained in the process of getting an asset ready for its intended use, i.e. receipts from sale of timber that has been cleared or salvage proceeds from sale of structure(s) on land at time of purchase, should reduce the land price.

Demolition costs incurred should be charged to expense as incurred and included in results of operations, **except** when incurred in conjunction with an acquisition of real estate and the demolition:

a) is contemplated as part of the acquisition; and

b) occurs within a reasonable period of time or is delayed, but the delay is beyond the NBCC component's control.

Demolition costs meeting the above criteria should be capitalized as part of the cost of the real estate. Whether the demolition costs are capitalized as land or building depends on the nature of the costs. For example, costs related to the demolition of a building in preparation for new construction would be capitalized as part of the land, whereas costs related to gutting the interior of a warehouse in preparation for reconstructing the interior as office space would be capitalized as part of the building.

In-service Stage

The fourth and final stage, the **in-service** stage, commences when the asset is substantially complete and ready for its intended use. Costs incurred during this stage relate principally to replacements of existing components, acquisition of additional components, repairs and maintenance and relocation costs.

The costs of normal, recurring, or periodic repairs and maintenance activities and all other costs related to the asset that are incurred during the in-service stage should be expensed as incurred **unless** the costs are incurred for:

a) the acquisition of additional components of the asset or

b) the substitution of a better component for the one currently in use

The removal costs, except for certain demolition costs – previously discussed, incurred in conjunction with the replacement of an asset should be expensed. Costs incurred to relocate an existing asset, or a component of an existing asset should be expensed as incurred.

General and Administration Costs and Overhead Costs

General and administration costs and overhead costs incurred by the NBCC component should be charged to ***expense as incurred***. Those costs include rent, depreciation, and other occupancy costs associated with the physical space occupied by employees and all costs of support functions, which include executive management, corporate accounting, acquisition and purchasing, corporate legal, office management and administration, marketing, human resources, and information systems.

Incremental direct costs incurred in transactions with an independent third party that are capitalized often include an element of the third party's administrative overhead. That element is considered to be an incremental direct cost.

General and administrative costs and overhead costs should be expensed as incurred whether incurred internally by the NBCC component or incurred by another enterprise on behalf of the entity. For example, an entity that outsources its information systems services to a third party should charge the costs to expense as incurred because information systems represent a support function, and the entity could choose to establish its own internal information systems branch.