

TREASURER'S DIRECTIONS

ACCOUNTING – ASSETS

Section A2.11 : Construction (Work in Progress)

STATEMENT OF INTENT

Costs associated with the construction or development of an asset can be significant and should be completely and accurately recorded. This Section explains concepts relating to the recognition and measurement of work in progress associated with the construction or development of assets.

MAIN FEATURES

Section 38 of the *Financial Management Act* requires every Accountable Officer and every employee of an Agency to comply with the Treasurer's Directions.

Construction (Work in Progress)

- Construction (Work in Progress) represents the cost of work performed in the construction or development of a non-current asset.

Recognition of Construction (Work in Progress)

- Construction or development costs are to be recognised as Construction (Work in Progress) where they meet the asset recognition and capitalisation criteria.
- Construction (Work in Progress) will be recognised by the Agency who manages the construction or development of an asset, with the exception of the Darwin Port Corporation who will record Construction (Work in Progress) related to its assets.
- Construction (Work in Progress) includes materials, labour and overhead costs that are either directly related or allocated to the construction or development of an asset.

Classification of Construction (Work in Progress)

- Construction (Work in Progress) is to be recorded in the classes provided by the Standard Classification Codes.

Recognition and Recording on Asset Completion

- On completion of construction works, costs associated with the construction or development of an asset are to be transferred to the Agency that will control the completed asset. Construction (Work in Progress) will subsequently be transferred to the relevant non-current asset class when the asset is completed and held ready for use.

For authoritative instruction and guidance, reference should be made to related Treasurer's Directions and associated commentary, relevant Australian accounting standards and other authoritative interpretations.

CONTENTS

What is Construction (Work in Progress) ?	A2.11.1
Recognition and Recording of Construction (Work in Progress)	A2.11.2
Classification of Construction (Work in Progress)	A2.11.6
Recognition and Recording on Asset Completion	A2.11.7
<u>Appendix A</u> Recording of Construction (Work in Progress) – Flowchart	
<u>Appendix B</u> Accounting for Construction (Work in Progress) – Examples	

AUTHORITIES

Financial Management Act

REFERENCES

AAS 29	Financial Reporting by Government Departments
AASB 116	Property, Plant and Equipment
	Capital Construction Principles
	Works Programming Procedures
<i>Related Treasurer's Directions:</i>	
A2.1	Accounting – Assets : Overview
A2.2	Accounting – Assets : Property, Plant and Equipment
A2.3	Accounting – Assets : Depreciation and Amortisation
A2.4	Accounting – Assets : Revaluation
A2.5	Accounting – Assets : Improvements and Repairs and Maintenance
A2.9	Accounting – Assets : Prepayments
A2.10	Accounting – Assets : Impairment of Assets
A4.2	Accounting – Equity : Owner Actions
C3.2	Cash Management – Transaction Management : Payments

WHAT IS CONSTRUCTION (WORK IN PROGRESS) ?

A2.11.1

Construction (Work in Progress) represents the cost of work performed in the construction or development of a non-current asset.

- (i) Some assets are constructed or developed over extended periods of time. Other assets may require extensive installation work or integration with other assets. During these processes such assets are referred to as Construction (Work in Progress). Examples include the construction or development of buildings, infrastructure assets and specialised equipment.
- (ii) These types of assets contrast with simpler Agency assets that are ready and available for use when acquired, such as office equipment.
- (iii) Construction (WIP) may relate to the construction, development or installation of a new asset or works that result in an improvement to an existing asset. Concepts relating to assets and improvements are provided in Treasurer's Directions Sections A2.1 and A2.5 respectively.
- (iv) Although Construction (WIP) is recorded as a non-current asset, it is not depreciated or subject to revaluation requirements until the asset is complete and first put into use or held ready for use by the relevant Agency. Treasurer's Direction A2.11.11 provides further instruction and guidance in relation to the depreciation, revaluation and write-down of Construction (WIP).
- (v) Funding and approval for construction of a capital nature is provided through the Territory Capital Works Program. The Works Programming Procedures and Capital Construction Principles provide additional instruction and guidance in relation to the formulation, implementation and variations to the Territory's works programs.

RECOGNITION AND RECORDING OF CONSTRUCTION (WORK IN PROGRESS)

A2.11.2

Construction or development costs are to be recognised as Construction (Work in Progress) where they meet the asset recognition and capitalisation criteria.

A2.11.3

Subject to Treasurer's Direction A2.11.2, Construction (Work in Progress) related to Territory or Agency assets is to be recognised and recorded by the:

- Department of Construction and Infrastructure, where works relating to the construction or development of Territory or Agency assets are managed by that Department;
- relevant Agency, where works relating to the construction or development of assets are managed by that Agency; or
- Darwin Port Corporation for works relating to the construction or development of Corporation assets.

Section A2.11 : Assets – Construction (Work in Progress)

- (i) Material construction and development costs will be recognised as assets where those costs meet the asset recognition criteria and the property, plant and equipment capitalisation threshold. Treasurer's Directions Sections A2.1 and A2.2 provide instruction and guidance in relation to asset recognition and capitalisation.
- (ii) Where the cost of the completed asset or asset improvement works is expected to be less than \$10,000, construction and development costs will be expensed in the Operating Statement of the relevant Agency in the reporting period in which they are incurred.
- (iii) The Department of Construction and Infrastructure (DCI) centrally manages the vast majority of construction and development works on behalf of Agencies. Capital Appropriation for Capital Works is also provided directly to DCI. The exception is Agencies who manage their own construction or development works.
- (iv) As part of these transitional arrangements, the cost of construction or development of assets will be recorded as Construction (WIP) by DCI until the works associated with that asset are complete. For example, Construction (WIP) associated with the construction of a new health centre will be recorded by DCI until the asset works are complete and not by the Agency providing health services.
- (v) Agencies that manage their own works will recognise costs incurred, on the construction or development of an asset as Construction (WIP), in their Agency's ledger.
- (vi) Darwin Port Corporation will also recognise the cost of Construction (WIP) for assets under its control in its ledger even though the construction or development works may in practice be managed by DCI.

A2.11.4

Construction costs are to be recognised as Construction (Work in Progress) in the reporting period in which the construction activity is performed.

- (i) Construction costs are recognised at the time the related construction activity is performed. In many situations this will be with reference to the stage of completion of the construction. From a practical point of view, assessment of the stage of completion should take into account significant cost components rather than seeking to account for individual cost components.
- (ii) The stage of completion of construction may be determined in a variety of ways including by:
 - reference to an architect's certificate or survey of work performed;
 - progress bills received; or
 - determining the proportion of physical work performed to date and comparing this to the estimated total physical work required to complete the construction or development of the asset.

Section A2.11 : Assets – Construction (Work in Progress)

- (iii) Construction or development costs that relate to future activities, including any advance payments do not reflect work performed and therefore are not part of Construction (WIP). Accordingly, materials purchased for use in construction but not used at the reporting date are not included in the cost of work performed to date.
- (iv) Payments made prior to the completion of a particular stage of construction or development will be recognised as prepayments rather than Construction (WIP). Treasurer's Directions Sections A2.9 and C3.2 provide further instruction and guidance in relation to prepayments and payments in general.

A2.11.5

Construction (Work in Progress) includes materials, labour and overhead costs that are either directly related or allocated to the construction or development of an asset.

- (i) Construction (WIP) includes costs that are directly related or allocated to the construction or development of an asset. These costs will provide the Government and Agencies with a clear idea of the complete cost associated with the construction or development of an asset.
- (ii) Construction (WIP) costs may include:
- costs of materials arising from direct purchases from suppliers or allocated based on appropriate costing principles such as first-in-first-out;
 - labour costs allocated on the basis of time spent on the project; and
 - overhead costs that can either be directly assigned to the project or allocated in accordance with material costs, labour costs or other reasonable basis.
- (iii) Overhead costs may include:
- building permits and tender development costs;
 - costs incurred under contracts with third parties and progress bills paid or owing during construction including architect's fees and engineer's fees;
 - site preparation, demolition works and excavation for foundations;
 - depreciation or hire charges for equipment used in construction;
 - telephone and power bills; and
 - management and supervision charges (for example, Construction Division management fees associated with managing the capital works project).
- (iv) While it is important that the full cost of Construction (WIP) is recognised in the correct reporting period, some cost information may not be administratively effective to collect. Agencies should therefore remain aware of the administrative costs and materiality of collecting Construction (WIP) information.

CLASSIFICATION OF CONSTRUCTION (WORK IN PROGRESS)

A2.11.6

Construction (Work in Progress) is to be recorded in the following classes provided by the Standard Classification Codes:

- NT Government Capital Works Program (Work in Progress);
- Recoverable Works Projects (Work in Progress); or
- Non-Government Works (liability account).

- (i) There are three categories for Construction (WIP) provided in the Standard Classifications:
- NT Government Capital Works Program (WIP) – includes projects forming part of the Territory's approved capital works programs, in which the resulting asset(s) will be owned or controlled by a Territory Agency upon completion;
 - Recoverable Works Projects (WIP) – includes projects where funding is from sources external to the Government, but the resulting asset(s) will be owned or controlled by a Territory Agency upon completion; or
 - Non-Government Works (liability account) – includes transactions associated with projects where funding is from sources external to the Government, but the resulting asset(s) will not become a Territory asset upon completion.
- (ii) Agencies should be aware that construction and development works may also be undertaken in relation to projects that are funded from sources external to Government. These projects may either result in the construction of assets that are controlled by the Territory or the construction of assets that are not owned or controlled by the Territory.
- (iii) In the case of assets that are not owned or controlled by the Territory, no asset will be recognised by an Agency or Government owned entity. The Non-Government Works standard classification code (liability account) will only be used by an Agency to hold the funds available for the construction of the asset. The Capital Construction Principles provides further instruction and guidance in relation to the accounting and budget treatment for the initial and subsequent stages of construction work projects.
- (iv) Within the Construction (WIP) and Recoverable Works Project (WIP) classes, the costs relating to the construction or development of individual Territory assets should be identifiable. This information is required for the transfer of the total cost of each asset on completion to its relevant non-current asset class, for example:
- buildings;
 - infrastructure; and
 - plant and equipment.

RECOGNITION AND RECORDING ON ASSET COMPLETION

A2.11.7

Where construction or development works are managed by the Department of Construction and Infrastructure (DCI), Construction (Work in Progress) is to be transferred from DCI to the Agency that controls the asset in the reporting period when works associated with the asset are complete.

- (i) In situations where construction or development works are managed by DCI, Construction (WIP) will be transferred to the Agency that controls the asset once construction works are complete. The completed asset will be transferred from DCI to the Agency that controls the asset at the asset's full cost of construction or development. These costs will initially be recognised as Construction (WIP) by the Agency. Treasurer's Directions Section A2.1 provides instruction and guidance in relation to the control concept.
- (ii) The recording of the full cost of the construction or development works in the Agency's Construction (WIP) account will enable the finalisation of any minor commissioning, integration or fitout works necessary before the asset is made available for use. Transfer of the full cost of construction will also provide Agency management with valuable information in relation to overall asset cost.
- (iii) The effect of the transfer of Construction (WIP) will be a reduction in assets and equity for DCI and an increase in assets and equity for the Agency receiving the completed asset. Transfers of assets between Agencies in accordance with Treasurer's Direction A2.11.7 will also impact the Government's investment interest in each Agency that is recorded in the Central Holding Authority. Accordingly, the Central Holding Authority will seek Treasurer's approval in accordance with section 36 of the *Financial Management Act* to adjust the equity of each Agency. As such, Agencies should liaise with their Treasury Financial Analyst when transfers occur. Reference should be made to Treasurer's Directions Section A4.2 for instruction and guidance in relation to equity transfers.

A2.11.8

Subject to Treasurer's Direction A2.11.9, an Agency is to transfer costs associated with construction or development of an asset from Construction (Work in Progress) to the relevant non-current asset class in a timely manner once the asset is completed and held ready for use.

A2.11.9

An Agency is only to expense costs included as Construction (Work in Progress) where they do not meet the asset recognition and capitalisation criteria.

- (i) When an asset is completed and held ready for use, costs associated with the construction or development of the asset will be transferred (in a timely manner) to the relevant non-current asset class and added to the Agency's Register of Assets. Treasurer's Directions Section A2.2 provides the requirements relating to asset registers.

- (ii) Costs incurred on existing non-current assets that are included as Construction (WIP) are classed as improvements. On completion of works these costs are added to the value of the existing asset. Treasurer's Directions Section A2.5 provides further instruction and guidance in relation to improvements.
- (iii) Costs included as Construction (WIP) that do not satisfy the asset recognition criteria and the property, plant and equipment capitalisation threshold will be expensed in the Operating Statement as repairs and maintenance, rather than being transferred to the relevant non-current asset class. Treasurer's Directions Section A2.5 provides further instruction and guidance in relation to repairs and maintenance.
- (iv) Costs included in Construction (WIP) that are expensed in accordance with Treasurer's Direction A2.11.9 are not expected to be material and as a non-cash adjustment, will not impact cash funding provided to Agencies. Where significant, Agencies should consider requesting budget adjustments (non-cash) to accurately reflect an increase in repairs and maintenance expenses and a reduction in the value of non-current assets.
- (v) Appendix A provides a flowchart depicting the recording arrangements for Construction (WIP), and Appendix B provides examples of accounting for Construction (WIP) and the expensing of certain costs.

A2.11.10

Where a construction or development project relates to a number of separately identifiable component assets, each material component may be recognised on an individual basis upon completion and not on the completion of the entire project.

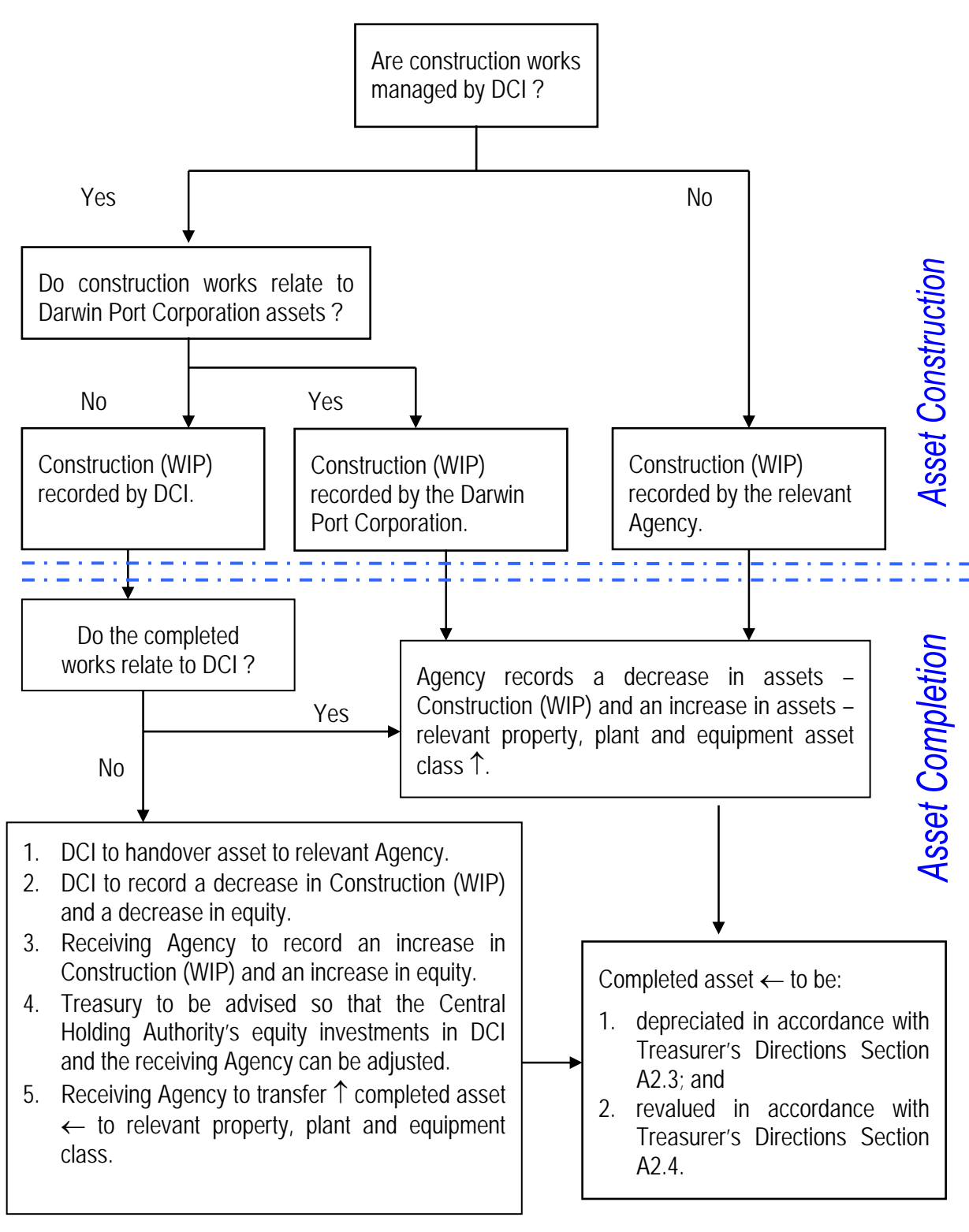
- (i) A project may involve construction or development stages that relate to a number of individually identifiable component assets or sub-projects that may be completed at different times. In these cases, it may be appropriate to transfer each component asset to the relevant non-current asset class when the individual component asset is completed and held ready for use, even though the construction of the other component assets is not complete.
- (ii) Costs incurred on the construction or development of assets will therefore need to be available for component assets where these assets are to be separately recognised. For example, where new school buildings are constructed to house a computer lab and a library, the cost of the completed computer lab will be transferred from Construction (WIP) to the building asset class when the lab building is completed and held ready for use, even though the library building may be incomplete at that time.
- (iii) From a practical point of view, Agencies will need to liaise with DCI during the planning and development phase of construction in order to facilitate the provision of cost of construction information on a sub-project basis where this information is required.

A2.11.11

Construction (Work in Progress) is not subject to depreciation or revaluation requirements.

- (i) Construction (WIP) is not depreciated. Depreciation will commence from the time the completed asset is transferred to the relevant non-current asset class and is first put into use or held ready for use by an Agency. Concepts relating to depreciation are explained in Treasurer's Directions Section A2.3.
- (ii) In addition, Construction (WIP) is not subject to revaluation requirements, with Construction (WIP) being carried at cost. Following transfer of Construction (WIP) to the relevant non-current asset class, the asset may be revalued on or before the next revaluation date for that class of assets. Agencies should remain aware that the cost of newly constructed assets will, in most cases, closely reflect the current replacement cost of that asset. Concepts relating to the revaluation of non-current assets are explained in Treasurer's Directions Section A2.4.
- (iii) It would be unusual for Construction (WIP) to be written-down, however where a write-down is required, it should not occur until reliable information in relation to total asset cost and asset value on completion are available. Requirements relating to the write-down and the impairment of assets are provided in Treasurer's Directions Sections A2.4 and A2.10 respectively.

RECORDING OF CONSTRUCTION (WORK IN PROGRESS)



← Once the asset is completed and held ready for use

↑ Subject to costs meeting the asset recognition and capitalisation criteria. Costs not meeting these criteria are expensed.

APPENDIX B

ACCOUNTING FOR CONSTRUCTION (WORK IN PROGRESS) – EXAMPLES

1. DCI manages and records Construction (Work in Progress)

DCI enters into a contract for the construction of a building for Agency B, for \$5.5 million (inclusive of GST and management fees). The construction commences on 1 April X3. On 30 June X3 a progress bill for the work performed is received from the project manager for \$3.3 million.

The journal entry to record Construction (WIP) in the books of DCI, on 30 June X3 is:

DR	Construction (WIP) – Capitalised Expenditure	<i>(Increase in Assets – Balance Sheet)</i>	\$3,000,000
DR	GST Owing / Paid	<i>(Increase in Assets – Balance Sheet)</i>	\$300,000
CR	Accounts Payable	<i>(Increase in Liabilities – Balance Sheet)</i>	\$3,300,000

On 10 September X3 the building is completed and a final bill for \$2.2 million (inclusive of GST and management fees) is received. The journal entry to record the final bill on 10 September X3 in the books of DCI is:

DR	Construction (WIP) – Capitalised Expenditure	<i>(Increase in Assets – Balance Sheet)</i>	\$2,000,000
DR	GST Owing / Paid	<i>(Increase in Assets – Balance Sheet)</i>	\$200,000
CR	Accounts Payable	<i>(Increase in Liabilities – Balance Sheet)</i>	\$2,200,000

The journal entry to transfer the completed building (in its entirety) from Construction (WIP) on 15 September X3 in the books of DCI is:

DR	Equity Transfers Out	<i>(Decrease in Equity – Balance Sheet)</i>	\$5,000,000
CR	Construction (WIP) – Transfers Out	<i>(Decrease in Assets – Balance Sheet)</i>	\$5,000,000

APPENDIX B (continued)

1. DCI manages and records Construction (Work in Progress) – continued:

The journal entry to recognise the Construction (WIP) associated with the completed building on 15 September X3 in the books of Agency B is:

DR	Construction (WIP) – Transfers In	<i>(Increase in Assets – Balance Sheet)</i>	\$5,000,000
CR	Equity Transfers In	<i>(Increase in Equity – Balance Sheet)</i>	\$5,000,000

Review of Agency B's Construction (WIP) account shows \$60,000 in costs that are in the nature of repairs and maintenance expenses that should not be transferred to the relevant non-current asset class. The journal entry to expense these costs is:

DR	Repairs and Maintenance – Minor New Works Non Cash	<i>(Increase in Expenses – Operating Statement)</i>	\$60,000
CR	Construction (WIP) – Transfers Out	<i>(Decrease in Assets – Balance Sheet)</i>	\$60,000

The journal entry to transfer the completed building to the relevant property, plant and equipment class (in this case 'Buildings') on 30 September X3 in the books of Agency B is:

DR	Buildings – Transfers In	<i>(Increase in Assets – Balance Sheet)</i>	\$4,940,000
CR	Construction (WIP) – Transfers Out	<i>(Decrease in Assets – Balance Sheet)</i>	\$4,940,000

The completed asset will now be depreciated by the Agency in accordance with Treasurer's Directions Section A2.3 and subject to revaluation requirements in accordance with Treasurer's Directions Section A2.4.

APPENDIX B (continued)**2. Agency manages and records Construction (Work In Progress)**

An Agency enters into a contract for the construction of a building for \$3.3 million (inclusive of GST). The construction commences on 1 April X3. On 30 June X3 a progress bill for work performed is received from the contractor for \$2.2 million.

The journal entry to record Construction (WIP) on 30 June X3 is:

DR	Construction (WIP) – Capitalised Expenditure	<i>(Increase in Assets – Balance Sheet)</i>	\$2,000,000
DR	GST Owing / Paid	<i>(Increase in Assets – Balance Sheet)</i>	\$200,000
CR	Accounts Payable	<i>(Increase in Liabilities – Balance Sheet)</i>	\$2,200,000

On 30 September X3 the building is completed and a final bill for \$1.1 million is received. The journal entry to record the final bill on 30 September X3 is:

DR	Construction (WIP) – Capitalised Expenditure	<i>(Increase in Assets – Balance Sheet)</i>	\$1,000,000
DR	GST Owing / Paid	<i>(Increase in Assets – Balance Sheet)</i>	\$100,000
CR	Accounts Payable	<i>(Increase in Liabilities – Balance Sheet)</i>	\$1,100,000

The journal entry to transfer the completed building from Construction (WIP) on 30 September X3 is:

DR	Buildings – Transfers In	<i>(Increase in Assets – Balance Sheet)</i>	\$3,000,000
CR	Construction (WIP) – Transfers Out	<i>(Decrease in Assets – Balance Sheet)</i>	\$3,000,000

The completed asset will now be depreciated by the Agency in accordance with Treasurer's Directions Section A2.3 and subject to revaluation requirements in accordance with Treasurer's Directions Section A2.4.