

Home and Community Care (HACC) Program in Western Australia

Funded Assets (Accrual Financial Reporting)

Policy

Aged Care Policy Directorate
Department of Health
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1 Purpose

The purpose of this document is to elaborate HACC policy with regard to HACC funded assets including: -

- Permitted use of HACC funds to replace existing assets;
- Permitted use of HACC funds to acquire additional assets;
- Accounting for:
 - Funds set aside for asset replacement and the acquisition of additional assets;
 - Annual depreciation;
 - Accumulated depreciation.
- Acceptable depreciation policy;
- Management of funds set aside for asset acquisition;
- Accounting treatment required for HACC assets and asset funding;
- Requirement to maintain a register of HACC assets;
- Issues that may arise when HACC assets are disposed of;
- Issues that may arise in the transition from cash basis financial reporting to accrual based financial reporting,
- Definitions of significant terms used in this policy

2 Background

HACC funding of service delivery to the HACC target population is as set down in the Service Specification Schedule (SSS) of the relevant Service Agreement.

The HACC Program in the 2006/10 Service Agreements has moved from cash basis financial reporting to accrual based financial reporting for the majority of HACC funded service providers.

The HACC Program had previously contracted for service provision on the basis of unit prices. From 1 July 2007, for service providers that have implemented the Unit Cost model, Service Agreements will use unit costs as the basis for contracting service provision. Unit costs, together with HACC and non-HACC revenue received by service providers, will be used as the basis to determine the service volumes provided by service providers.

The changes to financial reporting and the move to unit costing (inclusive of funding for depreciation) have significant impact on accounting for assets.

Currently, compliance with Australian Accounting Standard AASB1004 on Contributions, (not-for-profit entities) results in a surplus reflected in the financial statements in years when funding for an asset is received. Deficits are reflected in the financial statements in subsequent years as the depreciation expense related to the asset is incurred.

In the past, under the cash based financial reporting, service providers that had met their contracted outputs, had an operating surplus, and received HACC Contract Manager approval, were able to set funds aside for asset replacement. This practice is no longer relevant and will be discontinued. HACC will in future fund the depreciation expense of most HACC assets.

There are some transitional issues that require special treatment.

3 Asset Acquisition

Asset acquisition occurs when an existing asset is replaced (a replacement asset) or when an additional asset is purchased (an additional asset).

The use of HACC funds to acquire additional assets requires a HACC Growth Funding Application (GFA) application.

From 1 July 2007 HACC will fund the depreciation expense of HACC funded assets (excluding buildings) as part of the Annual Funding Limit (AFL) for service providers that have implemented the Unit Cost model. Provided the funds are available, replacement assets are deemed approved and can be replaced from the accumulation of these AFL depreciation funds.

If sufficient funds are not available to replace assets then the service provider needs to make a business case to their Contract Manager for additional funds.

HACC Contract Managers have, in the past, subject to certain conditions, approved service providers to set aside funds from an operating surplus in any given year towards future asset replacement. These funds were held in an Asset Replacement Reserve account. The assets identified for replacement were part of the approval process. This practice discontinues from 1 July 2007.

From 1 July 2007 the annual depreciation expense will be funded by HACC in the AFL. See 'Attachment 1 - Transition Issues'.

Funding for additional assets has always been, and will continue to be, via the GFA process.

Asset Replacement Reserve (Provision) accounts will cease to be used after the transition period. The Asset Replacement Reserve (Cash) account will remain pending expenditure on assets. See 'Attachment 1 - Transition Issues'.

Service providers that are not compliant with the unit cost model only acquire assets (replacement and additional) via the Growth Funding Application process.

3.1 Accounting Issues Relating to HACC Assets and Accrual Accounting

Accrual based financial reporting to HACC became effective on 1 July 2006 for most service providers.

HACC assets owned as at 1 July 2007 will have been funded as non-recurrent income prior to that date. Compliance with AASB 1004 means that the funds to purchase the asset will have created a surplus in the year received.

AASB 1004 - Contributions (applicable for Not-for-Profit entities) requires contributions received or receivable to be recognised immediately as revenue when:

- (a) the entity obtains control of the contribution or the right to receive the contribution;

- (b) it is probable that the economic benefits comprising the contribution will flow to the entity; and
- (c) the amount of the contribution can be measured reliably.

(Some service providers may have previously applied a different accounting treatment.)

Under accrual based accounting, the depreciation expense on HACC funded assets would result in an unfunded expense in the years subsequent to the purchase. See 'Attachment 1 - Transition Issues' for possible transition adjustments.

HACC policy from 1 July 2007 is to fund the annual depreciation on HACC assets as part of the AFL. The funding of depreciation will typically result in an operating cash surplus each year, but not an operating accounting surplus.

An amount equal to the funded depreciation should be placed in an interest bearing deposit account each year. These funds must not be used to fund operations and are to be used to replace identified assets. The funds set aside will equal the movement in the Accumulated Depreciation account. Note there may be a transition adjustment. (Where maintaining a separate account is not possible the funds should be identified and reported.)

Replacement assets purchased post 1 July 2007 will, to some extent, be funded by the depreciation component of the AFL. See Transition Issues - Attachment 1.

3.2 Principles of Asset Acquisition - Replacement Assets

Existing assets are replaced from funds that have been set-aside in the interest bearing deposit account from the cash surplus resulting from HACC funding the depreciation expense.

There may be insufficient replacement funds to replace existing assets. Any shortfall of asset replacement funds greater than \$1000 to replace an asset requires a special "business case". This business case is presented to the service provider's Contract Manager. The shortfall may result for various reasons including cost increases or assets being replaced sooner than anticipated.

Any disposal of an asset that results in a loss on disposal greater than \$1000 should be referred to the service provider's Contract manager.

3.3 Principles of Asset Acquisition - Additional Assets

All funding for additional assets requires a GFA (non-recurrent funding of assets). Replacement funds cannot be used to acquire additional assets.

Service providers that are unsuccessful in the GFA process for additional assets cannot use asset replacement funds to acquire the additional assets. The GFA process is assessed against stringent criteria and therefore asset replacement funds cannot be used as a means to bypass this process.

3.4 Principles of the Asset Acquisition - Donated or Gifted Assets

Donated assets are capitalised and shown at their 'fair value'. The fair value is shown as non-recurrent income in the year that the donated asset is received. The asset is depreciated over its estimated useful life.

Depreciation on donated assets is not funded by HACC and will result in an accounting deficit in years subsequent to the year the asset was donated. No replacement funds will have been provided and a GFA is required if HACC funds are sought to replace the asset.

4 Depreciation

Fixed assets are depreciated over the estimated useful life of the asset. This depreciation expense, excluding land and buildings, is funded by HACC from 1 July 2008.

Service providers should use the rate that is most appropriate to them for the class of asset and its usage.

HACC prefers the application of the straight line method of depreciation so that funding of the depreciation expense is smoother. However, HACC will accept alternative methods of depreciation where they more accurately reflect the pattern of consumption of assets.

HACC assumes that the Cost Model for depreciation as described in AASB 116 is applied.

HACC does not fund building depreciation. However, HACC expects that buildings will be kept in good repair and will fund normal maintenance; refer Category 7 in the Unit Cost Model. Building improvements and additions require a GFA.

See Attachment 4 - How to Treat Depreciation.

5 Management of Funds Set Aside for Asset Replacement

Funds equal to the movement in the Accumulated Depreciation account should be held in an interest bearing deposit account. They can be cumulated with other funds to obtain the best return on the funds. The cash funds need to be identified separately on the balance sheet when reporting to HACC. Cash flow reporting will reflect the transfer of funds to this account, and from this account, when assets are replaced.

This treatment helps ensure the funds set aside for asset replacement are identified and not used for other purposes.

There will be a requirement to reconcile the cash held to the cumulated depreciation of HACC assets listed in the asset register.

Interest earned on these funds is available for asset replacement.

6 Asset Register

The HACC asset register is one of the reports required each year by the 30th September as part of the Service Agreement.

All HACC funded assets with a value of \$1,000 or greater are recorded in an asset register. Note that the acquisition of multiple similar assets each costing less than \$1,000 can also meet the criteria for recording in the register, depending on the circumstances of the purchase. It may be appropriate to aggregate individual items and apply the criteria to the aggregated value of the composite asset.

When an asset is funded by multiple sources, including the HACC Program, the asset is recorded in the HACC asset register with the percentage funded by HACC recorded against the asset.

The asset register must contain, as a minimum:

- Asset Class;
- Description of Asset;
- Date of Acquisition;
- Cost;
- % Funded by HACC
- Accumulated Depreciation;
- Written Down Value;
- Depreciation Rate and Method.

The Contract Manager can request the Asset Register from a HACC funded service provider at any time.

Details of assets disposed of or scrapped should be contained in the register at least for the year of disposal. They may be deleted from the register in subsequent years. Fully depreciated assets still in use remain in the asset register.

Small value items costing less than \$1000 may also be entered to the asset register for control purposes. However, there is no need to record the depreciation and written down value.

7 Disposal of HACC Funded Assets (other than as a trade-in)

HACC approval (via the Contract Manager) is required prior to the disposal of any asset with a written down value (WDV) in excess of \$1000. In many instances this disposal will be part of a trade-in for a replacement and will have deemed approval.

If assets with a WDV in excess of \$1000 are destroyed and replaced through insurance cover, this should be informed to the Contract Manager.

If the Service Agreement is terminated HACC will determine and advise what to do with the HACC funded assets.

If an asset ceases to be used and is surplus to requirements, the service provider must inform the Contract Manager. The Contract Manager will advise on what action to take. Under-utilised and surplus assets inflate a service provider's unit costs.

Transition Issues:

Compliance with AASB 1004:

Most Not for Profit entities are regarded as reporting entities and as such must comply with the Australian equivalents of the International Accounting Standards.

'AASB 1004 - Contributions' requires that funds received to purchase assets will have been shown as income in the year in which the funds were received.

AASB 1004 - Contributions (applicable for Not-for-Profit entities) requires contributions received or receivable to be recognised immediately as revenue when:

- (a) the entity obtains control of the contribution or the right to receive the contribution;
- (b) it is probable that the economic benefits comprising the contribution will flow to the entity; and
- (c) the amount of the contribution can be measured reliably.

In many cases this will result in the funds received shown as income in the year in which the funds were received. Some service providers may have previously applied a different accounting treatment. They may, for example, have shown only income equivalent to the depreciation expense and hold the balance in a provision account.

This provision account will typically be styled 'Unearned Income' or 'Deferred Non-recurrent Income'. The funds are released each year to match the depreciation expense and so ensure that neither surplus nor deficit results from the funding received for the purchase of assets.

Service providers should comply with AASB 1004. Any remaining provision should be transferred to Retained Earnings or some other class of equity.

Asset Replacement Reserves:

Those service providers, with HACC funded assets, without an Asset Replacement Reserve as at 1 July 2008 equal to the accumulated depreciation will need to apply for additional non-recurrent funding to secure replacement funds equal to the accumulated depreciation. HACC has insufficient funds to meet all the possible requests. Funds may only be provided when assets are to be replaced. (Refer to the Asset Replacement Flowchart.) Service providers should liaise with their Contract Manager.

Some service providers may hold Asset Replacement Reserve accounts in their Balance Sheet. These are amounts reported as liabilities, matched by funds on deposit for replacing assets.

In the past, these funds have been released and shown as (Non-recurrent) income when assets have been replaced.

Dr. Asset Replacement Reserve

Cr. (Non-recurrent) Income

The cash on deposit is used to purchase the asset.

These Asset Replacement Reserve (Provision) accounts will cease after the transition period. There will be cash surpluses as a result of depreciation being funded, but no accounting surplus. Note that in normal years, post 1 July 2008, depreciation is funded in the AFL as recurrent income.

The Asset Replacement Reserve (Cash) account will remain pending expenditure on assets.

Attachment 2

Definitions:

AASB:

Australian Accounting Standards Board refer www.aasb.com.au

AASB 116:

Publication of the Australian Accounting Standards Board dealing with "Property, Plant and Equipment".

AASB 1004:

Publication of the Australian Accounting Standards Board dealing with "Contributions".

Additional Asset:

An incremental asset that increases the pool of assets as opposed to a replacement asset. Additional assets can only be acquired through the GFA process.

Asset Class:

A term used in AASB 116 to group assets into like categories viz;

- Motor vehicles;
- Furniture and fixtures;
- Office equipment;
- Machinery;
- Land and Buildings.

Asset Replacement Reserve (Provision):

A provision account used in cash accounting to identify funds earmarked to replace assets.

Asset Replacement Reserve (Cash):

The actual cash funds held in a separate bank account and identified separately as an asset account in the ledger.

Business Case:

A structured proposal to justify requested expenditure. It includes the reasons for the proposal, the expected benefits, the options considered and the expected costs.

Deposit Account:

An interest bearing account. In the HACC context, this is where funds identified for future expenditure and not required immediately are kept. The best rate of interest with minimum risk should be sought recognising the requirement to access the funds.

Fair Value:

This is defined in AASB 116 - Property, Plant and Equipment. 'Fair value is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.'

GFA:

This stands for Growth Funding Application. These are additional funds made available each year to service providers to cater for growth in service provision.

On-Costs:

Labour on-costs are those costs that are direct labour costs but not paid to the employee as normal pay. Examples are superannuation, workers compensation insurance, and annual leave payments.

Overhead:

Unlike the direct costs, overheads are the resources used by an organisation just to maintain its existence. They are the costs that enable the direct costs to be incurred and service provided. They are the Category 5 through Category 9 costs in the unit cost model.

Program:

A term used to describe the whole of the activities funded by Department of Health, Disability Services Commission, Department of Veterans Affairs, Department of Health and Ageing.

Replacement Asset:

An asset that takes the place of an existing asset. The existing asset is disposed of.

Service Type:

The support services delivered by service providers to their clients funded by the HACC Program e.g. meals, transport, domestic assistance, centre based day care etc.

Straight Line Depreciation:

Depreciation is defined in AASB 116 as the systematic allocation of the depreciable amount of an asset over its useful life.

Straight line depreciation is the method whereby the assets are written off in equal amounts each year over their estimated useful life.

Travel Costs:

These are the costs incurred when moving (travelling) between clients. They may include labour and vehicle or vehicle allowance costs.

Unit Cost:

Unit Cost is the actual cost to the service provider of providing a unit of service.

Unit Price:

Unit Price is the amount HACC pays for a unit of service.

Policy Specific to Motor Vehicles:

Purchase of Vehicles

The WA HACC Program does not provide funds to acquire vehicles that are not used in service provision.

HACC distinguishes between:

- Replacement Vehicles, and;
- Additional Vehicles.

Replacement Vehicles

From 1 July 2007 the HACC Program funds vehicle depreciation via the AFL for service providers that have implemented the Unit Cost model. These service providers do not apply to replace vehicles via the Growth Funding Application process.

HACC does not specify replacement criteria such as age or kilometres travelled. Service providers are expected to manage and optimise the replacement decision.

A loss on disposal of a trade-in vehicle that exceeds \$1000 must be notified to the HACC Contract Manager.

Additional Vehicles

Additional vehicles are funded via the Growth Funding Application process.

The HACC Program provides non-recurrent funding for up to 100% of the purchase cost of vehicles, including modifications, by the submission of a Non-Recurrent Growth Funding Application in the HACC Program's annual funding round.

Before considering the purchase of an additional vehicle, service providers must demonstrate in writing to the HACC Program through a Growth Funding Application the need and justification for the vehicle.

Service providers should select the most fuel efficient and economical vehicle (both short and long term) for the intended use. The basic model that meets the requirements should be selected.

Service providers need to consider whether the vehicle will be able to meet current and future client needs and service requirements.

Service providers should comply with the competitive pricing process and demonstrate compliance by providing three (3) written quotes obtained from different suppliers to establish the best price. Quotes from suppliers should include the specifications of the vehicle, such as manufacturer, type, model, class, number of seats, accessories, base price, and cost of modifications and applicable taxes.

The quotes from suppliers and the service provider's recommendation should be included in the Non Recurrent Growth Funding Application to the HACC Program.

The HACC Program will notify service provider's in writing the outcome of the Growth Funding Application.

Funding for the vehicle will be paid approximately ten (10) working days after written approval.

Once notified of successful application, providers should proceed to order the vehicle and arrange the necessary modifications.

As part of the conditions of funding, providers are required to provide the HACC Program proof of purchase of the vehicle. A copy of the supplier invoice, delivery docket and registration certificate are to be submitted to the HACC Program within ten (10) days of delivery/registration of the vehicle.

Service providers that are not compliant with the unit cost model only acquire vehicles (replacement and additional) via the Growth Funding Application process.

HACC service providers should also review:

- HACC Vehicle Best Practice Manual - March 2005
- Growth Funding Application requirements

<http://www.health.wa.gov.au/hacc/HACC-Publications.html>

How to Treat Depreciation:

Buildings:

HACC does not fund building depreciation.

If the building is owned by a third party and provided 'free of charge', then show a notional rental cost and equal notional income.

If the building is HACC funded or Lotterywest funded show a notional depreciation cost and equal notional income.

If there is an arm's length rental arrangement with a third party then the rent should be shown as a cost.

Some service providers may wish to charge an occupancy fee where the service provider permits part of a building to be used for the provision of HACC services. HACC will accept as part of the unit cost an apportionment of accommodation costs based on a reasonable rationale for the space used by the HACC program.

Other Fixed Assets:

HACC funded assets - HACC will fund depreciation.

100% Provider funded assets, used in HACC service delivery (100%) - then depreciation is only funded 100% by HACC after successful GFA application on replacement.

Partial Provider funded assets, used in HACC service delivery 100% - can claim depreciation for the HACC portion if HACC interest can be demonstrated. This normally occurs where a HACC funded asset has been traded for a new asset and the shortfall funded by the provider or different party. If the original HACC funding occurred more than 5 years ago it is deemed a 'non-HACC asset'.

Provider assets not used in service delivery but part of the overhead structure - then depreciation is part of the funded overhead cost structure. It is identified and subject to audit.

100% Provider funded assets occasionally used in service delivery - the depreciation is assumed included in the usage charge. This would be the case where service provider vehicles are sometimes used in the HACC program.

Other Fixed Assets:

HACC funded assets - HACC will fund depreciation.

100% Provider funded assets, used in HACC service delivery (100%) - then depreciation is only funded 100% by HACC after successful GFA application on replacement. (The service provider may elect to show the depreciation cost, even though not funded, as part of their unit cost.)

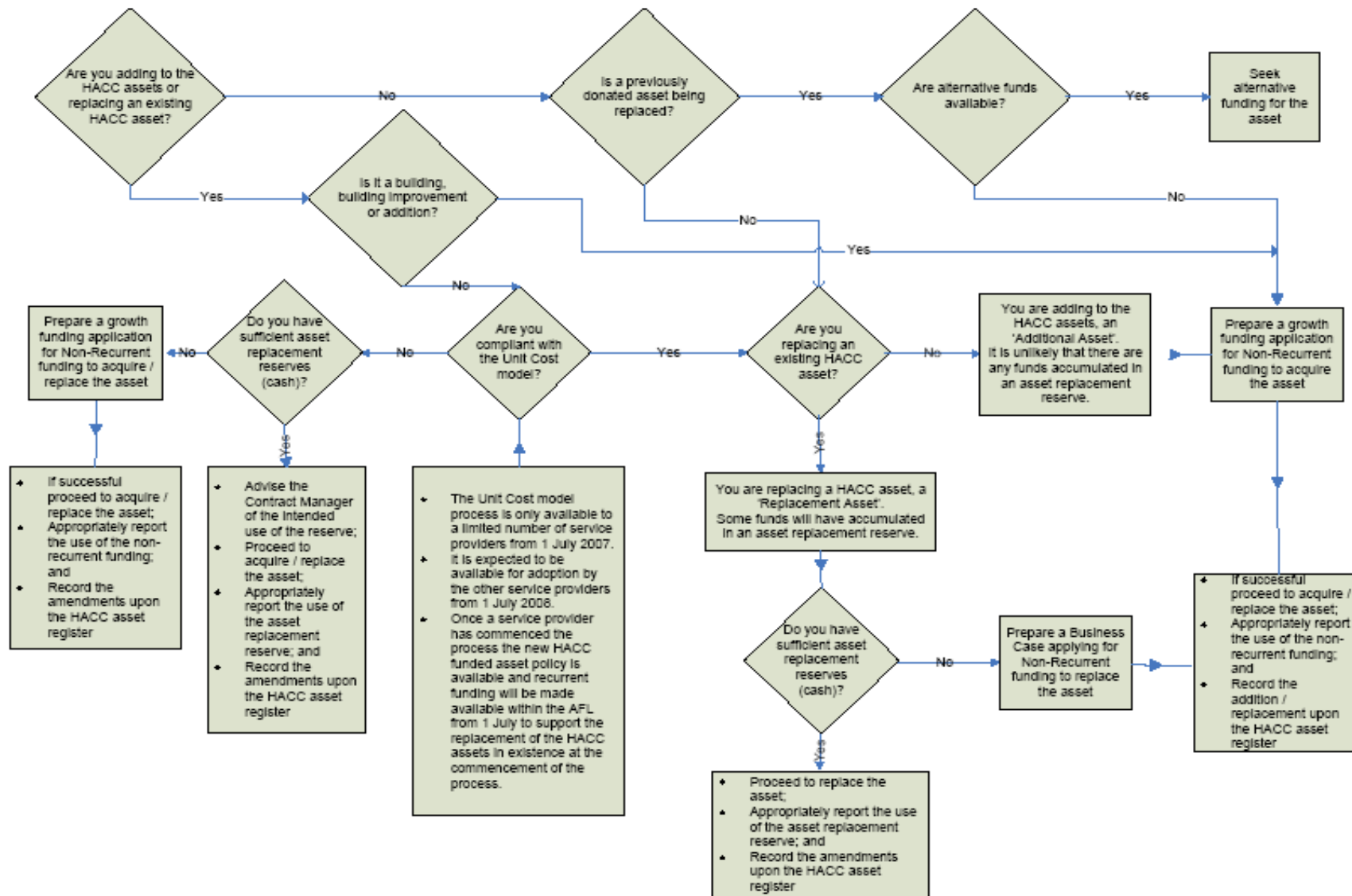
Partial Provider funded assets, used in HACC service delivery 100% - provider can claim funding of depreciation for the HACC portion if HACC component can be demonstrated. This normally occurs where a HACC funded asset has been traded for a new asset and the shortfall funded by the provider or different party. If the original HACC funding occurred more than 5 years ago it is deemed a 'non-HACC asset'.

Provider assets not used in service delivery but part of the overhead structure - then depreciation is part of the funded overhead cost structure. It is identified and subject to audit.

100% Provider funded assets occasionally used in service delivery - the depreciation is assumed included in the usage charge. This would be the case where service provider vehicles are sometimes used in the HACC program.

Donated Assets (excluding buildings):

An amount equivalent to the fair value of the donated asset is shown as income when the asset is received. Such assets are not HACC funded and hence the depreciation is not funded. The service provider should show the depreciation as part of the unit cost if the asset is used in the HACC program.



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