

## N6 Asset Valuation

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### Ideal Standard

Valuation of assets held by the activity is based on deprival method and includes optimisation. Contributed assets have been identified and appropriately treated.

### Outline/Summary

Councils are already required to value their assets on a deprival value basis, and this is subject to external audit. **Deprival value** is the cost of replacing the asset if the Council is deprived of the asset. To this extent it includes an element of optimisation. However, in reality most assets are recorded at replacement value, since there is little practical information on the optimal way assets could be replaced if the Council is deprived of them. Optimisation and Contributed assets are primarily of importance to Water and Sewerage.

The purpose of **optimisation** is to ensure that the asset base on which the activity sets its rate of return does not result in overcharging customers for any inefficiencies or excess capacity in the asset base. Although the accounting standards do not cater for optimisation, council's decision making processes needs to consider optimisation to ensure that current prices reflect efficient asset needs and the avoids any over-capitalisation in the future. However, apart from the following simple adjustments, in most cases the costs of establishing a separate asset register based on optimized valuation will outweigh the benefits, and a similar outcome can be achieved through modifying the funding of depreciation (see N7). Note that depreciation of excess assets should also be excluded from pricing decisions. For businesses with significant infrastructure assets, such as water and sewerage, the optimisation of the asset base should at the minimum:

- remove any redundant assets, i.e. not likely to be used or replaced; and
- remove any excess capacity in the network having regard to usage trends (i.e. peak demand and allowance for growth).

**Contributed assets** (which include all assets either provided or funded by developers or the Government) should be excluded from the asset valuation for the purposes of calculating the rate of return required. The rationale for this is that consumers should not be required to pay for a rate of return on assets which were not funded by the Council. The *Integrated Planning Act* (IPA) requires councils to establish streamlined planning processes and addresses the future treatment of contributed assets. (It is not unusual for 40%-60% and up to 80% of water and sewerage assets to have been contributed). It is expected that councils will have sufficient information to identify recent contributions, but will experience problems with assets prior to 1994. Therefore it is recommended that councils introduce a policy solution to identifying and treating contributed assets prior to 1994. It may also be useful to include in the Valuation policy a statement such as "a proportion of the valuation of assets has been adjusted for pricing purposes"

**Reports:** These adjustments can be achieved by adopting a report on the estimated level of contributed and optimized assets which should be excluded from the need to obtain a return on investment. From this starting point, the actual funding sources should be added each year. Several approaches have been used for contributed assets as follows:

- identifying assets contributed (cash or physical assets from developers or government) ;
- identifying areas where development was funded by developers government; and
- relating the funding source to the age of the asset.

### Key steps

1. Value all Council assets on a deprival basis subject to QAO audit;
2. Prepare Officer's Report estimating the value of excess and contributed assets (WS&S);
3. Adjust the asset base for pricing purposes to exclude contributed and excess assets.

### Further Information

PG 3.4.5.3, 3.4.5.4, 3.8

### QCA Documentation Standard

Audited Financial statements, Budget, Officer's report/s, Valuation policy