

Capital Expenditure Policy

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1 Introduction

1.1 Accounting for capital is governed by financial reporting standards under UK GAAP, listed below, and the associated accounting guidance for the Higher Education sector as set out in the Higher Education SORP 2007 (or its successors):

- SSAP 4 Accounting for government grants
- SSAP 19 Accounting for investment properties
- SSAP 21 Accounting for leases and hire purchase contracts
- FRS 11 Impairment of fixed assets and goodwill
- FRS 15 Tangible fixed assets
- FRS 30 Heritage assets

The College must adhere to these standards in preparing its accounts and this policy is consistent with these standards. They require that capital expenditure is recorded separately from revenue expenditure and to this end the College requires that they are budgeted for and approved separately in order that the implications for the income and expenditure account, balance sheet and cashflow can be identified.

1.2 The overall purpose of this policy is to:

- Confirm and clarify the current policies in place, which should be followed on behalf of the College
- introduce a new policy which relates to the capitalisation of finance costs and
- ensure that capital expenditure across the College is clearly identified, planned, authorised and accounted for accurately in a timely manner.

1.3 This document describes the Capital Expenditure Policy that must be adhered to on behalf of the College and includes details of what is classed as capital expenditure and the process to be followed.

1.4 This policy supports Queen Mary, University of London Financial Regulations, section 14 – Financial Planning, the Scheme of Delegation of Financial Authority and the accounting policies referred to in the Financial Statements, as defined in section 2 below.

http://www.arcs.qmul.ac.uk/policy_zone/index.html

1.5 Capital expenditure and associated costs on land, buildings, equipment and any other capital spend (e.g. software), can only be approved as part of the College's Capital Programme agreed by Council, as outlined in the Financial Regulations.

1.6 The Scheme of Delegation of Financial Authority outlines the areas of responsibility and approval limits related to capital expenditure.

http://www.arcs.qmul.ac.uk/policy_zone/index.html

- 1.7 This policy also provides examples of what should not be capitalised, that is expenditure that is classed as revenue and should be charged to income and expenditure.
- 1.8 This policy is owned by the Deputy Director Financial Control on behalf of the Director of Finance
- 1.9 This policy is supplemented by user guidance and training, as described in section 19.

2 Governance and funding

- 2.1 Queen Mary Senior Executive determines the overall capital budget for the College and retains overall responsibility for capital expenditure.
- 2.2 The capital budget is allocated between:
 - IT expenditure which is managed by the IT Steering Board and
 - the Capital Project Board, which oversees the remaining budget.

Note: The oversight of estates and facilities activities is currently under review. The Governance section of this policy will be amended to reflect the outcome of this review, which includes the future of the Estates and Services Committee.

- 2.3 For grant funded equipment – where full grant funding is provided, the responsibility for approval lies within the relevant School. However, the capital must be accounted for in the same way, as per guidance in this policy.
- 2.4 Capital funding for all capital spend including grant funded equipment is approved through completion and sign off of the Application for Project Funding (APF) form, through the relevant governance process. This includes review and sign off by Finance.

3 Capital budgeting process

- 3.1 All anticipated capital expenditure, with the exception of fully grant funded, should be budgeted for during the budgeting process, covering e.g. major estates and IT projects and equipment. Budget guidance is distributed by the Financial Management team.
- 3.2 The budgeting process is not authorisation to initiate spend. The College's capital authorisation process must be followed, in accordance with the governance described in section 2 of this policy.

4 Accounting policies

4.1 The following accounting policies are extracted from the Queen Mary, University of London Financial Statements.

Tangible fixed assets

Tangible fixed assets are stated at historic purchase cost less accumulated depreciation. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use.

- (i) Freehold land and building and long leasehold building are stated at cost or valuation. The College has applied the transitional rules, contained in Financial Reporting Standard 15, Tangible Fixed Assets, to retain the previous valuations of these properties but not to adopt a policy of revaluation in the future. Since 1 August 2001 all additions to fixed assets have been at cost.
- (ii) Depreciation on buildings is calculated at 2% per annum using the reducing balance method. Depreciation on leased buildings is calculated at 2% per annum or over the life of the lease if the lease is less than 50 years. No provision for depreciation is made against the value of land.
- (iii) Assets in the course of construction are stated at cost and are not depreciated until they are transferred to the completed asset class when ready for use.
- (iv) Plant and Machinery is depreciated over 10 to 15 years.
- (v) Equipment costing less than £10,000 per individual item or group of related items is written off in the year of acquisition. All other equipment is capitalised.
- (vi) Capitalised equipment is depreciated over 3 to 8 years in the consolidated balance sheet.
- (vii) Expenditure on an asset after it is purchased is capitalised when the expected future benefits from that asset as a result of the expenditure are greater than those previously assessed.
- (viii) Where assets are acquired with the aid of specific grants they are capitalised and depreciated as above. The related grants are treated as deferred capital grants and released to income in line with the depreciation charge.
- (ix) Assets held under finance leases are depreciated over the period of the finance lease or their useful economic life whichever is shorter.
- (x) Where it is considered that there has been any impairment in the value of an asset, the difference between the carrying value and the higher of its net realisable value or value in use is expensed in the income and expenditure account. Circumstances which could give rise to an impairment are reviewed annually.
- (xi) The College owns heritage assets, none of which either individually or collectively are material to these Financial Statements, which have not been capitalised.
- (xii) Expenditure to ensure that a tangible fixed asset maintains its previously recognised standard of performance is recognised in the income and expenditure account in the year it is incurred. The College has a planned maintenance programme which is reviewed annually.

Note: This paper clarifies (vi) above - Capitalised equipment includes IT equipment and software, is depreciated over 3 to 8 years in the consolidated balance sheet.

Leases

- (i) Finance Leases which transfer substantially all the benefits and risks of ownership of an asset to the College, are treated as if the asset was purchased outright. The assets are included in fixed assets and the capital elements of the leasing commitments are shown as obligations under finance leases. The lease rentals are treated as consisting of capital and interest elements. The capital element is applied to provide the outstanding obligation at the next option date and the interest element is charged to the Income and Expenditure Account so as to give a constant periodic rate of charge of the remaining balance outstanding at the end of each accounting year.
- (ii) Rental costs under operating leases are charged to expenditure in equal annual amounts over the period of the lease.

Recognition of income

- (i) Grants or donations received in respect of expenditure on fixed assets are treated as deferred capital grants and released to the income and expenditure account in line with depreciation over the life of the asset.

5 Capital vs revenue

What is capital?

- 5.1 Capital expenditure is money spent on acquiring, upgrading and building assets. It is generally used to purchase or develop property, furniture or fixtures, computer hardware and software, laboratory and other equipment.
- 5.2 The College defines capital expenditure (as per the Scheme of Delegation of Financial Authority) as:
 - any expenditure over £10,000 on an item or group of related items which has a life of more than 1 year and
 - has a use in the teaching of students, research, the care of patients or for administrative purposes.

This covers all construction and improvements which increase the value and useful economic life of a building, major equipment purchases, software, and expenditure related to research, consultancy and other areas of knowledge transfer.

- 5.3 Capitalised items are written off to the income and expenditure account, over the period of their useful economic life, through the depreciation charge (definition – see section 20 – Appendix 1 Glossary).
- 5.4 Costs should be considered as gross costs including VAT and Finance will review the VAT treatment on a project by project basis. Due to the mix of our activities the College is not able to recover all VAT and consequently should consider it to be a cost.
- 5.5 Examples of what would be included as capital:
- New construction (new buildings or major additions)
 - Building renovations, demolition prior to construction or upgrades (capital improvements)
 - Property acquisitions and long-term leases
 - New or replacement equipment or furniture (replacement only where any existing asset has been fully depreciated or disposed of)
 - Telecommunication and information technology hardware
 - Heating, ventilation and air-conditioning (new or replacement where any existing assets have been substantially depreciated)
- 5.6 The cost of a fixed asset is its purchase price and any costs directly attributable to bring it into working condition for its intended use. These costs include:
- Acquisition costs
 - Site preparation and clearance
 - Delivery and installation costs
 - Professional fees i.e. architect fees, quantity surveyor (but not Procurement)
- 5.7 For a repair or replacement to be capitalised, it must increase the value and useful economic life of the asset (see 5.9 below).
- 5.8 A replacement may also be capitalised if the new item / part is of significantly improved quality and higher value compared to the old item.
- 5.9 The following examples would be capitalised:
- Replacing a lift by enlarging the shaft and increasing the carrying capacity from 5 to 20 people
 - Building an extension to a lecture theatre
 - Replacing a flat roof with a pitched roof if it increases the useful life of the building
 - Extending a nursery to increase capacity

For more specific guidance refer to the relevant sections covering – Estates and Building Projects, IT Projects, Institute and Research Equipment

Note: Please also refer to section 9 – Feasibility Studies and section 10 – Strategic Studies.

What is revenue?

- 5.10 Replacement or restoration of the original functionality even if over £10,000 would not qualify as capital expenditure, where it is bringing the asset back to its original state (no enhancement).
- 5.11 The following maintenance examples would not be capitalised, as they only bring the asset back to the original state (no enhancement):
- General repairs and maintenance (e.g. repair of potholes)
 - Repainting office / nursery
 - Plumbing or electrical repairs (e.g. burst pipe, replacing lights, heating and ventilation system repairs)
- 5.12 Costs not directly related to the construction of the project such as administration and general overhead costs would be classed as revenue.

Note: Please also refer to section 9 – Feasibility Studies and section 10 – Strategic Studies.

6 Estates and buildings projects

- 6.1 If the asset is constructed by the College, the capital costs will include:
- Labour costs of own employees or building contractor, arising directly from the construction of the tangible fixed asset
 - Professional fees directly related to the construction of the asset (e.g. architect, employer's agent, project manager, quantity surveyor)
 - Delivery and installation of heating, lighting, lifts and air conditioning
- 6.2 The following costs will not be included as capital costs:
- Costs not directly related to the construction of the project such as administration and general overhead costs including unspecified and percentage based design office costs
 - Costs incurred by, or on behalf of those staff, who are directly working on the project but are not directly related to the construction or acquisition of the asset e.g. training, general advice (finance, procurement) and consumables.
 - Costs of moving into a new building.
- 6.3 Plant and machinery or furniture installed in a new or refurbished building should be distinguished from the construction or refurbishment and depreciated over its estimated useful life.
- 6.4 Maintenance costs which include elements of tangible improvements / “betterment” to the asset can be capitalised. For example – repainting a lecture theatre would be classed as revenue (and not capitalised). However, refurbishment of the lecture theatre which included an extension to increase capacity would be classed as capital.

7 IT projects

- 7.1 For IT related projects, the following can be capitalised (if over £10,000):
- Purchased software
 - Hardware
 - Training for implementation
 - Direct consultancy costs and internal staff costs (up to the point of implementation)
- 7.2 The following should not be included:
- Any margins
 - Staff training, software and hardware maintenance costs and software licences once the project has been completed
 - Costs related to Finance or Procurement staff
 - Annual software licences

8 College wide capital equipment including Institute and Research equipment

- 8.1 Equipment costing £10,000 or more per individual item or group of related items, and where the economic benefit of the asset has a useful life of more than one year, should be capitalised.

Example 1 - microscopes, slide scanners, centrifuges.

Example 2 - a computer lab where all computers are replaced may cost £50,000, but the individual computers cost less than £10,000 each – would not be capitalised.

Example 3 – where purchasing a number of component parts to build a piece of equipment (an asset) which overall costs more than £10,000 would be capitalised.

Note: It is important to be aware that it is not always what is invoiced. Need to take into account all the part payments for the related items e.g. 3 x payments of £8,000 = £24,000. The £24,000 would be capitalised. In such cases, Finance will rely on Faculties to provide information, to help determine and ensure these assets are identified and capitalised.

For further advice and guidance, please contact Finance (see section 19).

9 Feasibility studies

- 9.1 Feasibility studies for potential capital projects are capitalised by default. Where a project does not receive approval from the appropriate College Committee, the feasibility study costs (initially charged to capital), cannot be capitalised and must be charged back to income and expenditure, to the department initiating the study.

- 9.2 All projects in progress, will be reviewed in November and May, to ensure they are likely to provide value by the year end and will be continuing. Otherwise, costs cannot be capitalised.

If the project has not been started, a commitment will need to be provided from QMSE / Finance and Investment Committee that a project will proceed.

10 Strategic studies

- 10.1 Strategic studies may not be capitalised e.g. costs incurred to produce an IT Strategy, as these do not directly relate to a specific asset.

11 Grants

- 11.1 Where assets are acquired with the aid of a specific grant, the grant is attributed to the relevant asset and capitalised. The related grants are treated as deferred capital grants and released to income in line with the depreciation charge.

12 Operating leases

- 12.1 An operating lease is a contract agreement for the use of an asset and tends to be short term (but not always), compared to the useful life of the asset or piece of equipment. For example, a piece of equipment may have an economic useful life of 25 years, but may be leased under an operating lease to an organisation (lessee) for 5 years.
- 12.2 Costs incurred as part of an operating lease are classed as revenue and not capital.
- 12.3 With an operating lease, the title of the asset does not generally pass to the lessee (organisation using the asset), but remains with the lessor (organisation providing the asset).
- 12.4 When considering purchasing vs operating vs finance leases, a business case should be put forward to consider the benefits of both options for the College e.g. becomes a financing decision.
- 12.5 The accounting for operating leases is overseen by Financial Accounting and the Capital and Estates Accountant.

13 Finance leases

- 13.1 A finance lease is a contract agreement for the use of an asset and tends to be more longer term (but not always).

- 13.2 Drawdowns under capital leases should be capitalised. The regular monthly / quarterly leasing charges will need to be split between repayment of capital and the interest charge. The interest charge is a cost to the revenue budget over the life of the lease. Financial Accounting will provide a schedule of interest charges over the life of the lease.
- 13.3 For assets held under finance leases, the College has a policy to depreciate the assets over the period of the finance lease or their useful economic life, whichever is shorter.
- 13.4 The lessor (providing the asset) is usually the legal owner of the asset during the course of the lease. However, the lessee (using the asset) has control over the asset, providing the benefits and risks of economic ownership.
- 13.5 With a finance lease, the lessee may have the option to acquire ownership of the asset (e.g. paying the last rental amount, bargain option purchase price).
- 13.6 When considering operating vs finance leases, a business case should be put forward to consider the benefits of both options for the College e.g. becomes a financing decision.
- 13.7 The accounting for finance leases is overseen by Financial Accounting and the Capital and Estates Accountant.

14 Accounting for capital expenditure

- 14.1 Capital expenditure must be allocated to the relevant capital account codes at the time of commitment e.g. when a Purchase order is raised. Relevant account codes will be advised by the Financial Management team.
- 14.2 Finance will have overall responsibility for determining the distinction between capital and revenue and treatment of leases, in line with the UK accounting rules, based on information provided by faculties and departments. If in doubt, Finance should be consulted to discuss proposed items of spend, to ensure decisions are made about the correct treatment.
- 14.3 Purchase requisitions should be raised on Agresso for planned capital expenditure, after the governance process has been followed, to get the spend approved.
- 14.4 Committed capital expenditure - purchase requisitions should be raised, coded to the relevant capital account codes as advised by Finance and approved, for all committed capital funds. This ensures the College has visibility of its commitments throughout the financial year.
- 14.5 Accruals for e.g. equipment – should be included in the monthly management accounts. Receipting of goods / services against purchase orders related to capital spend should be actioned on a timely basis once the goods / services have been

received as per requirements in the original order, to ensure accruals can be included in the monthly management accounts.

- 14.6 Accruals for e.g projects - Project Managers should inform the Capital and Estates Accountant about work executed to date, so that the value of this can be taken into account, where the invoice has not yet been received and / or paid.
- 14.7 Assets under construction – will remain under “work in progress” until completed. Projects Managers and the Capital and Estates Accountant will regularly review projects and anticipated completion dates. Completed assets must be flagged and included on the Fixed Asset Register.
- 14.8 Depreciation - should be charged from the time an asset comes in to use, at the start of its useful life (e.g. building comes in to use). The Capital and Estates Accountant must be notified when an asset comes in to use, so that it can be included on the Fixed Asset Register and depreciation charged according to QMUL’s policy.
- 14.9 Depreciation will be charged monthly in the management accounts in line with the agreed depreciation policies outlined in section 4.
- 14.10 Retentions – a Register of Retentions is maintained and information is included in the notes to the accounts. Retentions are accrued monthly by Financial Management team, through the construction phase of the project. These will be reviewed periodically and released in the event that they are not due to be paid.

15 Monitoring and reporting

- 15.1 Capital expenditure will be monitored and reported on monthly, co-ordinated by the Financial Management Team and will cover spend overseen by:
- Project Board
 - IT Steering Group
 - Faculties / Professional Services

16 Disposal / sale of assets

- 16.1 If an asset, that has previously been designated as a capital item (e.g. piece of equipment, building), comes to the end of its useful life or is disposed of (e.g. given away, scrapped or sold), Finance must be notified via the Capital and Estates Accountant, so that the Fixed Asset Register can be updated and the relevant accounting entries actioned.

17 Impairment of assets

- 17.1 In the event of any impairment (loss) in the value of an asset over and above normal wear and tear (e.g. change in use of the asset or economic life is shortened), Finance

must be notified via the Capital and Estates Accountant, so that the Fixed Asset Register can be updated and the relevant accounting entries actioned.

17.2 Circumstances which could give rise to an impairment are also reviewed annually by the Capital and Estates Accountant.

18 Further guidance, queries and training

18.1 This policy is supported by user guidance and training arranged and provided by Finance.

18.2 If you require any further guidance or have any queries related to this policy or about capital expenditure, please contact:

- your Finance Manager or the Capital and Estates Accountant

Contact details can be found on the Finance intranet page

<http://qm-web.finance.qmul.ac.uk/people/index.html>

18.3 If you have any queries about raising purchase requisitions / orders or goods receipting, please contact:

- Procurement Team

Contact details can be found on the Procurement intranet page

<http://qm-web.finance.qmul.ac.uk/purchasing/team/index.html>

19 Appendix 1 - Glossary of accounting and QMUL terms

Term	Definition
Accruals concept	<p>The principle that revenue and costs are recognised as they are earned or incurred, are matched with one another, and are dealt with in the income and expenditure account of the period to which they relate, irrespective of the period of receipt or payment.</p>
Accruals at QMUL	<p>The College follows accruals accounting. This is when income and expenses are recorded as they occur, regardless of when cash is exchanged.</p> <p>This means that assets are recorded in the accounts when they are acquired or costs incurred.</p> <p>A Purchase Order example for the purchase of equipment:</p> <ul style="list-style-type: none"> • the school raised a purchase order for a microscope costing £15,000 and placed the order with the supplier in September • the supplier delivered the microscope in December as per the order but the organisation has not yet received and paid the invoice. • the school has “goods received” the Purchase Order for the microscope, as the microscope has been delivered as per the specification requested. • Finance can “accrue” (record in the accounts) the £15,000 amount owed (the liability) to the supplier for the microscope delivered, which will be paid at a later date once the invoice has been received. This means the accounts reflect the amount owed to the supplier, which provides a more accurate forecast. <p>For projects – we take into account the value of work executed to date but where the invoice has not been received and / or paid.</p>
Capital expenditure	<p>The cost of acquiring, producing or enhancing fixed assets.</p>
Capital commitments	<p>The estimated amount of capital expenditure:</p> <ul style="list-style-type: none"> ○ purchase order raised against a capital account code and order placed with supplier ○ contracted for but not yet provided for ○ authorised by directors but not yet contracted for <p>Purchase order example for purchase of equipment</p> <ul style="list-style-type: none"> • a school decides it needs to purchase a new microscope and raises a purchase requisition in

Term	Definition
	<p>September for £15,000, which is approved and a purchase order created.</p> <ul style="list-style-type: none"> • the purchase order is sent to the supplier to place the order, with the delivery date being in December. The school is now committed to spending the money, from its allocated budget. • the funds remain committed until the goods or services are received and paid for, when it becomes actual expenditure. <p>Major projects example –</p> <ul style="list-style-type: none"> • a contract has been signed for a new building project but it has not been completed yet. • the funds for the new building have been agreed from the budget and set aside to spend on the new building, but no actual expenditure has been incurred.
Depreciation	<p>The measure of wearing out, consumption or other loss of value of a fixed asset whether arising from use, the passing of time, or it becomes obsolete through technology or market changes.</p> <p>It is an accounting entry (non-cash), and indicates how much of an asset's value has been used up.</p> <p>Finance are responsible for the accounting entries, which writes down the asset cost in the balance sheet and are charged to the income and expenditure account.</p>
Financial Reporting Standard (FRS)	A UK accounting standard issued from 1 August 1990, when the Accounting Standards Board succeeded the Accounting Standards Committee.
Fixed asset	An asset that is not consumed or sold during the normal course of business, such as land, buildings, equipment, machinery, vehicles. Any asset expected to last, or be in use for, more than one year is considered a fixed asset and has a cost over £10,000.
Impairment of an asset	<p>For example –</p> <p>loss in the value of the asset, purpose no longer exists.</p>
SORP	Statement of Recommended Practice; a set of clarifications of how FRS / SSAPs apply to a specific sector e.g. Higher Education.

Term	Definition
Statement of Standard Accounting Practice (SSAP)	A UK accounting standard issued by the Accounting Standards Committee.