

**METHODOLOGY  
FOR THE  
CLASSIFICATION &  
TREATMENT OF LAND  
POLICY**

**UNCHANGED**

**JULY 2016**



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## **PURPOSE**

The purpose of this document is:

- To set out a methodology for the classification and measurement of land in line with the applicable accounting standards.

The classifications include:

- GRAP 12 Inventory;
- GRAP 16 Investment property;
- GRAP 17 Property, plant and equipment;
- GRAP 31 Intangible assets; and
- GRAP 103 Heritage assets.

## **SCOPE**

The methodology is applicable to all land registered in the name of the municipality and all servitudes purchased and obtained through legislation by the municipality.

## **Definitions and abbreviations**

“**ASB**” means Accounting Standards Board

“**CFO**” means chief financial officer

“**FAQ**” means frequently asked questions as issued by the Accounting Standards Board

“**Financial year**” means the period 1 July of one year to 30 June of the following year (both days included)

“**GRAP**” means generally recognised accounting practices

“**MFMA**” means Municipal Finance Management Act, Act 56 of 2003

“**Municipality**” means Steve Tshwete Local Municipality

“**PPE**” means property, plant and equipment as defined in GRAP 16.05

“**RDP**” means reconstruction and development programme

“**Reporting date**” means 30 June of each year

“**VAT**” means Value-Added Tax in terms of the Value-added Tax Act, Act 86 of 1991



## APPLICABLE ACCOUNTING STANDARDS

GRAP 12.07 *“Inventories are assets:*

- (a) in the form of materials or supplies to be consumed in the production process;*
- (b) in the form of materials or supplies to be consumed or distributed in the rendering of services;*
- (c) held for sale or distribution in the ordinary course of operations; or*
- (d) in the process of production for sale or distribution.*

GRAP 16.05 *“Investment property is property (land or a building – or part of a building – or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:*

- (a) use in the production or supply of goods or services or for administrative purposes; or*
- (b) sale in the ordinary course of operations.”*

GRAP 17.06 *“Property, plant and equipment are tangible items that:*

- (a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and*
- (b) are expected to be used during more than one reporting period”.*

GRAP 31.11 *“An intangible asset is an identifiable non-monetary asset without physical substance“*

## METHODOLOGY FOR CLASSIFICATION OF LAND

### 1. Use of municipal land by a third party

Use of municipal land by a third party includes:

- Land leased to third parties at market and non-market related rates;
- Land of which the right to use has been provided to third parties at no charge;
- Land donated to the municipality for the purpose of providing the use of the land to the community at no charge; and
- Land leased to employees for housing purposes, refer to the section on *Land occupied by employees.*

In determining if land leased to third parties should be classified as investment property the municipality determines if the purpose of the land is to earn rentals rather than for sale in ordinary course of business or for use in supply of services or for admin purposes. Therefore the municipality has to determine what the main purpose is **and** what the most significant use is. [GRAP 16.12 states *“This Standard [Investment property] is applicable if the main purpose and most significant use of the property is to earn rental...”*].



The main purpose is determined by looking at what the property is used for if not rented out. In determining the most significant use the Municipality assesses at what portion, in square meters, of the land is leased out. It is considered significant if 75% or more of the area of the land is leased out.

Land of which 75% or more of the area is rented out and there is currently no other use for the land is classified as investment property.

Land of which less than 75% of the area is rented out and there is currently no other use for the land is also classified as investment property. Refer to the section *Land held for undeterminable future use*.

Land held for the purpose of resale which is leased to third parties in the meantime, even if it is 75% or more of the area, is classified as inventory as the main purpose of the property is for resale in the ordinary course of business.

Land held for administrative purposes or for use in the production of goods or supply of services of which a portion, significant or not, is leased to a third party is classified as PPE as the main purpose of obtaining the land was for administrative purposes or for use in production of goods or the supply of services. This will include for example:

- The town hall which is leased to third parties on an ad hoc basis; or
- Community assets such as sport facilities being leased to third parties at a nominal value.

When land is donated to the municipality and a condition is attached to the land, the municipality assesses the condition attached to the land to determine the main purpose of the land and subsequently the classification of the land. An example includes:

- Land donated by Provincial Government with the instruction that the land has to be provided to a specific community, at no charge, for grazing. In this example the main purpose of the land is for economic growth in the community and to uplift the community, the land will be classified as PPE.

## 2. **Owner-occupied land**

Owner-occupied land includes all land used for administrative purposes, in the production of goods or services or for rental to others. This includes, but is not limited to:

- For administrative purposes:
  - Land on which municipal administrative buildings are situated
  - Ervens used by the municipality as car parks, for example where municipal construction vehicles are stored
- In the production of goods and services:



- Land on/in which infrastructure and community assets are situated
- For rent to others:
  - Land on which properties occupied by employees is situated. Refer to the section on *Land occupied by employees*

All owner-occupied land is classified as PPE.

### 3. **Land occupied by employees**

All properties occupied by employees which are require as part of their employment to locate to a specific area are classified as PPE in terms of GRAP 17.11(c), regardless if rental levied is market related or not or even if rental is levied.

### 4. **Landfill sites, borrow pits and quarries**

A landfill site (also known as a tip, dump, rubbish dump or dumping ground) is a site for the disposal of waste materials by burial.

Licensed and unlicensed landfill sites are classified as PPE.

Borrow pits are land from which construction material, such as sand and gravel, is taken for use as fill at another location.

Registered and unregistered borrow pits are classified as PPE.

Quarries are places from which dimension stone, rock, construction aggregate, riprap sand, gravel or slate has been excavated from the ground. Difference between quarries and borrow pits is that borrow pits produce some products that consist of round stones, whereas all products from quarries are crushed with lead to sharp edges.

Registered and unregistered quarries are classified as PPE.

### 5. **Repossessed land**

This land includes land seized from consumers due to non-payment of rates levies. The land is placed on auction and if there are no interested buyers, the municipality will buy the land itself.

Repossessed land is classified as inventory as the land is held for sale in the ordinary course of operations.

### 6. **Held for sale land**

Land held for sale includes:



- Land purchased or obtained through non-exchange transactions for the purpose of short term sale or distribution in the ordinary course of operations; and
- Land previously held for undeterminable future use on which development has commenced with the view to sell or distribute.

This land is classified as inventory in terms of GRAP 12 inventory.

## 7. Land held for an undetermined future use

Land held for an undetermined future use includes the remainder of land not specifically included as:

- Use of land by a third party;
- Owner-occupied land;
- Land occupied by employees;
- Landfill sites, borrow pits and quarries;
- Repossessed land; or
- Held for sale land.

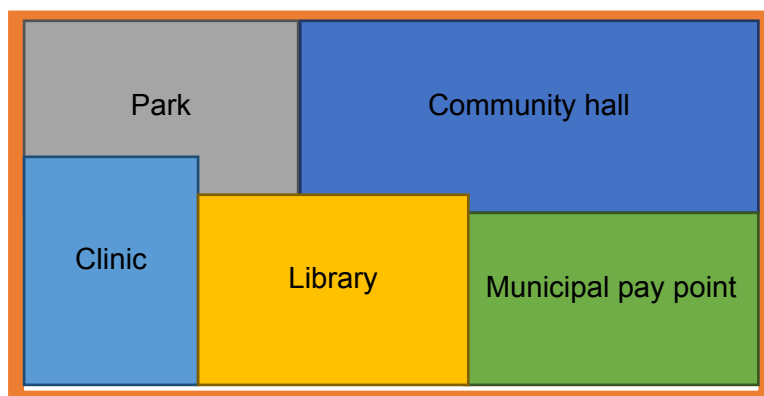
Land held for an undetermined future use is classified as investment property in terms of GRAP 16.10 (b).

## 8. Multi-purpose use of land

Multi-purpose use of land consists mainly out of three scenarios.

### Scenario 1

On one even different asset classes are found, however within on classification of either PPE or investment property. Refer to example below.



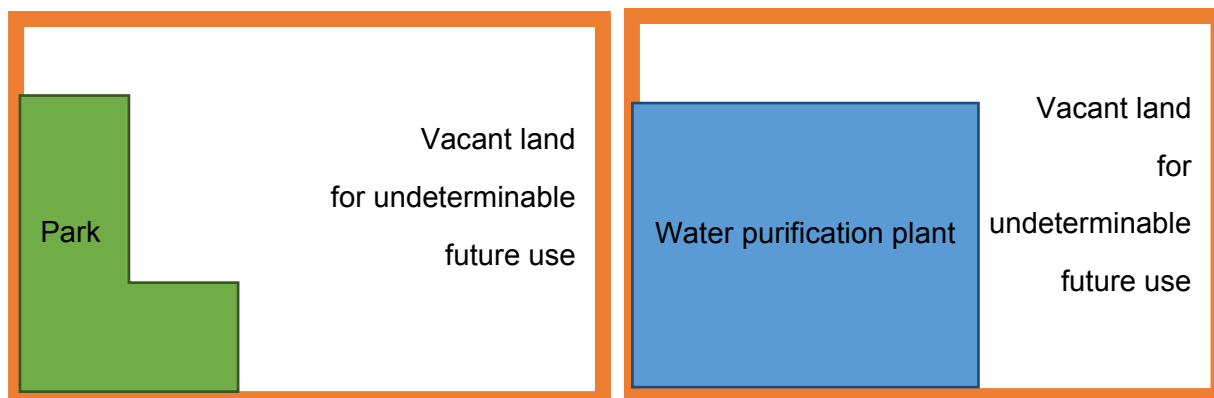
When the use of these individual parts is all classified as PPE then the land is classified as PPE. If the use of the individual parts is all classified as investment property then the land is classified as investment property.

### Scenario 2





A portion of land previously held for an undeterminable future use is now being used as owner-occupied property. Refer to example below.

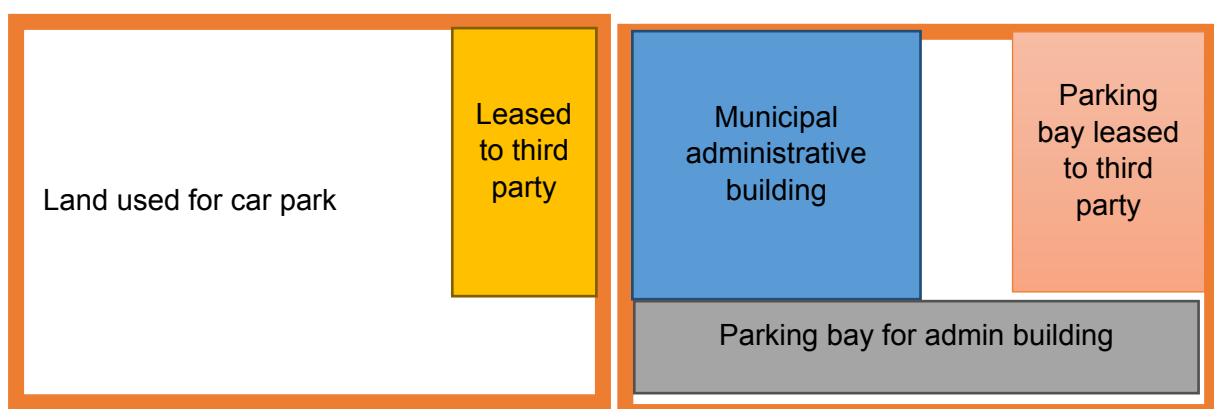


If the portions of land can be sold separately then they are classified separately as investment property (for the undeterminable future use portion) and PPE (the portion now being used as a park). If the portions cannot be sold separately the land will remain investment property unless a significant portion is now being used as PPE.

A portion of erven is considered significant if it is 75% or more of the total size of the erven.

### Scenario 3

Land previously classified as owner-occupied is now being leased. Refer to examples below.



If the portions of land can be sold separately then they are classified separately as investment property (leased portion) and PPE (owner-occupied portion). If the portions cannot be sold separately the land will remain as PPE unless a significant portion is now being used as investment property.

A portion of erven is considered significant if it is 75% or more of the total size of the erven.





## 9. Land specifically not investment property

The following are instances where land is not investment property:

- Owner-occupied land;
- Owner-occupied land waiting for disposal;
- Land held for future development in order to use it as owner-occupied property;
- Recreational, sporting or similar facilities held by the municipality as part of their mandate;
- Land held to provide goods and services and which also generates revenue;
- Land held for strategic purposes. This is property that, although not currently used as property, plant and equipment, is likely to be used in the production or supply of goods and services or for administrative purposes in future because of certain legislation, policies, decisions or plans adopted by the municipality;
- Property occupied by personnel which are required as part of their employment contract to be relocated;
- Land held by the municipality for transfer to beneficiaries in a housing scheme; and
- Property held for sale in the ordinary course of operations or in the process of construction or development for sale or development for housing stock.



## **METHODOLOGY FOR TRANSFER TO LAND**

### **1. From Investment property to PPE or Inventory**

Land is transferred from investment property only under the following circumstances:

- Commencement of owner-occupation, for transfer to PPE
- Commencement of development with view to sale (land previously held for undeterminable use), for transfer to inventory

Commencement date of owner-occupation is the earlier of:

- the date the premises is occupied or
- the date the premises is entitled to be occupied

Commencement date of development with the view to sell is the township proclamation date or date of council resolution on the utilization of land.

### **2. From Inventory to Investment property or PPE**

Land is transferred from inventory only under the following circumstances:

- Commencement of an operating lease (lease must be on a commercial basis) to another party, for transfer to investment property; or
- Commencement of owner-occupation, for transfer to PPE.

### **3. From PPE to Investment property or Inventory**

Land is transferred from PPE to investment property when owner-occupation ceases. Any construction and/or development cost is capitalised against investment property.

Land is transferred from PPE to inventory on commencement of development with the view to sell. The commencement date with the view to sell is the township proclamation date or date of council resolution where the utilization of land changed.



## METHODOLOGY FOR ASSET CLASSES FOR DISCLOSURE PURPOSES

### 1. Inventory

GRAP 12 Inventory requires the municipality to classify inventory in groups appropriate for the municipality. The municipality classifies the land per function, thus what the land is used for. These classes include, but are not limited to, the following:

Asset class	Example
Land held for sale	<ul style="list-style-type: none"> <li>▪ Land identified and proclaimed</li> <li>▪ Land repossessed</li> </ul>

### 2. Investment property

GRAP 16 Investment property also requires the same reconciliation however it does not have to be per asset class. The municipality classifies the land per function, thus what the land is used for. These classes include, but not limited to, the following:

Asset class	Example
Land	All land leased to third parties
Land held for undeterminable use	Remainder of land for which no use has been determined at date of disclosure

### 3. PPE

GRAP 17 property, plant and equipment requires the municipality to disclose, per asset class, a reconciliation between the opening and closing carrying amount. A class of assets is defined as a group of asset with a similar nature or function in the municipality's operations.

The function, thus what the land is used for, determines the classification for disclosure purposes as land forms and integral part of infrastructure and community assets. Land is recognised as a component of the asset it relates to, however for disclosure purposes they are grouped into the same class. The asset classes for disclosure purposes include, but not limited to, the following:

Asset class	Example
<b>Infrastructure assets</b>	
Roads, pavements and bridges	Road reserves
Storm water	n/a
Dams and reservoirs	Water works
Water purification	Pump stations / buildings
Water reticulation	Land servitude (only where pipelines are above ground)
Transportation	Taxi terminals / bus stops
Electricity reticulation	Substations
Sewer reticulation	Land servitude (bulk sewer lines)



Asset class	Example
Sewer purification	Pump stations / buildings / public toilets
Housing	Old age flats / hostels
Housing development fund	n/a
Street lighting	No land is recognised or disclosed under this section
Waste management	Landfill sites
Town planning and development	n/a
<b>Community assets</b>	
Parks and gardens	Land on which parks are developed (landscaping)
Sport fields and stadia	Golf course / bowling / rugby stadia
Swimming pools	Pump station / swimming pool
Community halls	Land on which community hall buildings are situated
Libraries	Land on which library buildings are situated
Recreational facilities	Land on which recreational facilities are situated
Fire, safety and emergency	Emergency services buildings
Security and policing	Land on which fencing is situated
Clinics	Land on which clinics are situated
Museums and art galleries	n/a
Cemeteries	Land on which cemeteries are developed, including roads, public toilets
<b>Other assets</b>	
Abattoirs	n/a
Civic land	Land on which administrative buildings are situated
Other land	n/a



## **METHODOLOGY FOR RECOGNITION AND MEASUREMENT OF LAND**

Land, identified as PPE, investment property and inventory, is initially measured at its cost and where the land was obtained at no cost or for a nominal value the cost is the fair value of the land at acquisition date. The difference between the fair value and the nominal cost or no cost is recognised in surplus and deficit.

The cost is the purchase price (excluding VAT) and any cost directly attributable expenditure.

### **1. Land identified not previously on the register**

Any land identified subsequent to 1 July 2007, which had to be on the Municipality's register however was not, for which the actual cost cannot be obtained will be taken onto the register at deemed cost and measurement date as per directive 7 deemed cost on initial adoption of Standards of GRAP.

The municipality is classified as a high capacity municipality in terms of Government Gazette No. 26511 dated 1 July 2004. In terms of National Treasury Circular No. 44 and Government Gazette 30013 dated 29 June 2007, high capacity municipalities had to be fully GRAP compliant for financial periods ending 30 June 2009. As a result directive 7 can be applied to all additions prior to 1 July 2007, if the actual cost cannot be determined.

The asset register was reconstructed to be in line with GRAP requirements as at 30 June 2008 and a complete asset valuation guide was prepared. The unit rates documented and applied during the reconstruction of the asset register will be applied as the deemed cost for any land subsequently identified which were not taken up in the financial system and the asset register as at 30 June 2008. Refer to annexure A: Units rates for these rates.

### **2. Landfill sites, borrow pits and quarries**

On initial recognition the cost of landfill sites, borrow pits and quarries include:

- The cost of the land itself; and
- The cost to rehabilitate the land.

Subsequent cost recognised in the carrying amount of landfill sites only includes the movement in the rehabilitation provision as a result of the changes in the timing and/or amount required to settle the obligation.

The annual unwinding of the discount is recognised in surplus and deficit as a finance cost, as it occurs.



### 3. **Transfers between Investment property, PPE and Inventory**

The municipality subsequently measures PPE and investment property using the cost model. Any transfers between PPE, investment property and inventory do not change the carrying amount of the land, therefore no gain or loss is recognised in surplus and deficit.

### 4. **Depreciation**

Land has an unlimited useful life except for sites used for landfill, borrow pits and quarries, therefor, land is not depreciated.

Depreciation is however calculated on the portion of the cost capitalised to rehabilitate the landfill site and borrow pits. This depreciation is calculated over the term of the license agreement.





## **METHODOLOGY FOR RECOGNITION AND MEASUREMENT OF INTANGIBLE ASSETS RELATING TO LAND**

### **1. Servitudes**

Servitudes are rights granted by a property owner to another person or entity to use the land for certain purposes, e.g. to construct assets on or over a specific property or the right to access to a property. As servitudes are rights attached to property, the municipality considers whether the definition and recognition criteria in GRAP 31 intangible assets are met.

Servitudes may be acquired in a number of ways including through expropriation, township establishment conditions, agreement between parties, court order, statute or other means.

#### **1.1. Servitudes created by way of legislation**

This would include, for example where the municipality registers servitudes over certain parts of the land that falls within the boundaries of the proclaimed township so that the municipality can install infrastructure to provide basic services. In these instances no compensation is required to the landowner for the servitudes granted to the municipality in terms of legislation.

Servitudes created by way of legislation do not meet the definition of intangible assets as these servitudes are not “separately identifiable” in terms of the definition of intangible assets.

The cost incurred (if any) to register these servitudes are expensed and not capitalised.

The land on which these type of servitudes are registered is in the name of the municipality. This land is recognised as PPE as it is land used in the production of goods or delivering of services. This land relates to infrastructure assets and is recognised as components of the relevant infrastructure assets in the asset register and is disclosed as part of the asset class land in the financial statements

#### **1.2. Servitudes created by way of acquisition (including an agreement)**

This would include for example instances where the municipality requires a piece of land to install certain infrastructure, e.g. a pipeline for a water network. The landowner (which is not the municipality) is compensated for the rights received associated with the land.

Servitudes obtained in this manner meet the definition of “separately identifiable” as they arise through a contractual or other legal right. In these instances the servitudes are recognised as intangible assets.



Once an asset is constructed on the land over which the servitude is registered, the cost of the servitude is transferred and capitalised as part of the cost of the asset. The servitude is an integral part of the asset and the asset cannot function without the servitude, in addition the servitude and the asset cannot be sold separately as the right to use of the land is required for the asset to be operated.

The cost incurred to acquire the servitude (e.g. the compensation paid to the landowner) and any additional cost to bring the asset to the condition and location intended by management (e.g. registration cost) will be capitalised as part of the cost of the asset.

In some cases, the municipality may acquire the use of a servitude at no cost. Under these circumstances the cost to be capitalised is the fair value at the date the use of the servitude is obtained. This cost is amortised over the term of the agreement.

The municipality is not the landowner of the land on which this type of servitudes is registered, therefore no land is recognised in the accounting records or the asset register of the municipality.

### **1.3. Servitudes created, on municipal land, by way of request from third party**

This would include for example instances where a third party, e.g. Eskom, requires a piece of land to install certain infrastructure, e.g. power lines. The municipality is compensated for the rights transferred associated with the land.

The land is in the name of the municipality and the municipality is only selling the right to use the land. There is no transaction required with regard to the land and no intangible asset is recognised as the municipality did not purchase the right, they sold the right.

The agreement for the right to use the servitude contains a lease for the following reasons:

- The agreement conveys the right to use the servitude; and
- Fulfilment of the arrangement is dependent on the use of a specific asset.

The revenue from the right to use the servitude will be recognised and measured in terms of GRAP 13 leases and iGRAP 3 determining whether an agreement contains a lease.



## REVIEW OF METHODOLOGY

In terms of section 17(1)(e) of the MFMA policies must be reviewed on an annual basis and the reviewed policy tabled to council for approval as part of the budget process.

<b>Section:</b>	Chief Financial Officer
<b>Current review date:</b>	
<b>Previous review date:</b>	

## APPROVAL AND IMPLEMENTATION OF METHODOLOGY

This methodology shall be implemented once approved by council.

<b>Section:</b>	Chief Financial Officer
<b>Approval date by council:</b>	

## SOURCE

- GRAP 12 inventory issued March 2012
- GRAP 13 leases issued March 2012
- GRAP 16 investment property issued March 2012
- GRAP 17 property, plant and equipment issued March 2012
- GRAP 31 intangible assets issued March 2012
- iGRAP 2 changes in existing decommissioning, restoration and similar liabilities issued February 2010
- iGRAP 3 determining whether an agreement contains a lease issued February 2010
- Directive 7 deemed cost on the adoption of standards of GRAP issued December 2009
- FAQ issued May 2011
- Valuation guide for immovable assets employed in service delivery dated 13 May version 3.5



## Annexure A: Unit rates

### 1. Potable water

Component	Description	Unit	Unit Rate Jun 2008 excl VAT
Land	Industrial	m <sup>2</sup>	R 150
	Urban settlement	m <sup>2</sup>	R 89
	Tribal settlement	m <sup>2</sup>	R 45
	Informal settlement	m <sup>2</sup>	R 7
	Open space	m <sup>2</sup>	R 7
	Farms	m <sup>2</sup>	R 7
	Agricultural holdings	m <sup>2</sup>	R 30
	State institutions	m <sup>2</sup>	R 59
	Large business	m <sup>2</sup>	R 59
Servitude	Industrial	m <sup>2</sup>	R 39
	Urban settlement	m <sup>2</sup>	R 23
	Tribal settlement	m <sup>2</sup>	R 12
	Informal settlement	m <sup>2</sup>	R 2
	Open space	m <sup>2</sup>	R 2
	Farms	m <sup>2</sup>	R 2
	Agricultural holdings	m <sup>2</sup>	R 8
	State institutions	m <sup>2</sup>	R 16
	Large business	m <sup>2</sup>	R 16

### 2. Sanitation

Component	Description	Unit	Unit Rate Jun 2008 excl. VAT
Land	refer to Water		R 0



### 3. Roads and storm water

Component	Description	Unit	Unit Rate Jun 2008 excl. VAT
Land	refer to Water		R 0

### 4. Electrical

Component	Description	Unit	Unit Rate Jun 2008 excl VAT
Land	refer to Water		R 0

### 5. Solid waste

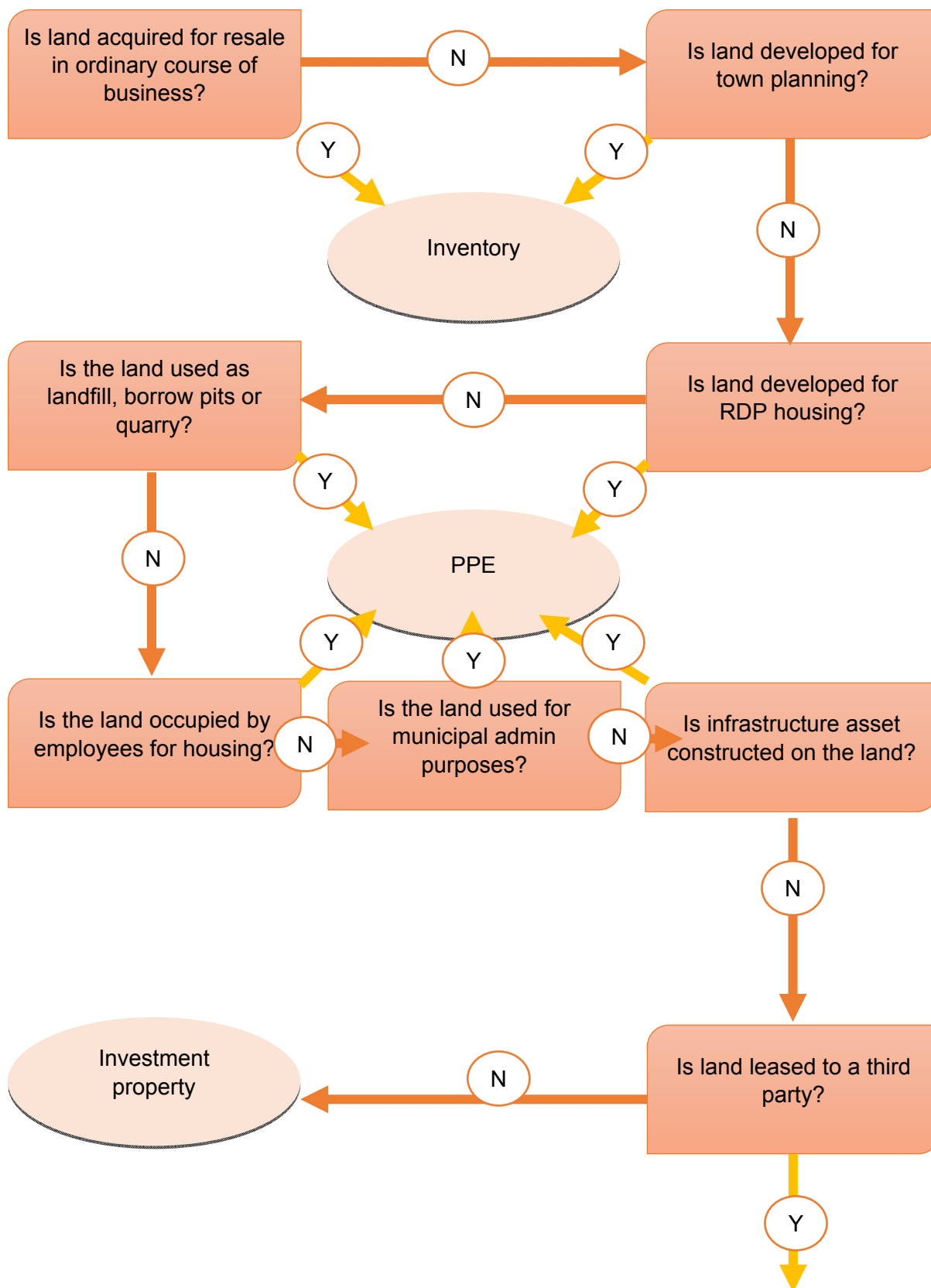
Component/Asset Type	Description	Unit	Unit Rate Jun 2008 excl. VAT
Land	refer to Water		R 0

### 6. Sport fields, parks, buildings and amenities

Component	Description	Unit	Unit Rate Jun 2008 excl. VAT
Golf course	9 hole – mache	№	R 2 412 000
	9 hole – municipal	№	R 7 236 000
	18 hole – municipal	№	R 14 472 000
Land	refer to Water		R 0
Sports field	Landscaping Grass, shrubs, trees	m <sup>2</sup>	R 51
	Cricket	№	R 1 809 000
	Football/rugby	№	R 723 600



## Appendix B – Decision tree





## Appendix B - continue

