

Capital Asset Policy for Financial Reporting Purposes in Government

Indiana League of Municipal
Clerks and Treasurers
Annual Conference, Evansville, Indiana
November 8, 2021

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Michael M. Nielsen
Government Fixed Asset Services, Inc.
Long Beach, Indiana 46360
773 294 0944
219 221 6147
nielsen@fixedassetservices.com

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Sources and Acknowledgments

First – State of Indiana, State Board of Accounts, *Accounting and Uniform Compliance Guidelines Manual for Cities and Towns* – Financial Reporting Requirements

Second – Governmental Accounting Standards Series, No. 171-A, Statement No. 34 of the Governmental Accounting Standards Board, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Government*

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State of Indiana, State Board of Accounts, *Accounting and Uniform Compliance Guidelines Manual for Cities and Towns* – Financial Reporting Requirements

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Cities and Towns Manual – continued

◆ *SBOA Accounting and Uniform Compliance Manual for Cities and Towns Disclosure Requirements*

- Capital Assets
 - Every unit must have a capital asset policy that details capitalization threshold
 - Every unit must have a complete listing of all capital assets owned reflecting acquisition value

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NO. 171-A | JUNE 1999

Governmental Accounting Standards Series

Statement No. 34 of the
Governmental Accounting
Standards Board

Basic Financial Statements—
and Management's Discussion
and Analysis—for State and
Local Governments



GOVERNMENTAL ACCOUNTING STANDARDS BOARD
OF THE FINANCIAL ACCOUNTING FOUNDATION

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Capital Assets for Financial Reporting

◆ GASB Statement No. 34 General Disclosure Requirements

- Capital assets should be reported at historical cost. The cost of a capital asset should include ... all costs that are directly attributable to asset acquisition. Donated capital assets should be reported at their estimated fair value at the time of acquisition plus ancillary charges, if any

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- ... the term capital assets includes land, improvements to land, easements, buildings, building improvements, vehicles, machinery and equipment, works of art and historical treasures, and all other tangible and intangible assets used in operations and have useful lives beyond a single reporting period

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- ... the term capital assets also includes infrastructure assets such as roads, rights-of-way, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems, (and potentially traffic signals, sidewalks, alleys)

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- ... Infrastructure assets are long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- Capital Assets should be depreciated over their estimated useful lives
- Depreciation expense is to be reported and measured by allocating the net cost of depreciable assets over their estimated useful lives in a systematic and rational manner

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- The policy for capitalizing assets and for estimating the useful lives of those assets (used to calculate depreciation expense) is a general disclosure requirement
- Current-period depreciation expense reporting is a required note disclosure

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- Capital assets that are being or have been depreciated should be reported net of accumulated depreciation in the statement of net assets.
- Capital assets should be depreciated over their estimated useful lives
- Land should not be depreciated

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- Information presented about major classes of capital assets:
 - ◆ Beginning- and end-of-year balances with accumulated depreciation presented separately from historical cost
 - ◆ Capital acquisitions

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continued

◆ GASB Statement No. 34 General Disclosure Requirements

- Information presented about major classes of capital assets, continued:
 - ◆ Sales or other dispositions
 - ◆ Current-period depreciation expense, with disclosure of the amounts charged to each of the functions in the statement of activities

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Part II

First – Analysis

Second – Examples

Third – Initial Implementation of Capital Assets - Management Decisions

Fourth – Considerations in the Process

Fifth – Conclusion

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Analysis and Allocation of Asset Account Balances

- ◆ By dollar amount
- ◆ By percentage of total
- ◆ This high level analysis takes minutes
- ◆ This process can assist setting priorities

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Municipal Example

Where's the Money

• Land/Rights of Way	\$28,715,361
• General Infrastructure	89,091,541
• Buildings	33,411,514
• Improvements other	14,146,333
• Vehicles	11,829,835
• Equipment	<u>4,383,862</u>
	\$181,578,446

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Municipal Example

Money by percentage of total

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Municipal Example

Equipment dollar amount and percentage impact of increasing capitalization threshold (for example) to \$25,000

- Equipment = \$4,383,862 represents 2.4% of total capital assets of \$181,578,446
- Take note to just where the dollars and %'s regarding capital assets is are located!

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Municipal Example

Equipment by dollar amount and percentage impact of increasing capitalization threshold (for example) to \$25,000

- Exception #1 to the \$25,000 threshold is the capitalization of all land and rights-of-way regardless of size of parcel, location, date acquired, or acquisition value
- Exception #2 to the \$25,000 threshold is the capitalization of all licensed vehicles regardless of acquisition value

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Municipal Example

Equipment by dollar amount and percentage impact of increasing capitalization threshold (for example) to \$25,000

- **... let's think for a moment – slides 19 – 22 ... if considered and implemented can make accounting for capital asset easier and streamline the process of annual updating and reporting of capital assets**

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Capital Asset Policy

◆ Capital Asset Accounting MANAGEMENT DECISIONS

- These are your capital assets
- This is your financial reporting
- Your Policy is a series of and statement of 'your management decisions'

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Capital Asset Policy – Initial Implementation

- ◆ Management Decisions
- ◆ Issues and Considerations

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Capital Asset Policy

◆ Capital Asset Accounting MANAGEMENT DECISIONS

- Again, per the Governmental Accounting Standards Board in Statement No. 34 you must disclose in your policy
 - ◆ Capitalization threshold
 - ◆ Determination of estimated useful lives
 - ◆ How depreciation is to be calculated (straight/line method, no salvage, full-year/convention)

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Capital Asset Policy

◆ Capital Asset Accounting MANAGEMENT DECISIONS

- Examples of progressive capitalization thresholds that reflect asset accounts or classifications
 - ◆ Land capitalize all
 - ◆ Improvements to Land \$25,000
 - ◆ Buildings \$100,000
 - ◆ Furnishings/Equipment \$25,000
 - ◆ Vehicles capitalize all
 - ◆ General Infrastructure \$100,000

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Capital Asset Policy

◆ Capital Asset Accounting MANAGEMENT DECISIONS

- Examples of Asset Estimated Useful Lives
 - ◆ Land non-depreciable
 - ◆ Improvements to Land 20 years
 - ◆ Buildings 50 years
 - ◆ Furnishings/Equipment 5 years
 - ◆ Vehicles 5-15 years
 - ◆ General Infrastructure 50 years

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Capital Asset Policy

◆ Capital Asset Accounting MANAGEMENT DECISIONS

- Lifting best based on your experience
- You can choose no salvage
- You can choose depreciation method and convention
- Reference allocation of acquisition value / historical cost over time

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Capital Asset Policy

◆ Capital Asset Accounting MANAGEMENT DECISIONS

- ... here is when and where to make the entire process easy – so go easy on yourself
- Important to think through from a management perspective
- Project and decide what we can do and how to be successful

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Capital Asset Policy – Issues and Considerations

◆ Establishing a Capital Asset Policy

- You do need the approval (Ordinance) of your elected officials and administration
- Easier if you give auditors a 'heads up' as to your plans
- This is where the whole process of accounting for capital assets can be made easier and do-able

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Capital Asset Policy – Issues and Considerations

◆ What **is** a Capital Asset

- A new capital asset that is on a unit basis at or above the established capitalization threshold in cost or acquisition value
- An improvement that increases capacity, efficiency, or extends the estimated useful life of an asset beyond the original expectation

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Capital Asset Policy – Issues and Considerations

◆ What **is** a Capital Asset

- An addition to a building provides additional square footage and increased capacity and the capital outlay is capitalized
- Newly constructed or totally reconstructed roads are capitalized
- Widening a road increases capacity and efficiency and is capitalized

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Capital Asset Policy – Issues and Considerations

◆ What **is not** a Capital Asset

- Expenditures that do not result in increased capacity, efficiency or extension of estimated useful life by improving an asset with a major structural change or alteration
- Repairs and maintenance

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Capital Asset Policy – Issues and Considerations

◆ What **is not** a Capital Asset

- Minor assets below that are below the established capitalization threshold on a unit basis are expensed in the current year
- Common building maintenance including painting, plumbing repairs, HVAC upgrades and the like are expensed in the current year
- Re-surfacing a road, while costly, does not increase capacity or efficiency and is expensed in the current year

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Capital Asset Policy – Issues and Considerations

◆ Policy document

- Determinations to be made
 - ◆ System for initial information and for annually updating data as to additions and retirements and a re-calculation of depreciation as to annual, accumulated, and net book value amounts
 - ◆ Excel works just fine and can become the tool for annual updating and reporting

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Capital Asset Policy – Issues and Considerations

◆ Information exists

- Buildings
- General Infrastructure
- Vehicles

◆ Information for annually updating the property record

- Additions centrally
- Retirements from departments

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Capital Asset Policy – Issues and Considerations

- ◆ Establishing historical cost and date of acquisition
 - Estimates are absolutely acceptable
 - ◆ Per GASB Statement No. 34
 - ◆ In general per accounting and financial reporting
 - ◆ Acceptable in past using normal and standard costing to estimate historical cost
 - ◆ Acceptable in past using vintages and other comparisons to age assets via estimates

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Capital Asset Policy – Issues and Considerations

- ◆ Establishing historical cost and date of acquisition
 - Per GASB Statement No. 34 estimates are absolutely acceptable
 - ◆ ... if determining the actual historical cost of ... assets is not practical because of inadequate records, governments should report the estimated historical cost for ... assets that were acquired or significantly reconstructed, or that received significant improvements, in fiscal years ending after June 30, 1980

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Capital Asset Policy – Issues and Considerations

- ◆ Establishing historical cost and date of acquisition
 - Per GASB Statement No. 34 estimates are absolutely acceptable
 - ◆ ... a government may estimate the historical cost of assets by calculating a current replacement cost of a similar asset and deflating this cost through use of price-level indexes to the acquisition year (or estimated acquisition year if the actual year is unknown)

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Capital Asset Policy – Issues and Considerations

- ◆ In all of this don't let the perfect get in the way of the good
- ◆ Don't forget ... done is better than perfect

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Capital Asset Policy – Issues and Considerations

- ◆ A word about accuracy
 - Good faith effort
 - Unless egregious errors, your property record should be ok and acceptable
 - These are your government's capital assets to submit to your auditors (in light of your responsibility)

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Capital Asset Policy – Issues and Considerations

- ◆ A word about accuracy continued
 - Again your capital assets and your reporting BUT smart to run your decisions in this regard by your auditors – a bit of deference and avoidance of a surprise
 - (we can't forget that your capital asset total is the largest dollar amount in all of your Annual Financial Reporting)

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Capital Asset Policy – Conclusion

- ◆ Reference in all of this to ...
 - ◆ Take a least-cost approach
 - ◆ Keep it simple
 - ◆ Do implementation in-house and capitalize on professional staff, available information, and extensive resources
 - ◆ Consider an internal staff member or external facilitator to drive the process

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Capital Asset Policy – Conclusion

- ◆ Nothing Authoritative in the Accounting Literature
 - You have the latitude to make many decisions and, thus, to make the process easier
 - These are the 'management decisions' that are your opportunities and responsibilities to make

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Capital Asset Policy for Financial Reporting Purposes in Government

The End

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Addendum to today's
presentation –

Financial Reporting in the Future

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Financial Reporting in the Future

... Generally Accepted Accounting Principles (GAAP)

- Accounting and Financial Reporting which includes depreciation
- Focus on annual depreciation, accumulated depreciation, and net book value amounts

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Financial Reporting in the Future

... assuming that your Capital Asset Policy streamlines the process of reporting and depreciating capital assets ...

- Choose straight-line depreciation
- Take full year's depreciation year one
- Recognize no salvage value

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Depreciation

◆ Annual Straight-line Depreciation

- A vehicle with an acquisition value / historical cost of \$50,000 and a five year estimated useful life = 20% depreciation rate per year (so) $20\% \text{ depreciation rate} \times \$50,000 = \$10,000$ annual depreciation (again, full-year depreciation in year of acquisition and no salvage value)

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Depreciation

◆ Accumulated Depreciation

- Total of all annual depreciation from date of asset acquisition to current year end for a specific asset

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Depreciation

◆ Accumulated Depreciation

- Assume a three year old \$50,000 vehicle with a five year estimated useful life = 20% annual depreciation amount (so) annual depreciation of \$10,000 x three years = \$30,000 in total accumulated depreciation

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Depreciation

◆ Net Book Value

- With a calculation of all annual depreciation to date being \$30,000 in annual depreciation reported in the past and in current year, a \$50,000 asset has a Net Book Value of \$20,000

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Depreciation

◆ Net Book Value

- So, an asset's acquisition value / historical cost is equal to accumulated depreciation **plus** net book value

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Depreciation

- ◆ Straight-line depreciation means an equal amount of annual depreciation per year of estimated useful life – the 'life' of an asset becomes the divisor in this calculation
- ◆ No negative numbers in any calculation
- ◆ No salvage value

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Depreciation

- ◆ Net Book Value can be \$0 as it is ok to have fully depreciated assets
- ◆ Basic, uncomplicated, and simple formulas to do the calculations
- ◆ Formulas need to 'turn off' annual calculation when accumulated = acquisition value / historical cost and net book value = \$0

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Depreciation ... one more thing

- ◆ The calculation of accumulated depreciation includes all annual depreciation charged and reported in the past plus the current year's annual depreciation amount

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Conclusion to Depreciation Addendum

- ◆ Keep it simple
- ◆ Excel works quite economically
- ◆ Excel works very well for the initial implementation of a capital asset report

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Conclusion to Depreciation Addendum

- ◆ Worksheets can easily become your tool for annual updating and reporting
- ◆ Depreciation formulas are made simple and easy to work with when you choose straight-line depreciation and no salvage value

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Depreciation example

Urban Local Roads Calculations													RDV for Urban Local Roads Calculations					
Road Name	From	To	Length (miles)	Width (ft)	Year Constructed (before 1980 go to middle of decade)	Length x Width (yards ²)	Replacement Cost Total (\$)	*Deflation for Year Constructed	**Historical Total Cost (\$)	Asset Life (years)	*** Annual Depreciation (\$)	Accumulated Depreciation (\$)	Net Book Value (\$)	**** Weighted Average Width of RDV (ft.) (Use 43.4' if value is not known)	RDV Area (Acres)	Total Fair Value per Acre for RDV (\$)	***** Deflation for Year Acquired for RDV (Used CPI Deflator)	Historical Cost/Fair Value of RDV (\$)
Madson	500E	600E	2.2	20	2003	25,555	\$14,31,091	1.00	\$14,31,091	50	\$28,622	\$57,244	\$1,373,849	43.4	116	\$266,687	1.000	\$266,687
Jersey	Union Ch.	Hursh	1.9	22	1999	24,277	\$1,269,537	0.91	\$1,237,778	50	\$24,744	\$49,486	\$1,088,717	43.4	10.0	\$230,321	0.905	\$208,440
Akron	SR1	Ohio Rd.	3.6	25	2000	52,272	\$2,927,232	0.97	\$2,839,416	50	\$56,788	\$283,942	\$2,555,474	43.4	19.0	\$436,337	0.936	\$406,468
Pull	CR 261	Frosh	0.9	25	1940	13,068	\$731,808	0.09	\$65,863	50	\$6,586	\$32,931	\$698,877	43.4	4.7	\$189,099	0.102	\$11,928
Popp	Suton	500E	2.7	22	1965	34,500	\$1,331,973	0.17	\$228,435	50	\$6,586	\$262,749	\$56,687	43.4	14.2	\$327,298	0.175	\$57,113
Deer Track	Manick Rd.	600E	7.9	20	1989	91,768	\$5,138,918	0.72	\$3,700,021	50	\$74,000	\$1,894,007	\$2,516,014	43.4	41.6	\$957,649	0.674	\$645,456
David	Hursh	Frosh	1.5	22	1909	19,958	\$1,073,318	0.03	\$32,200	50	\$32,200	\$32,200	\$1,041,118	43.4	7.9	\$191,832	0.035	\$6,310
Sunflower	Treelane	600E	6.1	25	2002	98,572	\$4,360,032	0.99	\$4,310,432	50	\$86,208	\$294,626	\$4,015,806	43.4	32.2	\$739,451	0.978	\$723,183
Farmland	100V	SR 34	0.7	22	1954	8,944	\$500,882	0.15	\$75,132	50	\$7,513	\$37,566	\$463,316	43.4	3.7	\$94,855	0.147	\$12,455
Walton	Treelane	250S	2.7	25	1968	39,204	\$2,195,424	0.17	\$373,222	50	\$7,464	\$276,184	\$37,038	43.4	14.2	\$327,298	0.175	\$57,113
51	SR 40	250S	7.9	22	1975	100,943	\$5,852,810	0.36	\$2,095,012	50	\$40,700	\$1,221,007	\$914,005	43.4	41.6	\$957,649	0.295	\$272,547
Newton	SR1	100V	1.5	20	1974	17,424	\$375,744	0.36	\$351,268	50	\$7,025	\$17,788	\$133,482	43.4	7.9	\$191,832	0.285	\$91,749
Taylor	Frosh	Treelane	6.1	20	1964	70,858	\$3,368,028	0.17	\$674,564	50	\$13,491	\$553,143	\$121,422	43.4	32.2	\$739,451	0.175	\$129,034
Ross	Manick Rd.	Ohio Rd.	0.7	25	1932	10,844	\$593,184	0.06	\$34,151	50	\$3,415	\$17,075	\$576,109	43.4	3.7	\$94,855	0.077	\$6,559
# more rows are added please change the total sum equation										Total Sum:	\$357,613	\$4,706,493	\$3,381,491				Total Sum:	\$2,856,253

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Michael M. Nielsen
 Government Fixed Asset Services, Inc.
 Long Beach, Indiana 46360
 773 294 0944
 219 221 6147
 nielsen@fixedassetservices.com

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