ASSET CAPITALIZATION POLICY

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SCOPE OF POLICY

This Asset Capitalization Policy applies to the capitalization of capital assets purchased with NWCCOG funds. Assets purchased with grant funds will be expensed at the time of purchase.

GENERAL OBJECTIVES

This Asset Capitalization policy establishes guidelines for determining:

- Which expenditures should be capitalized as a capital asset and which expenditures should be expensed
- How to value capital assets that are reported
- The estimated useful lives of capital assets

CAPITAL ASSET TYPES

Capital assets are divided between assets that are not subject to depreciation and assets that are subject to depreciation.

Assets that are not subject to depreciation include:

- ***Land***. The amount that should be capitalized for land should include the cost of the land itself; professional fees used to acquire the land (legal, engineering, appraisal, survey fees); costs for excavation, fill, grading, or drainage; demolition of any existing buildings or other improvements; and any other costs that are incurred to acquire the land and make the land suitable for use by the Council. Land is characterized as having an unlimited life and is therefore not depreciated.
- ***Construction in progress***. The costs of assets that the Council is constructing, where expenses are incurred over more than one fiscal year, are accumulated as construction in progress until the asset is placed in service. At that time, the total costs are then transferred to the appropriate asset type and depreciated.

Assets that are subject to depreciation include:

- ***Land improvements.*** Land improvements are those improvements, other than ordinary and regular site preparation, which ready the land for its intended use. Such improvements can include parking lots, athletic fields, fencing, paths and trails, and landscaping.
- ***Buildings and building improvements.*** Buildings are permanent structures that are intended for shelter of persons, materials or equipment. Building improvements are capital events that extend the useful life of a building or increase the value of a building, or both. Repairs that simply maintain the existing life or restore a building to its original condition do not constitute an improvement.

- ***Equipment.*** Equipment is an item of tangible, nonexpendable personal property with a useful life of more than one year, and includes machinery and vehicles.

Collections (works of art or historical artifacts) meet the definition of capital assets and ordinarily would be reported in the financial statements. However, the requirement for capitalization of these assets is waived if the collection is held for reasons other than financial gain; the collection is protected, kept unencumbered, cared for, and preserved; and the collection is subject to a policy requiring that the proceeds from sales of collection items be used to acquire other items for collections.

EXPENDITURE TYPES

Repairs are the costs necessary for the upkeep of the property that neither add to the permanent value of the property nor appreciably prolong its intended life, but keep it in an efficient operating condition. These costs should not be capitalized.

CAPITAL ASSET VALUATION

Capital assets should be reported at their historical cost. In the absence of historical cost information, the assets estimated historical cost may be used. Assets donated by parties outside the municipality should be reported at their fair value on the date the donation is made. If capital assets are moved from one fund or activity to another, the recipient fund or activity should continue to report those assets at their historical cost as of the date they were originally acquired.

The historical cost of a capital asset should include ancillary charges necessary to place the asset in its intended location (freight charges, for example); ancillary charges necessary to place the asset in its intended condition for use (installation or site preparation charges, for example); and capitalized interest (only for those assets that are utilized in enterprise funds and internal service funds that are reported as a part of business-type activities).

Estimating the historical cost of capital assets for which invoices or similar documentation of historical cost are not available can use either standard costing or normal costing. Standard costing involves using historical sources, such as old vendor catalogs, to establish the average cost of obtaining the same or a similar asset at the time of acquisition. Normal costing involves establishing the current cost of the same or similar asset and deflating that cost using an appropriate price index.

CAPITALIZATION THRESHOLDS

By definition, any asset that benefits more than one fiscal period potentially could be classified as a capital asset. As a practical matter, however, governments capitalize only their higher cost assets. Capitalization thresholds are established to determine which assets are capitalized and which assets are expensed when purchased.

The Council must maintain adequate control over all assets, including lower-cost capital assets. Capitalization is designed to focus on the Council's financial reporting needs, and is not designed for or particularly suited for the purposes of ensuring control over lower-cost assets. Capitalizing numerous small cost items will actually overburden the overall capital asset management system. Capitalization thresholds are established based on financial reporting needs and other policies will determine how the Council controls lower-cost assets.

That said, bulk purchase of like capital assets with unit costs of less than $5,000 <u>may</u> be capitalized as a group where the allocation of costs for the bulk assets over time is matched to the corresponding revenue generated by the bulk assets

The Council establishes the following Capitalization Thresholds for the following groups of assets:

Land and land improvements	$ 10,000
Buildings and building improvements	$ 20,000
Equipment and vehicles	$ 5,000

REPLACEMENTS:

For building improvements, other than buildings and equipment, capitalize the cost of outlays that replace a part of another capital asset when the cost of the replacement is $5,000 or more **and** at least 10 percent of replacement value of the asset, or $10,000, whichever is less.

DEPRECIATION:

Assets that are capitalized will be depreciated over their estimated useful lives. Depreciation will be calculated on the straight-line basis, using estimated useful lives as follows:

Land improvements	10 – 50 years
Buildings and building improvements	10 – 75 years
Equipment and vehicles	3 – 25 years
Infrastructure	20 – 75 years

Because depreciation is intended to allocate the cost of a capital asset over its entire useful life, it normally is not appropriate to report assets still in service as fully depreciated. Instead, the annual amounts of depreciation expense should be reduced prospectively as soon as it becomes clear that an asset's useful life will be longer than originally estimated.