



## BEST PRACTICES

## Capitalization Thresholds for Capital Assets

State and local governments should adhere to appropriate guidelines for capitalization thresholds.

The term capital assets is used to describe assets that are used in operations and that have initial lives extending beyond a single reporting period. Capital assets may be either intangible (e.g., easements, water rights, licenses, leases) or tangible (e.g., land, buildings, building improvements, vehicles, machinery, equipment and infrastructure).

As a practical application of the materiality principle, not all tangible capital-type items with useful lives extending beyond a single reporting period are required to be reported in a government's statement of net position. Items with extremely short useful lives (e.g., less than 2 years) and/or of small monetary value are properly reported as an "expense" or "expenditure" in the period in which they are acquired.

When outlays for capital-type items are, in fact, reported on the statement of net position, they are said to be capitalized. The monetary criterion used to determine whether a given capital asset should be reported on the statement of net position is known as the capitalization threshold. A government may establish a single capitalization threshold for all of its capital assets, or it may establish different capitalization thresholds for different classes of capital assets. In selecting capitalization thresholds, governments should be able to report and depreciate substantially all capital asset value while eliminating the cost of tracking a large number of small-value items.

A government's threshold for capitalization does not need to be calculated in the same way that the government would measure the asset, if it is ultimately capitalized, for reporting in accordance with GAAP. For example, a government's capitalization policy may be to determine whether improvements to an office building (primarily plumbing and electrical upgrades) meet a dollar threshold (\$20,000) before including the cost of new window and floor treatments, which will be part of the improvements, because it does not consider those to be "core costs" of the asset improvement. For assets constructed by a government's own employees, the dollar threshold might distinguish between direct costs (time spent by construction workers, architects and engineers on that project) and indirect costs (allocated costs of the capital improvements department of public works).<sup>1</sup>

The capitalization threshold should not be the only factor used when determining if an item should be capitalized. A government should be cognizant of whether similar items are capitalized in order to be consistent in reporting. For example, assume a government, with a capitalization threshold of \$10,000, purchases two pieces of similar equipment. Item A was purchased three years ago for \$11,000, and item B was purchased in the current year for \$9,000. The government also incurred its own direct costs (time spent by construction workers, architects and engineers on that project) and indirect costs (allocated costs of the capital improvements department of public works) for both items, which increased the values of the items to \$13,000 for item A, and \$11,000 for item B. Without the inclusion of the government's own costs, item B would not have been capitalized, while other similar items would be capitalized because they were purchased at a higher price. In this case, the government may choose to capitalize item B for the sake of consistent treatment.

Capitalization is, of its nature, primarily a financial reporting matter. That is, a government's principal concern in establishing specific capitalization thresholds ought to be the anticipated information needs of the users of the government's external financial reports. While it is essential to maintain control over all potentially capitalizable items, there are more efficient means than capitalization for accomplishing this objective in the case of a government's smaller tangible capital-type items. Furthermore, practice has demonstrated that capital asset management systems that attempt to incorporate data on numerous smaller items are often costly and difficult to maintain and operate.

## Recommendation:

GFOA recommends that state and local governments adhere to the following guidelines for capitalization thresholds:

- Establish minimum cost and useful-life based thresholds to avoid the cost of capitalizing immaterial items;
- Establish a minimum capitalization threshold of \$5,000 for any individual item;
- Establish a minimum capitalization threshold of at least a two-year useful life for any individual item;
- Consider establishing different dollar capitalization thresholds for different classes of capital assets (i.e. land, infrastructure, buildings and improvements, and equipment);
- Capitalization thresholds are best applied to individual items rather than to groups of similar items (e.g., desks and tables), unless the effect of doing so would be to eliminate a significant portion of total capital assets (e.g., books of a library district);
- Governments should perform a periodic review of their capitalization thresholds;
- In establishing capitalization thresholds, governments that are recipients of federal awards should be aware of federal capitalization thresholds requirements; and
- Governments should exercise control over potentially capitalizable items that fall under the operative capitalization threshold but require special attention.

<sup>1</sup>) Note that while indirect costs pertaining only to capital projects should be capitalized, general overhead costs such as human resources services or the commissioner's office staff of an agency not exclusively performing capital work should not be allocated to capital projects and capitalized. [Accounting for Capital Assets, A Guide for State and Local Governments, Stephen J. Gauthier, GFOA, 2008].

This best practice was previously titled *Establishing Capitalization Thresholds for Capital Assets*.



<b>SOUTHERN MANATEE FIRE RESCUE DISTRICT DIRECTIVE</b>		
<b>DATE</b> January 1, 2014	<b>VOLUME</b> #1 <b>ADMINISTRATION</b>	<b>NUMBER</b> #152
<b>CATEGORY</b> <b>POLICY</b>		
<b>SUBJECT</b> <b>Fixed Asset Policy</b>		

**Purpose:**

To create a policy for the District in accordance to Florida Statutes 274 “Tangible Personal Property Owned by Local Governments” and Florida Administrative Code 69I-73.001 – 69I-73.006 “Inventory of Property” for the purposes of defining an asset, establishing a minimum dollar threshold for an asset, processes for the removal of asset from inventory, and establishing an annual account of District assets.

**Definitions:**

**Control Accounts** – means summary accounts designed to control accountability for individual property records. Unlike individual property records which establish accountability for particular items of property, control accounts accumulate the total cost or value of the custodian’s property and, through entries to the control accounts documenting acquisitions, transfers and dispositions, provide evidence of the change in that total cost or value over periods of time as well as total cost or value at any time.

**Cost** – means acquisition or procurement cost (i.e., invoice price plus freight and installation charges less discounts). In determining cost, the value of property exchanged by the custodian in satisfaction of a portion of the purchase price of new property shall not be deducted from the full purchase price regardless of any property “traded in” on the new property.

**Custodian** – means the person(s) to whom the custody of county or district property has been delegated by the governmental unit.

**Custodian’s Delegate** – means a person acting under the supervision of the custodian to whom the custody of property has been delegated by the custodian and, from whom the custodian receives custody receipts.

**Data Processing Software** – has the meaning set forth in F.S. 119.011 (6). Data processing software is not considered to be property within the meaning of these rules.

**Depreciated Cost** – means cost less accumulated depreciation.

**Financial System** – means the fund accounting process used by local government for recording cash and other financial resources, expenditures and other financial uses, together with all related liabilities and residual equities or balances.

**Governmental unit** – means the governing board, commission or authority of a county or taxing district or sheriff of the county.

Fiscal year – means the governmental unit’s fiscal year established pursuant to law; otherwise, it means the calendar year.

Identification Number – means a unique number assigned and affixed to each item of property to identify it as property held by the custodian and for the purposes of differentiating one item of property from another.

Property – means all tangible personal property, owned by a governmental unit, of a non-consumable nature.

Unaccounted for Property – means property held by a custodian, subject to the accountability provisions of Section 274.03 of the F.S., which cannot be physically located by the custodian or custodian’s delegate, which property has not been otherwise lawfully disposed of.

Value – means the worth or fair market value at the date of acquisitions for donated property.

**Capital Asset Definition, Classes, and Capitalization Thresholds:**

All tangible personal property with a value or cost of \$1000 or more and having a projected useful life of one year or more shall be recorded in the financial system as property for inventory purposes. Cost is used if the property is purchased and represents the purchase price of the property item. Value is used if the property is donated and represents the fair market value of the property item at the date of donation. Southern Manatee Fire Rescue District reports the following asset classes:

- Land
- Buildings and building improvements
- Equipment

Capitalization thresholds have been established as follows:

Asset Class	Threshold
Land	Capitalize All
Buildings/Building improvements	Capitalize All
Equipment	\$1000 and above

**Cost of a Capital Asset:**

Capital assets should be reported at historical costs. The cost of a capital asset should include ancillary charges necessary to place the asset into its intended location and condition for use. Items to include in the cost of a capital asset are as follows:

- Original contract or invoice price
- Freight and transportation charges
- Import duties
- Handling and storage charges
- In-transit insurance charges

- Sales, use, and other taxes imposed on the acquisition
- Installation charges
- Charges for testing and preparation for use
- Costs of reconditioning used items when purchased
- Parts and labor associated with the construction of equipment
- Site preparation costs
- Professional fees

Costs of extended warranties and/or maintenance agreements, which can be separately identified from the cost of the equipment, should be not be capitalized.

Donated capital assets should be reported at their estimated fair value at the time of acquisition plus ancillary charge, if any.

**Depreciating Capital Assets:**

Capital assets should be depreciated over their estimated useful lives unless they are:

- Inexhaustible (i.e., land)
- Construction in progress

Southern Manatee Fire Rescue District uses straight-line depreciation (historical cost divided by useful life) applying the half-year convention method for all depreciable capital assets. It is the District's policy that capital assets have no residual value at the end of their lives other than apparatus.

**Disposition of Capital Assets:**

When a capital asset is disposed of, with a net book value greater than zero, a gain or loss must be recognized. A gain is reported when proceeds received are greater than the net book value of the asset. A loss is reported when the net book value is greater than the proceeds received. When proceeds received are equal to the net book value of the asset, a gain or loss is not reported.

**Capital Asset Classes:**

**Land**

The surface or crust of the earth, which can be used to support structures and roadways, and may be used to grow crops, grass, shrubs, and trees. Land is characterized as having an unlimited life (inexhaustible).

Betterments, site preparation and site improvements (other than buildings) that ready land for its intended use are added to the cost of the land.

Examples of expenditures to be capitalized as land are as follows:

- Purchase price or fair market value at time of gift
- Commissions
- Professional fees (title searches, architect, legal, engineering, appraisal, surveying, environmental assessments, etc.)

- Land excavation, fill, grading, drainage
- Demolition of existing buildings and improvements (less salvage)
- Removal, relocation, or reconstruction of property of others (railroad, telephone, and power lines)
- Accrued and unpaid taxes at date of purchase

Easements are interests in land owned by another that entitles its holder to a specific limited use. A right-of-way is a type of easement in which title remains with the property owner and therefore is not capitalized.

The estimated value of easements is immaterial and there will not be capitalized.

### **Buildings and Building Improvements**

A structure that is permanently attached to the land, has a roof, is partially or completely enclosed by walls, and is not intended to be transportable or moveable. A building is generally used to house persons, property, and fixtures attached to and forming a permanent part of such a structure.

Examples of items to be capitalized as buildings are as follows:

- Original purchase price and any other costs associated with getting the building ready for use
- All project costs associated with the original construction of a building

Improvements to existing buildings that materially extend the useful life a building, increase the value of a building, or both should be capitalized. The improvement must meet one of the following criteria:

- The improvement adds square footage to the existing building.
- The improvement is a major renovation that prepares an existing building for a new use.
- The improvement expenditure increases the life or value of the building by 25 percent of the original life or cost.

Examples of expenditures to be capitalized as building improvements are as follows:

- Replacement of an old shingle roof with a new fireproof tile roof
- Upgrade of heating and cooling systems
- Structures attached to the building such as covered patios, sunrooms, garages, carports, enclosed stairwells, etc.
- Structural changes such as reinforcement of floors or walls, installation or replacement of beams, rafters, joists, steel grids, other interior framing.

The following are examples of expenditures not to capitalize as improvements to buildings. Instead, these items should be recorded as ***maintenance expense***.

- Adding, removing and/or moving walls relating to renovation projects that are not considered major rehabilitation projects and do not increase the value or life of the building
- Plumbing or electrical repairs
- Cleaning, pest extermination, or other periodic maintenance
- Interior decoration, such as draperies, blinds, curtain rods, wall paper
- Maintenance-type interior renovation, such as repainting, touch-up plastering, replacement of carpet, tile or panel sections; sink and fixture refinishing, etc.
- Maintenance-type exterior renovation such as repainting, replacement of deteriorated siding, roofing, or masonry sections
- Replacement of a part or component of a building with a new part of the same type and performance capabilities, such as replacement of an old boiler with a new one of the same type and performance capabilities.

### Equipment

Fixed or movable tangible assets to be used for operations, the benefits of which extend beyond one year from date of acquisition and the cost is greater than \$1000.

Examples of expenditures to be capitalized as equipment include but are not limited to:

- Machinery
- Computers (file servers)
- Copy Machines (not leased)
- Radios
- Vehicles
- Furniture

The District shall use Best Practices for Governments and/or NFPA Standards in regards to establishing life expectancy of equipment.

### Recording of Property

The District shall maintain adequate records of property in their custody. The records shall contain at a minimum, the information required by Florida Law. Each item of property shall be accounted for in a separate property record. Related individual items which constitute a single system may be designated as a property group. A property group may be accounted for in one record if the component items are separately identified with the record. Examples of this would be modular furniture, and extrication equipment. All property group items, the total value or cost of which is equal to or greater than \$1000 shall be inventoried.

Each property record shall include the following information:

- Identification number.
- Description of item or item(s).
- Physical location (address, Station #, Vehicle #, etc.)
- Name of custodian with assigned responsibility for the item.

- In the case of a property group, the number and description of the component items comprising the group.
- Name, make or manufacture if applicable.
- Year and/or model(s) if applicable.
- Manufacturer's serial number(s) if any, and if a vehicle, vehicle identification number (VIN) and title certificate number if applicable.
- Date acquired.
- Cost or value at the date of acquisition for the item or the identified component parts thereof. When the historical cost of the purchased property is not practicably determined, the estimated historical cost of the item shall be determined by appropriate methods and recorded.
- Method of acquisition and, for purchased items, the voucher and check or warrant number.
- Date the item was last physically inventoried and the condition of the item at that date.

The District shall maintain a unit-wide control account showing the total cost or value of the custodian's property. Entries to control accounts shall be derived from documents evidencing transactions affecting the acquisition, transfer or disposition of property items and shall be posted contemporaneously with entries to the individual property records.

Depreciation shall be recorded to meet the District's financial report requirements relating to depreciation accounting. However, depreciation shall not be recorded on the individual property records or in control accounts in such a manner as to reduce the recorded acquisition cost or value (i.e., depreciation shall be recorded as item separate from the acquisition cost).

#### **Marking of Property Records**

Each property item shall be permanently marked with the identification number assigned to that item to establish its identity and ownership by the District holding title to the item. The marking shall visually display the property identification number (barcode) of the item.

Items of a similar nature shall be marked in a similar manner to facilitate identification. In determining a marking location, careful consideration shall be given to the intended use of the items; the probability that the marking could be obliterated by wear, vandalism or routine maintenance functions; and, the appropriateness of the marking method chosen. Electronic scanning codes shall be placed on property in the same manner as other markings specified above.

#### **Disposition of Property**

Property within the meaning of this policy may be lawfully disposed of, as provided in Section 274.05, 274.06 and 274.07 of the Florida Statutes. Property that is not accounted for during the annual audit will be handled under the procedure outlined below.

The following information shall be recorded on the individual property record for each item lawfully disposed of:

- Date of disposition.

- Authority for disposition (resolution of the Board properly recorded in the minutes as required by Florida Statute 274.07.
- Manner of disposition (sold, donated, transferred, cannibalized, scrapped, destroyed, traded).
- Identity of the employee(s) witnessing the disposition, if cannibalized, scrapped or destroyed.
- For items disposed of, a notation identifying any related transactions (such as receipt for sale of the item, insurance recovery, trade-in).
- For property certified as surplus, reference to documentation evidencing that such property was disposed of in the manner prescribed by Florida Statute 274.05 or 274.06.

The individual property record for each item lawfully disposed of, upon disposition of the item, transferred to a disposed property file. Destruction of such records shall be in accordance to the provisions of Florida Statute 119.

### Inventory of Assets

The District shall ensure a complete physical inventory of all assets is taken annually and whenever there is a change of custodian or change of custodian's delegate.

At a minimum the following information must be documented for each asset:

1. Date of inventory.
2. Identification number.
3. Existence of property item (or not).
4. Physical location (address, Station #, room number or compartment number)
5. Present physical condition.
6. Name and signature of the employee or other individual attesting to the existence of the item.
7. In the case of a property group, the number and description of the component items comprising the group.

The District currently utilizes electronic scanning of its fixed assets. Electronic scanning is acceptable as long as the recorded data is downloadable to a computer for the purposes of generating reports. These reports must include at a minimum the above listed information.

Any item found during the annual audit of assets which meets the requirements for accounting and control as defined by this policy, and which this is not on the inventory list, shall have the above information recorded and a number is to be issued.

Upon completion of the annual audit of assets, the data collected shall be compared with the previous year's data and/or the data contained on the computer database. Noted differences such as location, condition, etc. shall be reported to the custodian for investigation and corrected as appropriate or alternatively, the asset item should be relocated to its original assigned location as recorded on the database record.

Item(s) not located during the annual audit of assets shall be promptly reported to the Administration, which shall cause a thorough investigation to be made. If the investigation

determines that the item was stolen, the individual asset item record shall be so noted and a report filed with the Manatee County Sheriff's Department describing the missing item and the circumstances surrounding its disappearance.

For items identified as unaccounted for, the custodian shall conduct a thorough inspection to try to locate the unaccounted item by starting at the location of where the item was seen during the last audit and then expanding out to all District facilities.

If the item is still unaccounted for, the District shall then contact the Manatee County Sheriff's Department for the purposes of filing a report. A copy of this report will be attached to the unaccounted item property record.

The Custodian will then proceed with the procedures of removal of the unaccounted item from the District's Inventory of Assets. Final removal is through Board action by resolution.