Capital Assets & Depreciation Policy
GASB Statement 34 Edition
Effective July 1, 2002 and Approved by Council on June 9th, 2003

Overview

The City of Marshalltown wishes to establish accounting control and accountability for the City's assets. The Finance Department is the central accounting locale for all audited fixed assets. Assets under this classification follow specific accounting rules and are subject to annual audit requirements. The accounting and reporting policies of the City conform to generally accepted accounting principles (GAAP) applicable to state and local governments. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The City applies all applicable Government Accounting Standard Board pronouncements as well as follows all Financial Accounting Standard Board Statements and Interpretations, Accounting Principles Board Opinion and Accounting Research Bulletins of the Committee on Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. Any change to one of the referenced authoritative accounting pronouncements will supersede all financial reporting requirements referenced within this policy.

Capital Assets Definition

Capital assets are real or personal property that have a value equal to or greater than the capitalization threshold for the particular classification of the asset and have an estimated life of greater than one year. They include: land, land improvements, buildings, building improvements, machinery and equipment, vehicles, infrastructure, leasehold improvements, works of art and historical treasures and construction in progress (excluding projects from outside developers). A capital asset is to be reported and, with certain exceptions, depreciated in government-wide statements. In the government-wide statements, assets that are not capitalized are expended in the year of acquisition.

Infrastructure assets are long-lived capital assets that normally can be preserved for a significantly greater number of years than most capital assets and that are normally stationary in nature. Examples include roads, bridges, tunnels, drainage systems, water systems, and dams. Infrastructure assets do not include buildings, drives, parking lots or any other examples given above that are incidental to property or access to the property.

Inventory Records

Completeness and accuracy of inventory records should be ensured through physical counts, review of purchase records, prior inventory count records, listings maintained by other agencies, and other methods deemed necessary.

An inventory of all capital assets that meet or exceeds the City's threshold limits shall be maintained. Each inventory record should include: description, year of acquisition, method of acquisition (e.g., purchase, donation, etc.), funding source, cost or estimated cost, salvage value, and estimated useful life. The inventory record will also need to identify the function(s) that use the asset. The inventory of assets will be centrally maintained through the Finance Department.

Establishing and Setting the Threshold Levels for Recording Capital Assets

GASB Statement #34 does not give a "complete" definition of a capital asset. Paragraph #19 is a good beginning in that it lists the many categories, but that is not enough. Estimated useful life, asset cost, associated debt, and exceptions must also be considered. Explanations of the other criteria and the threshold levels for capitalizing and depreciating are:

Estimated Useful Life - The first criterion is useful life. An asset must have an estimated useful life greater than one reporting period to be considered for capitalization and depreciation. Assets that are consumed, used-up, habitually lost or worn-out in one year or less should not be capitalized.

Estimated useful life means the estimated number of months or years that an asset will be able to be used for the purpose for which it was purchased. In determining useful life, the City should consider the asset's present condition, use of the asset, construction type, maintenance policy, and how long it is expected to meet service demands.

Asset Cost - The second criterion for determining depreciable capital assets is cost. The City does not need to capitalize every asset with a useful life greater than one year. To do so is an unnecessary burden and will not materially affect financial results. The table listed below will be used in determining the dollar thresholds to use for tracking the City's capital assets. The capitalize and depreciate column will be audited on an annual basis as part of the external auditors fieldwork.

Capitalize and Depreciate Thresholds

Land	$1 - Capitalize only
Land Improvements	$5,000
Building	$5,000
Building Improvements	$5,000
Machinery and Equipment	$5,000
Works of art and historical treasurers	$5,000
Infrastructure – based on total project cost	$50,000
Sanitary Sewers & Lift Stations	$50,000
Construction in Progress	Capitalize only

Associated Debt - The third criterion is associated debt. The City should carefully consider the merits of capitalizing assets purchased with debt proceeds. Doing so may minimize the potential of negative net assets being reported in the statement of net assets.

Recording Land, Rights of Way and Easements:

Land:

Land is to be capitalized but not depreciated. It is recorded at historical cost and remains at that cost until disposal. If there is a gain or loss on the sale of land, it is reported as a special item in the statement of activities. All land will be capitalized unless the City plans to immediately sell it instead of putting it to use.

The following items should be included as part of the cost of land: purchase price or fair market value at the time of the gift; commissions; professional fees (title searches, legal, appraisal, etc.), grading, removal, relocation, or reconstruction of property of others (railroad, telephone and power lines); interest on mortgages accrued at date of purchase; accrued and unpaid taxes at date of purchase; other costs incurred in acquiring the land. All land will be capitalized, regardless of cost, unless it is saleable land (land that the City has plans to sell instead of using).

Rights of Way (ROW)

ROW costs will be booked at the time of the project. If ROW costs are known at the time of the project, those values will be set up based upon actual costs. If the actual cost is not available, a cost per square foot will be determined by using an assessor's valuation of bare agricultural land in the vicinity.

Easements

An easement is an interest in land owned by another that entitles its holder to a specific limited use or enjoyment (right to use the land). The City has no ownership interest in the property associated with easements across private property, only a right to access the property for the stated use (i.e. water lines, sewer lines, etc). Therefore, easements are not reported in the financial statements.

Recording Land Improvements

Land improvements consist of betterments, other than buildings, that ready land for its intended use. A few examples include retaining walls, parking lots, sidewalks, outdoor lighting, fencing/gates, and landscaping. Land improvements can be further categorized as non-exhaustible and exhaustible.

Non-Exhaustible - Expenditures for improvements that do not require maintenance or replacement, expenditures to bring land into condition to commence erection of structures, expenditures for improvements not identified with structures, and expenditures for land improvements that do not deteriorate with use or passage of time are additions to the cost of land and are generally not exhaustible and therefore not depreciable. The portion of the cost attributable to nondepreciable land improvements should be reported with other assets not being depreciated, such as land and construction in progress in the Comprehensive Annual Financial Report (CAFR).

Exhaustible - Other improvements that are part of a site, such as parking lots, landscaping and fencing, are usually exhaustible and are therefore depreciable. Depreciation of site improvements is necessary if the improvement is exhaustible. Other items include: fencing, gates, landscaping, outside sprinkler systems, athletic fields, golf courses, septic systems, stadiums, swimming pools, tennis courts, fountains, retaining walls, bleachers, soccer fields, recreational lighting, parking lots, sidewalks, bus ramps, etc.

Recording Buildings

Buildings should be recorded at either their acquisition cost or construction cost. The cost of new construction should be carefully evaluated. Usually projects consist of major components such as land, land improvements, building construction (including professional fees and permits), furniture, fixtures and equipment. The various components should be broken out when setting up the initial building construction project. The components of the building itself (heating/air conditioning, carpet, windows etc.) should be included in the initial cost of the building.

Recording Building Improvements

Building improvements that extend the useful life of the building by more than 25% should be capitalized. Examples of building improvements include major roofing projects that tear the original roof down to the joints or peak a flat roof, major energy conservation projects, or remodeling and replacing major building components. Normal maintenance and repair projects like re-shingling or re-tarring a roof will be expensed. The inventory will need to include a project description, the year completed, funding source and dollar amounts. Only those projects that meet the capitalization threshold need to be included.

Recording Equipment and vehicles:

Assets such as furniture, shop equipment, lawn equipment, computers, machinery, and other equipment that meet the threshold levels should be identified and inventoried. Some assets, individually, may fall below the capitalization threshold but may be purchased in large quantities by the governmental entity. Examples include library books, textbooks and computers.

Library Books

Library books are considered to have a useful life of more than one year. They are considered capital assets and are depreciable. The collections will be grouped based on fiscal year purchase and set up in the aggregate. Periodicals will be excluded from the annual purchase cost. This category will be included with Machinery and Equipment on the financial statements.

Computer Equipment

Computers will be excluded if they individually cost less than the threshold limit. If the dollar amount exceeds the limit, those assets will be capitalized and depreciated.

Vehicles

Vehicles should be identified, inventoried, and depreciated if they exceed the threshold limit. When setting up the initial costs of the vehicle, lettering will be added to the cost of the vehicle. In addition, for the police department; the cost of the sirens, light bars etc. will be included as part of the cost of getting the car into service. In the case of moving existing sirens etc, that cost will be included as part of the initial cost associated with new purchases.

Leased Equipment

Equipment should be capitalized if the lease agreement is non-cancelable **and** meets any one of the following criteria:

* The lease transfers ownership of the property to the lessee by the end of the lease term.
* The lease contains a bargain purchase option.
* The lease term is equal to 75 percent or more of the estimated economic life of the leased property.
* The present value of the minimum lease payments at the inception of the lease, excluding executory costs, equals at least 90 percent of the fair value of the leased property.

Leases that do not meet any of the above requirements should be recorded as an operating lease in the financial statements.

Recording Works of Art and Historical Treasures

Works of art, historical treasures, and similar assets should be recorded at historical costs if the dollar amount exceeds the capitalization threshold or fair value at date of donation (estimated if necessary) whether they are held as individual items or in a collections.. Depreciation is not required for collections or works of art that are inexhaustible. Exhaustible collections or individual items whose useful lives are diminished by display or educational or research applications, should be depreciated over their estimated useful lives.

Recording Infrastructure Assets -Determining Historical Cost or Estimated Historical Cost

As most new infrastructure construction is associated with a project, with certain funds set aside based on the project, infrastructure items will be evaluated based on the total cost of the project. Any project with a total cost that meets the threshold for infrastructure should be capitalized, with the council date of acceptance as the acquisition date. If a project includes more than one type of infrastructure, each part of the project should be set up. In addition to the actual construction costs, engineering fees and other incidental expenses should be added into the project cost. If engineering costs cannot be determined for each segment, then the costs should be prorated to each segment based on the segment's percent of the overall project (excluding costs that will be allocated).

If ownership of infrastructure associated with land, such as roads, sewers etc is unclear, the government with primary responsibility for managing the asset should report the asset.

Streets, roads and other components

The City will include frontage roads and alleys as part of the street & roads network if they exceed the dollar threshold. Within this category, the original project will include costs associated with curb and gutter. Roads will be broken down by the following types: seal coat, gravel, concrete, asphaltic concrete and brick or stone. Sidewalks constructed on private property will be excluded from the total cost of the project.

Bridges

Bridges will be a network of its own and broken down into vehicular and pedestrian subsystems. The cost of the initial project will include the sidewalk and guardrails associated with the bridge. The bridges will be further broken down into the classifications listed in the class lives schedule.

Sidewalks

Although the City does own the sidewalks that are on city ROW, private residents are responsible for maintaining them; therefore the City will not be capitalizing sidewalks as an infrastructure asset. Other sidewalks associated with property owned and maintained by the City will be classified as a land improvement and subject to the category threshold limits of that class.

Street Signs

The street department installs the street signs after the project is complete. The cost of the signs is not part of the construction costs. Currently the annual budget amount for replacement is approximately $25,000. Based upon the above criteria, the City will not be capitalizing street signs.

Street Lighting

Alliant Energy owns most of the streetlights except the decorative lights on main street, lights on bridges and some parking lot lights. Streetlights included in any project that meets the capitalization threshold will be capitalized as a part of that project.

Traffic Lights

Traffic lights will be evaluated by intersection and all intersections that meet the infrastructure threshold will be capitalized.

Storm Sewers

Detention ponds and other collection systems will be kept separate., Storm sewer projects often involve assets under different departments, such as replacing the street over the sewer that is being worked on. A project that involves replacing a section of storm sewers also included replacing the street that must be torn up. The entire project meets the capitalization threshold, but the street portion does not. The street portion will still be set up as a separate asset. The exception to this would be if the street is not improved by this process or is made worse; in this case the entire cost of the project would be under the sewer asset.

Bike Paths

The assets should be set up by project with the entire cost included in one asset. This will include benches, receptacles, engineering costs, etc, included in the initial project costs. They will not be set up separately with a parent number because this detail is not necessary in this case. Costs associated with the replacement of the benches, receptacles etc will be expensed in the year acquired.

Other infrastructure

* Obtain a description/inventory of the asset.
* The initial capitalization amount should be based on historical cost. If determining historical cost is not practical because of inadequate records, estimated historical cost may be used.

Recording Sanitary Sewers and Lift Stations

Capital assets in this category will be further broken down into the following classifications: sanitary sewers and lift stations. If the sanitary sewer and/or lift station is part of a project, whether the City or a private developer finances it, that has a total cost of $50,000 or more, it/they will be capitalized.

Recording Construction in Progress

Construction in progress that is financed by the City should be capitalized and not depreciated. It should be reported with land and other non-depreciating assets at the government-wide level. Unspent debt proceeds from capital assets related debt should be reported in the net assets section of the statement of net assets as "restricted for capital projects."

Capital Asset Donations

GASB Statement No. 33, Accounting and Financial Reporting for Non-Exchange Transactions, defines a donation as a voluntary non-exchange transaction entered into willingly by two or more parties. Both parties may be governments or one party may be a nongovernmental entity, including an individual. A voluntary contribution of resources between state agencies is not a donation. Donated capital assets should be capitalized at the fair market or appraised value of the asset at the date it was donated.

Real estate

All gifts of real estate must have council approval prior to title transferring. Contributed capital assets are valued at their appraised or estimated fair market value on the date donated.

Developers

Private developers will install infrastructure that will be given to the City. The acquisition date will be the date the council accepts the development. The developer must give the City the following contract item amounts to correctly capitalize each component of the development into the appropriate classification.

- Land or rights of way cost, including square footage
- Breakdown of the quantity and cost of the following components of the project:
  - Storm sewer
  - Lift stations
  - Sanitary sewer
  - Water mains
  - Street, curb and gutter
  - Traffic signals
  - Bike paths
  - Street lights
- Engineering costs

The Engineering Department will be responsible for obtaining this information from the developer.

Obtaining an Asset's Cost or Acquisition Value

Capital assets should be reported at historical cost and should include the cost of freight, site preparation, architect and engineering fees, etc. If something other than cash is used to pay for the asset, then the fair-market value of the non-cash payment or consideration determines the asset's cost or acquisition value. When the value of the consideration paid can't be determined, the asset's fair-market value determines its cost.

With few exceptions, an asset's cost should also include necessary costs incurred to place the asset in service. Costs include the invoice price plus incidental costs (insurance during transit, freight, capitalized interest as described earlier, duties, title search, registration fees, and installation costs).

Capitalized Interest

GASB 34 states and GASB 37 clarified that interest on general long-term debt generally should not be allocated to functions or programs as a direct expense. Therefore, unless the debt is expected to be retired by the enterprise fund, it is considered general long-term debt, and construction-period interest should not be included in the cost of the capital assets constructed.

Interest is capitalized on proprietary fund assets acquired with tax-exempt debt. The amount of interest to be capitalized is calculated by offsetting interest expense incurred from the date of the borrowing until completion of the project with interest earned on invested proceeds over the same period.

Repairs and Maintenance

The following table will determine if maintenance or repair should be capitalized or expensed. With respect to asset improvements, costs over $5,000 ($50,000 for infrastructure) should be capitalized if:

1. The estimated life of the asset is extended by more than 25%, or
2. The cost results in an increase in the capacity of the asset, or
3. The efficiency of the asset is increased by more than 10%, or
4. Significantly changes the character of the asset, or
5. In the case of streets and roads – if the work done impacts the "base" structure.

Otherwise the cost should be expensed as repair and maintenance.

Maintenance costs allow an asset to continue to be used during its originally established useful life. Maintenance costs are expensed in the period incurred. Preservation costs generally extend the useful life of an asset beyond its original estimated useful life, but do not increase the capacity or efficiency of the asset. Preservation costs are capitalized and depreciated if it extends the original estimated life by more than the assigned percent listed above.

A change in capacity increases the level of service provided by an asset. For example, additional lanes could be added to a road or the weight capacity could be increased. A change in efficiency maintains the same service level, but at a lower cost. For example, an electric generating plant could be reengineered so that it produces the same megawatts per day using less fuel.

The following improvements will be considered maintenance and not capitalized: tuckpointing, roof repair or replacement (unless it extends the life of the building, such as going from a flat roof to a pitched roof), window replacement (unless replaced with energy efficient windows), repainting, epoxy repair, re-carpeting, etc.

Depreciation

Definition

In accounting terms, depreciation is the process of allocating the cost of tangible property over a period of time, rather than deducting the cost as an expense in the year of acquisition. Generally, at the end of an asset's life, the sum of the amounts charged for depreciation in each accounting period (accumulated depreciation) will equal original cost less salvage value. Good accounting and financial management practices require that a government entity take both the cost expiration and the declining value of an asset into consideration. The cost expiration of a government entity's assets must be recognized if the cost of providing services is to be realistically reported. Also, the decline in the value of those assets must be considered if the government entity's net assets are to be stated correctly.

Information Needed to Calculate Depreciation

To calculate depreciation on a capital asset, the following five factors must be known:

* the date the asset was placed in service
* the asset's cost or acquisition value
* the asset's salvage value
* the asset's estimated useful life, and
* the depreciation method.

Asset's Salvage Value

The salvage value of an asset is the value it is expected to have when it is no longer useful for its intended purpose. In other words, the salvage value is the amount for which the asset could be sold at the end of its useful life. This value can be based on (1) general guidelines from some professional organizations such as GFOA, ASBO, etc., (2) information from other governmental entities, (3) internal experience, or (4) professionals such as engineers, architects, etc. Since the City normally keeps assets until there is not a remaining value, due to being obsolete, scrapped or junk, most equipment and vehicles should have a zero salvage value. In most cases, it is probable that many infrastructure assets will have no residual value, given the cost of demolition or removal.

Asset's Estimated Useful Life

Estimated useful life means the estimated number of months or years that an asset will be able to be used for the purpose for which it was purchased. In determining estimated useful life, a government should consider an asset's present condition, use of the asset, construction type, maintenance policy, and how long it is expected to meet service and technology demands. Useful lives should be based upon the government's own experience and plans for the assets. Although comparison with other governments or other organizations may provide some guidance, property management practices, asset usage, and other variables (such as weather) may vary significantly between governments.

It is difficult to come up with a "laundry list" of estimated useful lives for equipment when condition and usage are a factor. Let's take for example a city bus. A diesel bus is expected to last 250,000 miles. One city could put 250,000 on that bus in seven years, while another city will take 10 years. Therefore, the City has created it's own suggested useful lives table developed from using the above methods. This table can be periodically revised by city staff ; therefore it is not included as part of this policy, but will be maintained by the Finance Department

Depreciation & Convention Methods Used to Calculate an Asset's Depreciation

The City will use the straight-line method, which is the simplest and most commonly used for calculating depreciation. It can be used for any depreciable property. Under the straight-line depreciation method, the basis of the asset is written off evenly over the useful life of the asset. The same amount of depreciation is taken each year. In general, the amount of annual depreciation is determined by dividing an asset's depreciable cost by its estimated life. The total amount depreciated can never exceed the asset's historic cost less salvage value. At the end of the asset's estimated life, the salvage value will remain. For example, a $12,000 copier is placed in service on March 16, 2000. It has an estimated life of five years and a salvage value of $2,000. The depreciation calculation for the straight-line method would be:

Original cost	$12,000
Salvage value	2,000
Adjusted basis	$10,000
Estimated life	5
Depreciation per year	$ 2,000

To avoid the complications of depreciating each asset from the specific date on which it was placed in service, GAAP supports guidelines that assume various assets are placed in service or disposed of at designated dates throughout the year. These guidelines are called averaging conventions.

It is recommended that governmental entities use the full-month convention, therefore the City of Marshalltown will use this convention. Under the full-month convention, property placed in service at any time during a given month is treated as if it had been placed in service on the first day of that month. This allows depreciation to be taken for the entire month in which the asset is placed in service. If the property is disposed of before the end of the estimated useful life, no depreciation is allowed for the month of disposition.

Library books will use the straight line – half-year convention method of depreciating. Under this method of depreciating, the total cost for the year will have an acquisition date on the 1st day of the 7th month of the fiscal year.

Reporting Depreciation Expense in the Financial Statements
For general capital assets, depreciation is reported only on government-wide financial statements. Depreciation expense is reported on the Statement of Activities. Statement 34 requires that depreciation for assets specifically identified with specific functions is to be included in the direct expenses of those functions. Capital assets that serve essentially all functions are reported on a separate line or reported as part of the general administration (or its counterpart) function. If depreciation is reported as a separate line item, the face of the statement must clearly indicate that this line item excludes depreciation expense charged to functions.

City hall will be classified in the general government category and the associated depreciation expense will not be divided amongst the various departments that are housed within.

Depreciation expense for general infrastructure assets should not be allocated to the various functions. It should be reported as a direct expense of the function (for example, public works) that the reporting government normally associates with capital outlays for, and maintenance of, infrastructure assets or as a separate line in the statement of activities.

Disposal of Capital Assets
All assets included in this policy must be taken to Council for approval prior to disposition. The report to council will include the method of disposal whether it is for sale, obsolete, junked or other disposal reason.

When an asset is sold, a gain or loss must be recognized in the annual report when:
* Cash is exchanged and the amount paid does not equal the net book value of the asset.
* Cash is not exchanged and the asset is not fully depreciated or has a residual value.

Based on the answer from question #131 of GASB 34 implementation guide #1, GASB recommends that as a practical matter, insignificant gains or losses could be eliminated by adjusting the current period's depreciation expense by the amount of the gain or loss.

A gain or loss is not reported when:
* Cash exchanged equals the net book value and the asset does not have a residual value.
* Cash is not exchanged and the asset is fully depreciated and has no residual value.

Acquisition, Disposal and Transfer Forms

Special forms have been created for the acquisition of capital assets and infrastructure, in addition, to disposal of the capital assets. Forms will need to be completed for the following circumstances:

* All acquisitions whether it was purchased, donated or constructed will have the appropriate acquisition form completed by the receiving department and signed by the department head or other authorized personnel. The only exception to this is if the department is receiving an asset from another department and then the rules for transfers will apply.
* All dispositions of capital assets will have a disposition form completed by the department having ownership of the asset and will be signed by the department head or other authorized personnel of that department.
* A transfer form will be completed by the department transferring the asset and signed by the appropriate personnel.

The forms have been specially created to conform to the City's accounting software and will be maintained by the Finance Department.

Reporting Capital Assets in the Audited Financial Statements

Capital assets and the associated accumulated depreciation are reported in the Statement of Net Assets. Accumulated depreciation will be reported separately. Capital assets will be reported in greater detail by major class of asset (for example, infrastructure, buildings and improvements, machinery and equipment etc).

Insurance Records

The City will maintain insurance records in conjunction with the fixed assets. It is the responsibility of each department to notify the Finance Department concerning insurance coverage. Coverage, when applicable, must be added to new equipment prior to use. Reference the insurance guidelines procedures to see current deductibles and items to insure.

Record Retention

The Finance Department will keep individual asset detail associated with the capital assets that meet or exceed the city's threshold limits while an asset is current. Individual asset detail records may be disposed three years after an asset's disposal date. All fiscal year end reports can be disposed three years after the audit has been finalized unless grant provisions require a longer retention period. The recommendations from the "Record Retention Manual for Iowa Cities" will supersede any time periods covered in this paragraph if their retention period exceeds the time period listed.

Physical Inventories

The Finance Department or external auditors will periodically conduct a physical inventory of selected items. Assets not accounted for in the inventory shall be removed from the fixed asset records after the proper disposal procedures have been completed.

Implementation Dates for GASB 34

Marshalltown is a Phase 2 government with total annual revenues of $10 million or more but less than $100 million. Requirements of this Statement are for financial statements beginning July 1, 2002.

Prospective reporting of general infrastructure assets in the statement of net assets is required in fiscal year beginning July 1, 2002. Retroactive reporting of all major general infrastructure assets is encouraged at that date. However, the following dates are allowed to retroactively report infrastructure assets:

* Phase 2 governments should retroactively report all major general infrastructure assets for fiscal years beginning after June 15, 2006.