Town of Luray, Virginia

Capital Assets

Accounting Policies and Procedures Manual

Prepared for the

Town Council

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TABLE OF CONTENTS

INTRODUCTION

Proper accounting for capital assets is required by generally accepted accounting principles to obtain an unqualified opinion on the financial statements. It is also required by the Government Finance Officers' Association and is an essential ingredient in obtaining a Certificate of Achievement for Excellence in Financial Reporting. Capital assets accounting can also assist in planning for replacements and insurance coverage. To properly implement Governmental Accounting Standards Board Statement Number 34, Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments, the Town must account for its capital assets.

The term *capital assets* is defined to include: land, improvements to land, easements, buildings, building improvements, vehicles, machinery, equipment, works of art and historical treasures, infrastructure, and all other tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period.

CAPITAL ASSETS

In conformity with generally accepted accounting principles, guidelines of Government Accounting, Auditing and Financial Reporting (GAAFR) and the Government Finance Officers' Association (GFOA), the Town of Luray requires that for an asset to be capitalized it must be tangible or intangible in nature, have a life longer than one year, and have a significant value. Capital assets should be reported at historical cost. The cost of a capital asset should include capitalized interest (if an Enterprise Activity) and ancillary charges normal and necessary to place the asset into its intended location and condition for use. Ancillary charges include costs that are directly attributable to asset acquisition—such as freight and transportation charges, site preparation costs, installation costs, and professional fees. Donated capital assets should be reported at their estimated fair value at the time of acquisition plus ancillary charges, if any.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Improvements are capitalized over the remaining useful lives of the related fixed assets if restorative in nature, or as a new asset with the same initial life as the existing asset, if the life of the improvement is considered to extend the life of the existing asset.

Each capital asset is categorized and placed within a class of similar assets. Assets are classified as follows:

Land

Land improvements

Building & improvements

Equipment & Machinery

Vehicles

Infrastructure/Streets

Construction in progress

Capital Assets (Cont'd)

A description of each asset classification follows:

Land -The land capitalized fixed asset account should include all land and land rights purchased or otherwise acquired by the Town. The cost of land should include all legal and title fees, surveying fees, appraisal and negotiation fees, site preparation costs, and the cost of razing unwanted structures. Donated land should be recorded at fair market value at the time of donation. If land is acquired with a building as a single parcel, the value of the land should be determined at the time of the purchase and carried in the land fixed asset account. Where the historical cost of land is not available, historical cost values have been determined through construction costs indices to determine estimated historical cost, or estimated costs if construction costs indices are not available. 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). Therefore, easements are not required to be reported in the financial statements unless the entity paid for the easement.

Land improvements - The land improvements fixed asset account should include the value of all improvements to land at original price or cost of construction. If costs are associated with readying land for its intended purpose, then such costs are included in the cost of the land and are not separately accounted for as depreciable land improvement assets. Examples of land improvements include drainage and irrigation systems, fencing, landscaping (excluding ongoing costs of period cost landscaping, which would be expensed), swimming pools, parking lots and walkways.

Buildings and improvements - The building fixed asset account should include the value of all buildings at original purchase price or cost of construction. All structures used by the Town to house or safeguard equipment, services, people and functions should be included. All fixtures permanently attached to the building which cannot be removed without impairing the value of the building are considered part of the building. A donated building should be recorded at fair market value at the time of donation.

Additions and improvements to buildings including heating and ventilating system's, should be added to the building account when these costs are considered permanent additions and they exceed the capitalization thresholds. Improvements, including permanent additions, provide significant enhancement to an asset through an extended life cycle, increased productivity and/or efficiency, expansion of existing units, or addition of new units. Alterations are changes in the physical structure or arrangement of capital assets which do not qualify as increases in capital assets under the definitions of permanent additions. The cost of alterations should not be capitalized.

Where the historical cost of a building is not available, historical cost values have been determined through use of "backtrending". In "backtrending" the historical cost of an asset is estimated by taking the current cost of a similar asset and dividing it by construction cost index to determine estimated historical cost. In cases where construction cost indices are not available estimates were made.

<u>Equipment & Machinery and Vehicles</u> - The equipment & machinery fixed asset account group includes all machinery, power equipment, electronic data processing equipment, contractor's equipment, communication equipment, audio visual equipment, photographic equipment, kitchen equipment, laboratory, medical, duplication and photocopying equipment, mowers, and yard equipment. The vehicles fixed asset account group includes all motor vehicles and associated transportation equipment that is required to have a Vehicle Identification Number (VIN) as issued by the Department of Motor Vehicles. Vehicles whose acquisition cost does not meet the capitalization thresholds should still be listed on the fixed asset listing so that the vehicle fixed asset listing will be complete when compared to the insurance listing.

These assets include property that does not lose its identity when removed from its location and is not expended in use. The property is recorded at cost, including freight, installation, and other charges incurred to place the asset in service. If machinery or equipment is acquired through donation, the appraised value of the asset shall be established at the date of donation and used as the asset cost.

Equipment with a significant value in and of itself should be individually listed as an asset unit of one and given a unique asset number. Other identifying information such as make, model, serial number, size, capacity, material etc., as it applies, is recorded as part of the item description.

Infrastructure - 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. Examples of infrastructure assets include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems. Buildings, except those that are an ancillary part of a network of infrastructure assets, should not be considered infrastructure assets for financial reporting purposes.

Construction in Progress - Construction in progress should be capitalized and not depreciated. This classification of capital assets represents costs to date spent on projects that are not substantially completed at the end of the fiscal year. Costs are accumulated on such projects from year to year until such time as the projects are substantially completed and are transferred to another asset classification. Construction in progress should be reported with land and other non-depreciating assets at the government-wide level.

Capitalization Policy

All purchased fixed assets are valued at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated fixed assets are valued at their estimated fair market value on the date received.

Fixed assets to be recorded to the land, land improvements, building and improvements, equipment and machinery, vehicles, and construction in progress classifications are to cost $ 5,000 or greater, with the following exceptions:

All land is recorded.

All vehicles are recorded if they have a vehicle identification number.

Major additions, including those that significantly prolong a fixed asset's economic life or expand its usefulness, should be capitalized. Normal repairs that merely maintain the asset in its present condition should be not be capitalized. Generally, renovations, restorations, or improvements to existing buildings and infrastructure will be expensed unless the cost of the project exceeds $50,000.

Debt-financed acquisitions. On a case-by-case basis, an exception to the general rules above for capitalization may be made for significant repairs or acquisitions that are debt-financed, when the debt repayment period exceeds one year.

Accounting Procedures for Capital Assets

All assets acquired through June 30, 2017 will be valued at historical cost, as available, and by the used of backtrending as described above. Asset values will be determined using financial audit reports and accounting records. When original cost is not available asset values will be determined by the use of construction indices and other formulas designed to reflect historical cost.

Additions - All fixed assets purchased during the fiscal year, old and new, as well as all donated assets and assets acquired through capitalized leases are defined as current year additions. When an existing fixed asset has capitalizable additions or improvements, the additional costs will be added as a separate asset if the cost of the addition or improvement meets the capitalization threshold noted above.

Procedures to capture current year additions include a detailed examination of charges to capital outlay and capital project accounts by obtaining purchase orders/invoices/and other documentation supporting disbursements above the threshold amounts. Once criteria for determining an addition for fixed assets has been examined, the capital assets are identified as such and recorded in the fixed asset accounting system.

Capital assets may be acquired by eminent domain through condemnation proceedings. While the major part of the costs of these assets are the awards set by the court, the legal and recording fees must also be included.

Replacements - Replacements are assets acquired to replace previously capitalized assets which are being sold, abandoned, or otherwise disposed of. The replacement asset(s) is entered into the capital assets system in the same manner as a new asset. The asset(s) being replaced is removed from the records as described under dispositions.

ACCOUNTING PROCEDURES FOR CAPITAL ASSETS (CONT'D)

Dispositions - All assets sold, traded-in, scrapped, abandoned or in any way removed from service during the current fiscal year are classified as dispositions or disposals. Upon retirement, or other disposal, the acquisition cost of the asset is removed from the fixed asset listing.

Examinations of proceeds from various auctions, sale of surplus vehicles, and sale of salvage/surplus will be used to determine dispositions.

Transfers - A transfer is defined as any movement of an asset by virtue of change in location, either by account, department, building, floor or room. This change in location and/or managerial responsibility should be recorded in the fixed asset system. As the essential identifying information about the transferred asset is already contained in the system on inventory lists, it is only necessary to change those data fields affected, unless the system used has a transfer feature.

Maintenance - Maintenance refers to expenses that are necessary to achieve efficiency and neither materially prolong the original life nor appreciably increase the value of the asset. Maintenance expenses are not capitalized, but are considered current period expenditures.

Accounting Procedures for Capital Assets (Cont'd)

Annual capital asset inventory

Each department head will inventory all fixed assets under his/her control. Blank Capital asset inventory forms will be supplied each department head. Forms can be completed in Excel format and emailed to the Finance Department.

The following information will be maintained in subsidiary records for each individual capital asset:

- ☐ Major asset class;
- ☐ Function
- ☐ Reference to acquisition source document
- ☐ Acquisition date;*
- ☐ Name and address of vendor;*
- ☐ Description of asset;
- ☐ Manufacturer's serial number model number or other identification number
- ☐ Funding source of property;*
- ☐ Organization unit charged with custody
- ☐ Location;
- ☐ Fund and account from which purchased
- ☐ Estimated useful life;*
- ☐ Date, method and authorization
- ☐ Tag number (if applicable)

*Information to be obtained where available

Accounting Procedures for Capital Assets (Cont'd)

The following functions will be utilized to report capital assets:

- ☐ General government administration
- ☐ Judicial administration
- ☐ Public safety
- ☐ Public works
- ☐ Health and welfare
- ☐ Education
- ☐ Parks, recreation and cultural
- ☐ Community development

The following activities will be utilized to report capital assets:

- ☐ Town Council
- ☐ Town Manager
- ☐ Public Works
- ☐ Treasurer
- ☐ Library
- ☐ Finance and budget
- ☐ Police Department
- ☐ General property
- ☐ Recreation

Transaction Date - The date an asset is capitalized is the date the asset is placed in service. For most assets this will generally be the date the asset was purchased. For buildings, this will be the date the building was occupied or otherwise placed in service. These guidelines are applicable for additions as well as deletions and disposals. The key date is the day the asset was placed in or removed from service.

Depreciation - Capital assets should be depreciated over their estimated useful lives unless they are either inexhaustible or are infrastructure assets reported using the modified approach. Inexhaustible capital assets such as land and land improvements should not be depreciated.

Depreciation - Capital assets are depreciated over their estimated useful lives unless they are either inexhaustible or are infrastructure assets reported using the modified approach. Inexhaustible capital assets such as land are not depreciated. Depreciation expense is reported in the statement of activities for governmental and business type activities assets and in the fund statements also for enterprise funds. Depreciation expense is measured by allocating the net cost of depreciable assets (historical cost less estimated salvage value) over their estimated useful lives in a systematic and rational manner.

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.

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 (typically estimated to be zero)
- the asset's estimated useful life, and
- the depreciation method.

The Town depreciates all assets using the straight-line method and assumes no salvage value. The Town begins depreciating all assets in the year subsequent to acquisition. No depreciation is taken in the year of acquisition or disposition.

ACCOUNTING PROCEDURES FOR CAPITAL ASSETS (CONT'D)

Estimated Service Life - Life is the mean or normally expected duration of an asset. Life estimates are required for all asset units except land and land rights. Any extended life resulting from a major change in the asset unit is specified at the time of the change. The following estimated lives can be used as general guidelines:

	General Life (Years)
Building and Improvements	
Permanent buildings	40
Recreation facility i.e. concession stand	10
Land improvements - signs, fencing, pools	15
Machinery and equipment	
Kitchen equipment	10
Mowers and yard equipment	5
Small power tools	5
Large power tools: tractor, compactor	10
Bulldozers, graders, backhoe, and other equipment	10
Motor Vehicles	
Automobiles-police cars	5
Other automobiles	5
Light general purpose trucks	5
Heavy general purpose trucks	10
Other Equipment	
EDP hardware and software	5
EDP software	5
Office furniture	10
Copiers, duplicating equipment	5
Communication Equipment	
Base stations, mobile and hand transmitters, other communication equipment	10
Infrastructure	
Roads, bridges, sidewalks, curbs, guttering	30
Water and sewer systems	20-40
Pumps	15

Accounting Procedures for Capital Assets (Cont'd)

Financial Reporting - Capital assets that are being or have been depreciated are reported net of accumulated depreciation in the statement of net assets. Accumulated depreciation may be reported on the face of the statement or disclosed in the notes. Capital assets that are not being depreciated, such as land or infrastructure assets reported using the modified approach should be reported separately if the government has a significant amount of these assets. Capital assets also may be reported in greater detail, such as by major class of asset (for example, infrastructure, buildings and improvements, vehicles, machinery and equipment).