Chapter 30 – Fixed Assets

30.20 Valuing, Capitalizing and Depreciating Fixed Assets

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30.20.10 How to value Fixed assets

Fixed assets should be valued at cost, plus all ancillary charges necessary to place the asset in its intended location and condition for use.

30.20.10.a Determine the value of Fixed assets in the following manner:

Purchased Assets - Use historical costs including all non-refundable purchase taxes (e.g., sales taxes), plus all appropriate ancillary costs less any trade discounts or rebates. If the historical cost cannot be determined, use a reasonable estimated cost.

If land is purchased, the capitalized value is to include the purchase price plus costs such as legal fees, filling, and excavation costs incurred to put the land in condition for its intended use.

Building values should include both acquisition and capital improvement costs. Capital improvements include structures (e.g., office buildings, storage quarters, and other facilities) and all other property permanently attached to, or an integral part of, the structure (e.g., loading docks, heating and air-conditioning equipment, and refrigeration equipment). Departments have the option of capitalizing buildings by components when the useful lives of the components vary. Buildings owned by proprietary and trust funds are to include net construction period interest in arriving at the building value.

Furniture, fixtures, or other equipment not an integral part of a building are not considered capital improvements and should be classified as equipment. The cost for this asset type reflects the actual or estimated cost of the asset.

Include the cost of extended maintenance/warranty contracts in the asset valuation if the contract is purchased at the same time (or soon thereafter) as the Fixed asset. Depreciate these contracts over the useful life of the asset. Do not capitalize payments for contracts not purchased at the same time as the Fixed asset.

30.20.10.b **Self-Constructed Assets -** Capitalize all direct costs associated with the construction and department management costs associated with a construction project. Department project management costs may be capitalized in one of two ways:

1. Use actual project management costs directly associated with the project; or

2. Apply a percentage of total budgeted project costs. The application rate may or may not be designed to recover total agency project management costs. Exclude indirect costs unless they are increased by the construction.

In proprietary and trust funds, include net interest costs incurred during the period of construction in the capitalized cost of the asset, if material. Capitalized interest on assets constructed with tax-exempt borrowing should be netted against any interest earned on the investment of the proceeds of the related tax-exempt borrowings. Interest costs are not capitalized in governmental funds.

Self-Constructed Assets – Internally Generated Software – Software is considered internally generated if it is produced/created by the State, or if it is purchased from a third party, and requires more than an incremental effort before placed into operation.

Capitalize all costs relating to application development. Application development includes software configuration and interfaces, coding, installation of hardware, and testing.

Costs related to the preliminary project stage (i.e. conceptual formulation, determination of need, and final selection of alternatives) and the post implementation/operation stage (i.e. training and software maintenance) should be expensed as incurred.

Costs associated with payroll should be recorded using MS-TAMS (Maine State Time and Attendance Management System). Payroll costs should also indicate the project phase (preliminary project, application development, or post implementation).

30.20.10.c **Ancillary Costs** - Normally, ancillary costs should be included in the cost of a Fixed asset. However, minor ancillary costs, not measurable at the time a Fixed asset is recorded in the Advantage Fixed Asset Subsystem, are not required to be capitalized but may be capitalized if the information becomes readily available. Ancillary costs include such items as:

For land and Infrastructure:

- Legal and title fees;

- Professional fees of engineers, attorneys, appraisers, financial advisors, etc.;
- Surveying fees;
- Appraisal and negotiation fees;
- Damage payments;
- Site preparation costs; and
- Costs related to demolition of unwanted structures.

For buildings and improvements other than buildings:
- Professional fees of architects, engineers, attorneys, appraisers, financial advisors, etc.;
- Damage payments;
- Costs of fixtures permanently attached to a building or structure;
- Insurance premiums, interest (refer to Subsection 30.20.10.a), and related costs incurred during construction; and
- Any other costs necessary to place a building or structure into its intended location and condition for use.

For furnishings, equipment, collections, and other Fixed assets:
- Transportation charges;
- Sales tax;
- Installation costs;
- Extended maintenance/warranty contracts (refer to Subsection 30.20.10.a); and
- Any other normal or necessary costs required to place the asset in its intended location and condition for use.

30.20.10.d **Donated Assets** - Use the fair market value at the date of donation, plus all appropriate ancillary costs. If it is not practical to determine the fair market value, use a reasonable estimated cost. If land is acquired by gift, the capitalized value is to reflect its appraised or fair market value at the time of acquisition.

30.20.20 When to capitalize assets

Departments should capitalize assets that meet the minimum dollar threshold (see below) and will be used for more than one fiscal year. If the utility of an asset will be exhausted within one fiscal year the asset may be expensed when purchased.

State assets shall be capitalized by recording in Advantage according to the following thresholds:

- All land (including ancillary costs);

- Infrastructure, other than the State highway system, with a cost of $5,000 or greater;
- Buildings with a value of $100,000 or greater in the Proprietary Funds or $1,000,000 or greater in the Governmental Funds
- Software with a cost of $1,000,000 or greater
- All other Fixed assets with a unit cost (including ancillary costs) of $5,000 or greater, or collections with a total cost of $5,000 or greater, unless otherwise noted.

For Fixed assets acquired by and used in proprietary and trust fund type accounts, record the value of the assets in the fund itself.

Although small and attractive assets do not meet the State's capitalization policy above, they are considered controllable property for purposes of marking and identifying (refer to Section 30.30), inventory records requirements (refer to Section 30.40), and physical inventory counts (refer to Section 30.45).

Close out Construction in Progress and capitalize total, accumulated costs into the appropriate asset classification when a project is substantially complete, accepted, and placed into service.

30.20.20.a **New acquisitions –** Capitalize new assets that meet the State's capitalization policy as stated above.

Additions, improvements, repairs, or replacements to existing Fixed assets are not considered new acquisitions and are discussed below.

30.20.20.b **Additions –** Capitalize expansions of or extensions to an existing Fixed asset that meet the State's capitalization policy above.

30.20.20.c **Extraordinary repairs, betterments, or improvements –** Capitalize outlays that increase future benefits for an existing Fixed asset beyond its previously assessed standard of performance, if they meet the State's capitalization policy as stated above. Increased future benefits typically include:

- An extension in the estimated useful life of the asset.
- An increase in the capacity or efficiency of an existing Fixed asset.
- A substantial improvement in the quality of output or a reduction in previously assessed operating costs.

Leasehold improvements that meet the State's capitalization policy are recorded in the General Ledger as "Leasehold Improvements."

30.20.20.d **Replacements –** For buildings, improvements other than buildings, and equipment, capitalize the cost of outlays that replace a part of another Fixed asset when the cost of the replacement is $5,000 or more *and* at least 10 percent of the replacement value of the asset, or $100,000, whichever is less.

Example:

A $9,000 replacement of a heating boiler (which did not meet any of the criteria to be considered a betterment) in a building having a replacement value of $120,000 would *not* be capitalized. The $9,000 cost is not at least 10 percent of the building's replacement value. Had the building's replacement value been $90,000 or less, the $9,000 boiler replacement would have been capitalized.

EXCEPTIONS to this policy are:

- Replacement roof coverings are not capitalized (whether or not the replacement is with superior materials) unless the replacement extends the useful life of the building.

- Replacement floor coverings and window coverings are not capitalized.

- Costs to remodel (convert) a building to a different use, where the remodeling does not extend the useful life of the structure itself, are not capitalized.

Remove the capitalized value and the associated accumulated depreciation of the replaced Fixed asset or original building component from the accounting records if the amounts are determinable, and capitalize the cost of the replacement.

30.20.20.e **Renovations –** Capitalization Threshold for Renovations

A renovation enhances an already existing asset to a condition beyond that which results from normal maintenance repairs, and/or increases the useful life of the asset. Replacing a roof, or installing a better electrical system in a building, are examples of renovations.

Any renovation to a building must meet the following criteria to be included in the fixed asset system:

1. The cost must be more than $100,000.
2. The renovation must extend the useful life of the component.
3. The renovation must occur when 75% or more of the estimated useful life of the component being renovated has expired.

After determining that a renovation qualifies for inclusion in the fixed asset system, an additional test must be performed to determine whether the original component (being renovated) should be retired.

If the actual cost of the renovation is 75% or more of the replacement cost of the component at the time of completion, the original cost of the component should be retired.

Example:

Replace and upgrade the roof on the OGS Building. The estimated useful life of the roof is 20 years, the remaining useful life is 4 years, the replacement cost of the roof is $500,000, and the renovation actual cost is $400,000.

Does the renovation meet the 75% of the useful life test? Expired life/useful life = 16/20 = 80%; answer is yes.

This renovation would be included in the fixed asset system.

Does the renovation meet the 75% of the replacement cost dollars? $400,000/$500,000 = 80%; answer is yes.

The original component would be retired from the fixed asset system and a new asset recorded.

30.20.20.f **Bulk Purchase –** For proprietary funds, bulk purchases of like Fixed assets with unit costs of less than $5,000 *may* 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.

30.20.20.g **Collections –** Collections of Historical Treasures, Works of Art, Library Books, and other similar assets are to be capitalized if the conditions described in Section 30.20.22 are not met.

30.20.22 Assets not capitalized

30.20.22.a Collections of Historical Treasures, Works of Art, Library Books, and other similar assets are not required to be capitalized if their value does not diminish over time and if all of the following conditions are met:

- The collection is held for public exhibition, education, or research in furtherance of public service, rather than financial gain.
- The collection is protected, kept unencumbered, cared for, and preserved.
- The collection is subject to a department policy that requires the proceeds from sales of any collection items to be used to acquire other items for the collection.

Departments meeting these conditions have the option of capitalizing their collections.

Library resources are capitalized and may be carried on the department's property records as a single item.

For collections not capitalized, disclosures should provide a description of the collection and the collection meets the conditions, above.

Departments must be able to provide descriptions of their collections and the reasons the collections are not capitalized.

While these collections are not required to be capitalized, they are to be catalogued per Subsection 30.40.10.

Donations of works of Art, etc. must be recorded as revenue (GASB-33) and for collections not capitalized, a program expense must be recorded to offset the revenue (GASB-34, par. 28).

30.20.22.b Assets with values that fall below the capitalization threshold should be expensed. The exception being internal service funds which may want to capitalize these items as Type X in order to properly match revenues with expenses.

30.20.30 Capital Leases

The presence of a fiscal funding clause in a lease does not prevent the lease from qualifying as a capital lease, provided that the likelihood of the State invoking the fiscal funding clause is considered remote.

A capital lease is a lease with contractual terms that transfer substantially all the benefits and risks inherent in the ownership of property to the State. A capital lease is viewed as an installment purchase rather than a rental of property. A lease must meet one or more of the following four criteria to qualify as a capital lease:

1. Ownership of the leased property is transferred to the State by the end of the lease term; or
2. The lease contains a bargain purchase option; or
3. *The lease term is equal to 75 percent or more of the estimated useful life of the leased property; or
4. *If, at the inception of the lease, the present value of the minimum lease payments, excluding executory costs (usually insurance, maintenance, and taxes paid in connection with the leased property, including any profit thereon) is 90 percent or more of the fair value of the leased property. (The interest rate to be used in computing the present value is available by contacting the Division of Financial and Personnel Services (DFPS), and is the rate in effect at the execution date of the lease.)

*Neither the third nor the fourth criterion is to be applied when the inception of the lease (inception is the date of the lease agreement) occurs during the last 25% of the life of the asset.

If the lease meets any one of the above criteria, it is to be capitalized at the present value of the minimum lease payments up to the fair value of the leased property. Minimum lease payments include:

- Minimum rental payments - Minimum payments the lessee is obligated to make to the lessor under the lease agreement (excluding executory costs).
- Guaranteed Residual Value - The residual value is the estimated fair market value of the leased property at the end of the lease term. The lessor often transfers the risk of loss to the lessee through a guaranteed residual value. The guaranteed residual value is the certain or determinable amount at which the lessor has the right to require the lessee to purchase the asset, or the amount the lessee guarantees the lessor will realize.
- Penalty for Failure to Renew or Extend the Lease - The amount payable that is required of the lessee if the agreement specifies that the lease must be extended or renewed and the lessee fails to do so.
- Bargain Purchase Option - An option given to the lessee to

purchase the asset at the end of the lease term at a price that is fixed sufficiently below the expected fair market value so that, at the inception of the lease, purchase appears to be reasonably assured.

When lease agreements are capitalized, the property rights acquired under the lease are reported as an asset in the acquiring fund. For example, if the Office of Information Technology (OIT) has a capital lease with a vendor for telecommunications equipment they lease to the Department of Health and Human Services, OIT records the asset as theirs.

Capital leases in governmental funds will be reported only in the government-wide financial statements. Capital leases for proprietary fund types will be reported in the fund-level and government-wide statements, similar to other assets of that type.

The threshold for capital leases is $100,000, that is, if the net present value of the minimum lease payments, excluding executory costs (usually insurance, maintenance, and taxes paid in connection with the leased property) is $100,000 or greater, it is to be recorded. If the net present value is below that threshold, the asset is to be accounted for as an operating lease. If title to these assets transfers to the State at the conclusion of the operating lease, at title transfer they are to be capitalized and added to inventory.

30.20.40 Capital Lease Accounting

30.20.40.a Account for a capital lease as acquiring a Fixed asset and incurring a liability. If the lease involves acquiring more than one asset, each asset is to be capitalized if its fair market value exceeds the threshold.

Account for a lease as an operating lease, when the net present value of the future minimum lease payments or fair value, whichever is lesser, is less than $5,000. If title to the leased asset transfers to the State at the conclusion of the operating lease, capitalize the fair market value of the asset upon receiving title pursuant to Subsection 30.20.20.

30.20.40.b If a lease between State departments meets the requirements of a capital lease per Subsection 30.20.30:

- The lessor department is to treat the lease as a sales-type lease (record a sale on account and remove the asset from inventory); and,
- The lessee department is to treat the lease as a capital lease (record a Fixed asset and a liability).

30.20.40.c Capital leases are to be used only to acquire Fixed assets. (Refer to

Subsection 30.20.20.)

30.20.50 Certificates of Participations

Fixed assets acquired through Certificate of Participations (COPs) are to be capitalized in accordance with the State's capitalization policy.

Fixed assets acquired through a COP should be capitalized when responsibility for the asset is assumed by the department.

(Refer to Subsections 30.20.20)

30.20.60 Infrastructure Accounting

30.20.60.a In accordance with Governmental Accounting Standards Board (GASB) Statement Number 34, acquisitions of Fixed assets defined as infrastructure, which meet the State's capitalization policy, are to be capitalized.

30.20.60.b The State highway system, operated by the Department of Transportation, is classified by the State as Transportation Infrastructure-Modified Approach. Refer to Subsection 30.20.80.

30.20.60.c All transportation related infrastructure not included in Subsection 30.20.60.b and all non-transportation infrastructure assets are required to be depreciated. Refer to Subsection 30.20.70.

30.20.70 Depreciation policy

30.20.70.a Calculate and record depreciation for all depreciable Fixed assets.

Non-depreciable Fixed assets include:

- Land;
- The State highway system operated by the Department of Transportation, which is classified as Transportation Infrastructure-Modified Approach (refer to Subsection 30.20.80);
- Collections of Historical Treasures, Works of Art, Library Books/Reserves, and other similar assets that are inexhaustible (refer to Subsection 30.20.22); and
- Construction in progress.

30.20.70.b Depreciation normally begins when an asset is purchased or completed, and accepted. However, if an asset is not placed into service immediately, depreciation should begin when the asset begins to lose value. Either option should be applied consistently and should be reasonable in the circumstance. Depreciation may be calculated using either the straight-line or composite method.

- To calculate depreciation using the **straight-line method**:

  Annual Depreciation = (Cost – Salvage Value)/Asset Useful Life

- Calculate the **composite method** based on weighted average estimated lives or an estimate of the useful life of the grouping of assets, such as library resources. The assessment could be based on condition assessments or experience with the useful lives of the groupings of assets.

- A consistent composite depreciation rate should generally be used throughout the life of the grouping of assets, but the rate should be recalculated if the composition of the assets or estimate of the useful lives changes significantly.

  For example, if the average useful life of library resources, or portion thereof, is estimated to be 25 years, an annual depreciation rate of 4% would be used. The annual depreciation expense is calculated by multiplying the annual depreciation rate by the cost of the collection.

30.20.70.c **Useful Life for Fixed Assets**

Departments should use the following recommended guide for assigning a useful life to an asset. However, different lives may be used if an department has a compelling reason and the life assigned to an asset can be justified by historical experience. A brief explanation for the use of different lives must be on file with the State Controller's Office.

2-5 year property — includes computers and peripheral equipment, and computer software designed to cause a computer to perform a desired function;

5 year property — includes office machinery, automobiles, light and heavy general purpose trucks;

5-10 year property — includes internally generated intangibles;

7 year property — includes office furniture and fixtures, agricultural machinery and equipment;

10 year property — includes building improvements such as a new roof, plumbing and electrical renovations, vessels and water transportation equipment;

15 year property — includes land improvements;

30-50 year property — includes residential and nonresidential real property such as buildings;

A more comprehensive list is referenced in Appendix 1 to this document. This list is from IRS Publication 946, "How to Depreciate Property."

The State of Maine follows IRS Publication 946 which can be located under publications of the IRS website.

30.20.70.d Departments are responsible for establishing and utilizing an appropriate useful life for assets acquired in less than new condition.

30.20.70.e For leasehold improvements, the useful life is the estimated service life of the leasehold improvements, or the remaining term of the lease, whichever is shorter.

30.20.80 Non-depreciable transportation-related infrastructure assets reported using the modified approach

The State capitalizes the State highway system as a class of infrastructure assets and reports these assets using the “modified approach" to depreciation. Under the modified approach, these infrastructure assets are not depreciated as long as two requirements are met:

1. The assets are managed in an asset management system, which includes keeping an up-to-date inventory of assets, performing condition assessments of the assets and summarizing the results, and estimating the annual amount to maintain and preserve the assets.
2. The State documents that the assets are being preserved approximately at or above the condition level established and disclosed previously by the State.