



# ***STATE OF DELAWARE***

  

## ***CAPITAL ASSET***

  

### ***ACCOUNTING POLICY***



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## **I. INTRODUCTION**

### **A. Overview**

The State of Delaware has a significant investment in capital assets such as land, land improvements, buildings, machinery, equipment and infrastructure. These assets have initial useful lives that extend beyond a single reporting period.

The Governmental Accounting Standards Board's (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, requires that governments depreciate their exhaustible capital assets, including infrastructure.

To improve financial reporting, accountability and operational efficiencies in managing these capital assets, the State has established a Fixed Asset Accounting System (FAAS).

There are numerous reasons why the State must implement and maintain an effective capital asset management system in accordance with Generally Accepted Accounting Principles (GAAP). Inadequate capital asset records are one of the major causes of deficiencies in state and local government's financial statements. This deficiency often leads to a qualified auditor's opinion, which in turn has a negative impact on the underwriters of debt offerings. A qualified opinion can be translated into higher interest rates.

Public scrutiny is also of primary concern. A well-maintained capital asset system demonstrates to the public the legitimacy of the expenditures as well as the State's sense of responsibility for the proper care and maintenance of assets purchased with public funds.

Complete and accurate capital asset records can help managers identify underutilized buildings or surplus assets that can be reassigned for more productive use. Accurate records can also help identify replacement and renovation needs of existing assets. This type of management information is useful in making budgetary decisions for specific requests and long term capital planning.

### **B. Purpose and Use of the FAAS Manual**

The purpose of this manual is to establish consistency and uniformity among all state organizations regarding maintenance of property and property records and how to report inventory information to the Department of Finance. It also provides procedures to assist state organizations in understanding their roles and responsibilities for control and recording of capital assets in the State's automated FAAS.

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## II. ORGANIZATIONAL RESPONSIBILITIES FOR FAAS

### A. System Responsibilities

The Director of the Division of Accounting (DOA) is responsible for the maintenance and operation of the accounting system. Support is provided to state organizations on matters relating to capital asset accounting, reporting, development, and maintenance. The Division of Accounting:

1. Develops implements and maintains uniform capital asset policies, procedures, reports, and systems. All policies are periodically reviewed and updated as needed.
2. Develops and maintains operational and procedural manuals, directives, and instructional memoranda relating to uniform capital assets.
3. Trains and advises State organizations in the use of the capital asset system.
4. Includes capital asset data in the State's financial statements and reports.

### B. State Organizational Responsibilities

All State organizations are responsible for executing and adhering to capital asset accounting and reporting policies, guidelines, and standards. Organization officials must:

1. Establish internal written procedures and controls necessary to implement and monitor prescribed capital asset accounting and reporting policies, guidelines, and standards.
2. Assign responsibilities to specific individuals for the various capital assets accounting and reporting functions.
3. Ensure the timely, accurate, and complete processing and recording of all necessary transactions in conformance with prescribed capital asset accounting and reporting policies, guidelines, and standards.
4. Ensure proper maintenance of source documents and records pertaining to capital assets.
5. Establish adequate procedures and controls to safeguard and physically account for general capital assets.
6. Verify every year by means of a physical inventory that the capital assets reported on the FAAS are accurate. A certification must be forwarded to the Division of Accounting no later than July 31 following the fiscal year in which the inventory was taken. Documentation must be maintained in support of the physical inventory until a successful audit is completed.
7. Maintain documentation to support the state organization's capital assets as reported in the FAAS. Such documentation shall be maintained in accordance with standard accounting guidelines and is subject to examination.

### **C. Inventory Control of Non-Capital Assets**

The administrative head of each State organization has the responsibility for developing internal policies and procedures to protect and control the use of all capital assets, including those below the required threshold for financial reporting purposes. Organizations are encouraged to maintain property listings of “Public Appeal” and other non-capital asset items for the purpose of safeguarding these items against loss or misuse. “Public Appeal” items are those items that are easily misplaced or stolen; e.g., personal computers, printers, tools, office equipment, etc.

Each organization may use its own discretion when selecting items to be maintained in its property listing and should consider costs versus benefits in developing individual policies and procedures. When establishing criteria for inclusion of items in the property listing, organizations should consider such factors as grant requirements, insurance provisions, cost-benefits of maintaining and monitoring selected items involved, etc.

The federal threshold for capital asset capitalization is \$5,000. Since the State’s threshold for many types of assets is greater than \$5,000, it is the organization’s responsibility to ensure that assets purchased with federal funds are properly accounted for in the State or organization’s records.

Organizations may continue to maintain items below the required threshold in the State’s FAAS or they may maintain these items outside the state system.

### **D. Construction-Work-In-Progress (CWIP)**

#### **1. Office of Management and Budget (OMB)**

Although the Office of Management and Budget (OMB) is primarily responsible for the construction of new buildings as well as additions and renovations to existing buildings, any department that has construction projects must follow the same procedures as OMB. At the close of the fiscal year, OMB will report CWIP balances in the State’s annual GAAP Package (see Appendix B) for inclusion in the State’s financial statements. For complete projects, the department processing payments must enter the item into the DFMS system and complete a transfer to the department that has control of the asset. In addition, the purchasing agency must remove the asset from the CWIP report. Adding the complete project to the State’s FAAS must be done in the same fiscal year that the project is removed from the CWIP report.

Changes to the original capital asset value cannot be made after the original capital asset document has processed. Any unpaid bills or retainage fees paid after the asset has been transferred from CWIP to one of the asset classes should be added to the capital asset as betterment. Documentation to support the land/buildings/improvements and construction-work-in-progress will be maintained by OMB.

#### **2. School Districts and Colleges**

Each local school district and Delaware Technical and Community College is responsible for the reporting of construction projects as well as additions, betterments, and renovations to existing buildings. The Business Manager will report CWIP balances in the State's annual GAAP Package (see Appendix B) for inclusion in the State's financial statements. Completed projects will be removed from the CWIP and reclassified into the appropriate capital asset category; i.e., building and building improvements, and land improvements. Adding the completed project to the State's FAAS must be done in the same fiscal year that the project is removed from the CWIP report. Documentation to support the buildings/improvements and construction-in-progress will be maintained by the School, subject to review by the Division of Accounting. To assist with end-of-year reporting for CWIP, these balances will be updated on a quarterly basis.

### III. REPORTING POLICY

#### A. Capital Asset Capitalization Policy

An important consideration for financial reporting is the capital asset capitalization thresholds established for the various classes of capital assets. In setting the capital asset capitalization policy, a determination was made as to what the minimum cost (i.e., the significant value) of an asset must be to justify the time and expense of maintaining the information, as well as the relative materiality to the general purpose financial statements of the State taken as a whole. Based on this determination, all state organizations are required to use the capital asset capitalization thresholds established by asset classification as follows:

<u>Asset Classification</u>	<u>Minimum Capital Asset Capitalization Threshold</u>
Buildings	No minimum—all buildings will be reported
Building Improvements	≥ \$100,000
Construction Work in Progress	≥ \$100,000
Easements	No minimum—all agriculture easements will be capitalized.
Infrastructure	≥ \$1,000,000
Land	No minimum—all land is reported
Land Improvements	≥ \$100,000
Leased Assets	Depends on Class of Asset
Leasehold Improvement	≥ \$100,000
Software	Not capitalized prior to July 1, 2005 ≥ \$1,000,000 after July 1, 2005

<u>Asset Classification</u>	<u>Minimum Capital Asset Capitalization Threshold</u>
Vehicles, Furniture and Equipment	$\geq$ \$15,000, prior to July 1, 2004 $\geq$ \$25,000, effective July 1, 2004
Works of Art and Historical Treasures	Not capitalized

**NOTE:** *The capital asset capitalization policy is for financial reporting purposes only. It does not supersede any policies established by individual organizations for maintaining internal control over their capital assets using a lower threshold. State Organizations are encouraged to maintain property listings of "Public Appeal" and other non-capital asset items for the purpose of safeguarding these items against loss or misuse (See II-C).*

#### IV. RECORDING OF ASSETS

##### A. Capital Asset Criteria

1. Under accounting rules required by GASB Statement No. 34, all capital assets of a governmental entity must be reported at the entity-wide perspective in the Statement of Net Assets at historical cost (or estimated historical cost) less accumulated depreciation. Capital assets include land and land improvements, buildings and building improvements, vehicles, furniture, equipment, easements, infrastructure, computer software, software work in progress and construction work in progress. Capital assets must meet the following criteria:
  - a) Be tangible; (i.e., buildings and equipment) or intangible; (i.e., easements and software).
  - b) Have an estimated life of more than one year; and
  - c) Be of significant value. The significant value test relates to the capital asset capitalization thresholds of an individual asset. (See III-A-1)
2. Capital assets are not intentionally acquired for resale, nor are they readily convertible to cash.
3. Capital assets can be obtained through direct purchase, installments, capital lease, donation, or confiscation. They are recorded at historical cost, or fair market value, for donations and confiscation. The cost of capital assets includes, in addition to acquisition or construction

costs, ancillary charges to place the asset in its intended location and condition for use. These charges include:

- ◆ Freight and Transportation Charges
- ◆ Site Preparation Expenditures
- ◆ Installation costs
- ◆ Professional Fees (such as surveying, engineering or project management fees)
- ◆ Legal Claims Directly Attributable to Asset Acquisition

Trade-in allowances do not reduce the cost base. Agency administration charges are not part of the recorded cost basis of an asset.

The desired method of valuation is actual (historical) cost. This data may be found by retrieving original invoices, purchase orders, check copies, contracts, minutes, etc. However, if an organization is unable to establish actual cost after a reasonable amount of effort, estimated cost data may be used. Methods available for ascertaining estimated costs include:

- ◆ Engineering Studies
- ◆ Catalogue Prices
- ◆ Vendor Price Lists
- ◆ Internal Appraisal via the Purchasing Department
- ◆ External Appraisal
- ◆ Matching to Previously Purchased Items

## B. Capital Asset Classifications

1. **Buildings.** A building is any structure erected to stand permanently and designed for human use or occupancy or as shelter for animals or goods. Each building is comprised of components such as framing, interior finish, roof structure and cover and building service systems. Building service systems are those systems and their components that provide plumbing, sewerage, heating, ventilation, air conditioning, lighting, power, elevators or escalators, and fire protection, as well as special or unique services to specific structures such as public address and emergency power systems.

The cost of a building includes its construction or purchase costs and the costs of all fixtures permanently attached and made part of the building. Purchase costs include original purchase price, expenses for altering a purchased building to make it ready to use for the purpose for which it was acquired, and professional fees (legal, architect, inspections, tile searches, etc)

For purchase costs, there isn't a dollar threshold for expenditures to be capitalized as a building; if it meets the criteria as a building all expenditures are to be capitalized.

Construction costs are those for completed construction projects or additions (extension, expansion, or enlargement to an existing capital asset such as a second floor or new wing on a building). The constructed costs should be capitalized if it is valued at \$100,000 or more.

Land costs, furniture or other equipment to furnish the building should not be included in the building costs. These items should be recorded separately in the appropriate asset class.

2. **Building Improvements** An improvement's primary purpose is to increase output, lower operating costs, improve working conditions, enhance the original quality, extend the useful life or otherwise add to the worth of future benefits or utility expected to be received from the asset.

The following are examples of expenditures to be capitalized as improvements to buildings:

- ◆ Major conversion of attics, basements, etc., to usable office, clinic, research or classroom space.
- ◆ Structures attached to the building such as covered patios, garages, carports, enclosed stairwells, etc.
- ◆ Installation or upgraded heating and cooling systems.
- ◆ Major structural changes such as reinforcement of floors or walls, installation or replacement of beams, rafters, joists, steel grids, or other framing.
- ◆ Installation or upgraded windows or doors, or built-in closet and cabinets.
- ◆ Major interior renovations associated with casings, baseboards, light fixtures, ceiling trim, etc.
- ◆ Major exterior renovation such as installation or replacement of siding, roofing, masonry, etc.
- ◆ Installation or major upgrades of plumbing and electrical wiring.
- ◆ Installation or major upgrades of phone or closed circuit television systems, networks, fiber optic cable, wiring required in the installation of equipment (that will remain in the building).
- ◆ Other costs associated with the above improvements; i.e., architectural fees, construction management fees, etc.

The cost of an improvement should be capitalized if it is valued at \$100,000 or more.

The following are examples of expenditures **not** capitalized as improvements to buildings and should be recorded as maintenance expense:

- ◆ Adding, removing and/or moving of walls relating to renovation projects which are not considered major rehabilitation projects and do not increase the value of the building. An alteration refers to the modification or modernization of buildings and structures. Examples of alterations are installation of new entry and exit openings, closing old ones, erecting new walls, windows, and partitions, and removing old ones. Expenditures for alterations are not capitalized unless they represent extraordinary alterations or are so major in value that the entire asset is substantially rebuilt.
- ◆ Improvement projects of minimal or no added life expectancy and/or value to the building.
- ◆ Plumbing or electrical repairs.
- ◆ Cleaning, pest extermination, or other periodic maintenance.
- ◆ Interior decorations such as draperies, blinds, curtain rods, wallpaper, etc.

- ◆ Exterior decoration, such as detachable awnings, uncovered porches, decorative fences, etc.
- ◆ 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, roof 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.
- ◆ Moving of furniture from one building to another during construction.
- ◆ Asbestos abatement or mold removal charges.
- ◆ Pollution Remediation Obligations, including pre-clean-up activities; clean-up activities; external government oversight and enforcement; and operation and maintenance of the remedy.
- ◆ Any other maintenance-related expenditure which does not increase the value of the building.

However, if any of these alterations or maintenance repairs items are so major in value that the entire asset is substantially rebuilt the determination should be made of whether it is an improvement or an addition.

To provide central control and consistency of application, questions regarding the methodology or actual instances of when assets are capitalized should be referred to the Division of Accounting.

3. **Construction-Work-In Progress (CWIP).** Paid labor, material, and overhead costs of a construction project are temporarily capitalized in the account “Construction-Work-In-Progress.” As construction progresses, the cumulative expenditures of all vendors involved in the project are tracked and then sorted to be capitalized as CWIP if the vendors meet the criteria for construction items. When the project is completed, construction costs in this account are transferred and allocated to one or more of the other major asset classes such as buildings and/or land improvements.

Costs **not** considered CWIP are audit fees, non-construction insurance costs, furniture purchases, equipment purchases, asbestos abatement, storage fees, moving expenses, payroll of state employees, and portable buildings. Also unpaid bills or encumbered funds do not meet the criteria either.

Assets qualifying as CWIP for financial statement and capital asset accounting purposes must meet the following criteria:

- (a) The asset must satisfy the established criteria of a capitalized asset.
- (b) Estimated total cost at completion must be \$100,000 or greater.
- (c) The asset must not have a final inspection or occupancy date prior to the close of the fiscal year.

A project is considered **complete** when it is ready for its intended use. As an example, a department should remove from CWIP, and enter into the capital asset subsystem, a new building when it has received an occupancy certificate or the building is ready for its intended use. If a building is ready for occupancy in May 2008 but the employees do not move in until July 2009, the building should be entered into State's FAAS in May. If there is any doubt that the project may or may not be complete, please contact the Division of Accounting for guidance on this matter.

Changes to the original capital asset value cannot be made after the original capital asset document has processed. If corrections are found after submission to Division of Accounting, please notify DOA immediately.

The amount for any unpaid bills relating to the project or retainage fees paid after the asset has been transferred from CWIP to one of the asset classes should be added to the capital asset as a betterment to the original capital asset.

4. **Easements.** An easement is a non-possessory interest in land owned by someone else, which entitles the owner of the interest to a limited use or enjoyment of the land and to protection from interference with its use. For example: a conservation easement is a legal agreement between a landowner and a conservation organization. The easement places permanent restrictions on future uses of the property in order to protect its agricultural character. Conservation easements prohibit residential or commercial development and uses or practices, which would be destructive to the agricultural value and productivity of the land. The landowner retains fee title to the property while the conservation organization maintains the rights to control development of the land. The purchase of such easements will be reported in the State's FAAS.
5. **Infrastructure.** Infrastructure is defined as long-lived capital assets that normally are stationary in nature and can be preserved for a significantly greater number of years than most capital assets. Examples include highways, roads, bridges, dams and lighting systems. GASB Statement No. 34 separates infrastructure assets into networks and sub-systems.

A *network* of assets is a group of assets that provide a particular type of service for a government. An example of a network of infrastructure assets would be a dam composed of a concrete dam, a concrete spillway, and a series of locks.

A *subsystem* of a network of assets is composed of all assets that make up a similar portion of segment of a network of assets. Interstate highways, state highways, and rural roads would each be considered a subsystem of the network of all the roads of a government.

Buildings, except those that are an ancillary part of a network of infrastructure assets, should not be considered infrastructure assets for purposes of GASB 34. Examples of buildings that may be an ancillary part of a network of subsystem include road maintenance structures such as shops, garages associated with a highway system.

The majority of the State's infrastructure assets is maintained within the Department of Transportation and includes roadways, bridges and traffic management devices. At the current time, only the Department of Transportation will report infrastructure.

6. **Land.** Land is considered real property. Land costs include the land's initial cost, surveying fees, appraisal and negotiation fees, legal and title fees, damage payments, site preparation costs (clearing, filling, and leveling), and assumption of any liens, mortgages or encumbrances on the property. The demolition of unwanted structures at the time of acquisition of the land with the intention of using the cleared land is considered part of the land costs. Land that is purchased with the intent to resell is accounted for as inventory. Each "parcel" of land owned by the State is recorded as a separate asset (exclusive of buildings). If property is purchased that includes a building(s), the value of the land must be separated from the total cost and recorded as a separate asset. There is no minimum dollar threshold for land; therefore, all land must be recorded in the FAAS. Right-of-ways will not be capitalized; however, land purchased for highway construction will be capitalized.
7. **Land Improvements.** Land improvements are physical changes in or appurtenances to land of such character as to increase the utility of the land (exclusive of structures).

Certain assets, which may appear to meet the definition of infrastructure assets, may be more technically considered land or building improvements, which are directly related to a capitalized asset – land or building. These assets include roadways, walks, parking lots, lighting systems, fencing, docks, piers, boat ramps, telecommunications cabling, etc. These assets are ancillary capital assets (ancillary to another asset i.e., land, building or a group of buildings) incurred as a result of increasing the level of service of an existing capital asset land or building.

Land improvements meeting the \$100,000 per unit historical cost threshold will be capitalized and entered into the FAAS. Land improvements include, but are not limited to:

- ◆ Paving (parking lots)
  - ◆ Curbing
  - ◆ Sidewalks
  - ◆ Fences
  - ◆ Retaining walls
  - ◆ Boat ramps
  - ◆ Piers and docks
  - ◆ Utility distribution systems
  - ◆ Lighting systems
  - ◆ Swimming pools
  - ◆ Playgrounds
8. **Leasehold Improvements.** Capital expenditures made to real estate not owned by the State but the State has the right to the use of real estate by virtue of a lease. The lessee capitalizes leasehold improvements. Improvements made in lieu of rent should be expensed in the period incurred. The capitalization threshold for leasehold improvements is \$100,000.

9. **Leased Assets.** The State leases assets that may be considered a lease purchase agreement. Due to the relative immateriality to the financial statements of the State taken as a whole, and the fact that in many cases the State does not take possession of the asset at the end of the lease term, a determination was made not to capitalize these leases. However, if at the conclusion of the lease, the asset title is transferred to the state organization, the capital asset will be added to the FAAS based on the cost incurred by the organization to purchase the asset including interest costs. Assets purchased via lease purchase agreements should be entered into the State's FAAS after final payment has been made on the lease. Lease purchase assets with an in-service date prior to June 30, 2004 should be entered into the State's FAAS if their value was equal to or greater than \$15,000, while those with an in-service date of July 1, 2004 or later should not be entered unless their value was equal to or greater than \$25,000.
10. **Software.** The State recognizes that entities purchase computer software for many of the same reasons that they purchase other capital assets including reducing costs, improving efficiencies, strengthening internal controls and improving customer service. Effective July 1, 2005, all computer software with a useful life of one year or more and purchased with cost of \$1,000,000 or more must be tracked for reporting as a capital asset. The software will be amortized over its estimated useful life of 5 years

#### 11. **Software Work in Progress (SWIP)**

The standard for capitalizing the costs of software developed or obtained for internal use is the American Institute of Certified Public Accountants (AICPA) State of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Uses". Under this standard, software projects are divided into three stages: the preliminary project stage, the application development stage and the post implementation operation stage. Only costs that are associated with the **application development stage** are to be capitalized.

The State made the capitalization of software effective starting July 1, 2005 for software projects estimated to be \$1,000,000 or more. Any costs incurred prior to July 1, 2005 cannot be capitalized.

Costs that are associated with the **application development stage** are capitalized. These costs include the following activities:

- ◆ Design of chosen path, including software configuration and software interfaces
- ◆ Coding
- ◆ Installation of hardware
- ◆ Testing, including parallel processing phase
- ◆ Vendor costs for commercially purchased software.
  
- ◆ Contractors or employee costs to implement and install the commercially purchased software.
- ◆ Contractors or employee cost to design, program, install and implement internally developed software.
- ◆ Salaries and fringe benefits for employee time spent directly coding and testing.

- ◆ External direct costs of material and services consumed in developing or obtaining software, such as fees paid to third parties for services and costs incurred to obtain the software from third parties.

The paid costs in the application development stage must be tracked by each entity using a tracking system similar to Construction Work in Progress. Once the software enters the production stage, the costs must be entered into DFMS. A separate GMEN reporting category was created in fiscal year 06 to track software costs incurred for systems not yet in production.

Costs that are associated with the Preliminary Project stage and the Post-Implementation stage are **not** to be capitalized. Those costs are to be expensed as incurred. They are as follows:

Preliminary Project Stage- These costs include the following activities:

- ◆ Conceptual formulation of alternatives
- ◆ Evaluation of alternatives
- ◆ Determination of existence of needed technology
- ◆ Final selection of alternatives

Post-Implementation Operation Stage- These costs include:

- ◆ Training
- ◆ Application maintenance

Accounting for costs of reengineering activities, which often are associated with new or upgrade software applications, are not to be capitalized.

General and administrative costs related to software development should **not** be capitalized. These costs include heat, electric, rent, security, building maintenance or secretarial.

Cost of upgrades and enhancements to computer software are capitalized only if the upgrades or enhancements provide additional functionality and the cost exceeds \$1,000,000.

11. **Vehicles/Furniture/Equipment.** Effective July 1, 2004, items that cost \$25,000 or more and have a useful life of one year or more will be recorded in the FAAS. Capital assets placed in the system prior to June 30, 2004, with a value equal to or greater than \$15,000 but below \$25,000, should not be deleted from the subsystem. These items include but are not be limited to:

- ◆ Cars
- ◆ Trucks
- ◆ Construction machinery
- ◆ Computers (i.e., processing units, tape drives, disk drives)
- ◆ Printing presses and reproduction equipment
- ◆ Tractors
- ◆ Buses
- ◆ Telecommunications equipment

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- ◆ Furniture

Each item acquired must be recorded as a separate asset. Capital assets purchased in quantities of two or more are capitalized only after determining the unit cost of each individual asset. Only individual capital assets (quantities of one) are recorded; group purchases of assets are not recorded in the aggregate.

Costs of vehicles/furniture/equipment include the total purchase price after discounts, plus any trade-in allowances, transportation charges, installation costs, and any other costs required to prepare the asset for its intended use.

An asset with associated component parts that are necessary to the functioning of the asset is considered to be one asset when the life and utility of the component parts are mainly dependent on that of the asset. Effective July 1, 2004, the cost of the asset and its component parts are together subject to the \$25,000 threshold. For example, a mainframe CPU with a cost of \$24,000 and its associated cables with a cost of \$1,500 would qualify for financial reporting since their combined cost exceeds the \$25,000 financial reporting threshold. Assets with associated component units that qualify for financial reporting are reported as one asset, and the component parts are included in the description of the asset.

In addition to asset systems and assets with associated component parts are assets with associated attachments. Attachments purchased at the same time as the asset are considered part of the asset because their life and utility coincide with that of the asset (e.g., a collator installed in a copy machine). Attachments obtained subsequent to the purchase of the asset are not considered to be associated with that asset and, therefore, are accounted for as separate assets, if they meet the capitalization criteria. For example, if a copier with a cost of \$26,000 and a collator with a cost of \$12,000 are purchased at the same time, they are considered to be associated. Since their combined cost exceeds the \$25,000 threshold, the copier is reported at a cost of \$38,000 and the collator is included in the description of the asset. By way of contrast, the same assets purchased at different times are not considered to be associated. Therefore, the copier is reported at a cost of \$26,000, but the collator is not reported since its cost does not meet the \$25,000 thresholds.

12. **Works of Art and Historical Treasures.** GASB 34 states that governments should capitalize works of art, historical treasures, and similar assets at their historical cost or fair value at the date of donation (estimated if necessary), if they are held as a collection. Governments, however, will be exempted from capitalizing collections if the following conditions are met:

- ◆ Collections are not held for financial gain but for public exhibition, education or research in furtherance of public service.
- ◆ Collections or individual items are protected, cared for and preserved.
- ◆ Collections are subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections.

This exemption does not apply to collections already capitalized as of June 30, 1999, even if they meet the above conditions for exemption from capitalization. These collections will continue to be capitalized along with all future additions to the collection.

GASB 34 states that capitalized collections, which are exhaustible, should be depreciated over their estimated useful lives. Depreciation is not required for collections, which are inexhaustible.

- ◆ *Exhaustible collections or items* – items whose useful lives are diminished by display or educational or research applications.
- ◆ *Inexhaustible collection or items* – where the economic benefit or service potential is used up so slowly that the estimated useful life is extraordinarily long. Because of its cultural, aesthetic, or historical value, the holder of the asset applies efforts to protect and preserve the asset in a manner greater than that for similar assets without such cultural, aesthetic, or historical value.

Below is a listing of the possible historical treasures, works of art and similar assets. It is not an exhaustive list, and each agency should be diligent in identifying collections that would need to be reported. GASB 34 does not define what or how many works of art, historical treasures, and similar assets constitute a “collection.” Therefore, the definition is left to professional judgment. The State of Delaware defines collections of works of art, historical treasures, and similar assets as one or more items, which are inexhaustible and held for public education, educational purposes, or research in enhancement of public service instead of financial gain.

- ◆ Paintings, photography, maps, manuscripts, libraries, musical instruments, recordings, film, furnishings, artifacts, tools, weapons, and other memorabilia located at various state museums and office buildings.
- ◆ Monuments and statues on display at various sites around the State.

The State of Delaware has elected not to capitalize collections in order to expedite the completion of the State’s CAFR each year and to reduce the amount of time and effort required of State organizations in maintaining this information in the FAAS. However, in order for the State to be exempt from the capitalization requirement of GASB 34 for works of art, historical treasures, and similar assets, all organizations holding such assets must have in place a policy concerning those assets. These policies should include language stating that all collection items donated to the agency or purchased with state funds are:

- ◆ Not held for financial gain, but rather for public exhibition, education or research in furtherance of public service.
- ◆ Protected, cared for and preserved.
- ◆ Subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections.

**C. DEPRECIATION**

1. Depreciation is the method of distributing the cost of a capital asset over its estimated useful life. All capitalized assets will be depreciated using the straight-line method of depreciation, except those assets that are considered inexhaustible such as land, works of art, historical treasures and similar assets. Depreciation will be calculated based on the date the asset was available for use or placed in service. If the asset was purchased or available for use during the first six months of the fiscal year, a full year depreciation expense will be calculated. If the asset was purchased or available for use during the last six months of the fiscal year, only one half of the annual depreciation will be calculated.

Historically, the State uses its capital assets well beyond their useful lives. There is little, if any, value left when an asset is retired. Therefore, no residual or salvage value will be used in the depreciation calculation due to the insignificant value remaining in the asset upon retirement.

The depreciation expense associated with each asset will be maintained in FAAS to be aggregated and recorded at fiscal year end. When a capital asset is deemed lost, obsolete, sold, stolen, or otherwise disposed, all accumulated depreciation to the date of the action is removed, as well as the capital asset itself.

2. The estimated useful lives of capitalized assets are as follows:

Buildings and building improvements .....	40 years
Vehicles .....	7 years
Furniture/Equipment .....	10 years
Land improvements .....	20 years
Software.....	5 years

State hospitals within the Department of Health and Social Services and the Veteran’s Home within the Department of State are exempt from the above schedule of useful lives. A longer or shorter life assignment may be used by the State hospitals for the purpose of Medicare reimbursement with approval by the Medicare fiscal intermediary. Such schedule of useful life should be documented and maintained as part of the hospital’s written property inventory policies.

The Department of Transportation (DOT) is also exempt from the State’s schedule of useful life. A longer or shorter life assignment may be used by DOT; however, a schedule of useful life should be documented and maintained as part of DOT’s written property inventory policy.

3. Infrastructure Assets - Modified Approach vs. Depreciation

The modified approach is an alternative to reporting depreciation for infrastructure assets that meet the following criteria:

- ◆ The assets are managed using a qualifying asset management system.

- ◆ It is documented that the assets are being preserved at or above a condition level established by the government.

Depreciation is not reported for infrastructure assets using the modified approach. Costs for both maintenance and preservation of these assets should be expensed in the period incurred. Additions and improvements, however, will be capitalized.

The State has elected to use the modified approach for reporting infrastructure assets. The Department of Transportation must develop written policies and procedures to manage its asset management system. These policies shall coincide with the State's policies and procedures as well as ensure compliance with GASB 34. Policies should include:

- ◆ Identification of eligible infrastructure assets that are comprised of either a network or subsystem. The modified approach shall be applied to all assets within that network or subsystem.
- ◆ Establishment and documentation of minimum acceptable condition levels for each element of the network or subsystem.
- ◆ Reference documents that detail replicable condition assessment and the frequency in which assessments are completed.
- ◆ Reference documents that detail annual estimates to maintain and preserve the eligible infrastructure assets at the condition level established and disclosed by the State.

#### 4. Presentation Requirements for expenses in the Statement of Activities – Shared Assets

Depreciation expense for capital assets that serve essentially all functions, such as multipurpose buildings need not be included in the direct expenses of the various functions. Instead, it may be included as a separate line item in the Statement of Activities or as part of a "general" function. Because of the additional effort required to prorate depreciation expense among various functions, the State has opted to report this expense as a separate line item and not allocate the expense as an indirect expense to other functions.

## **V. RECORDS AND PROCEDURES**

### **A. Property Inventory**

1. The State requires that a physical inventory of the property must be taken and the results reconciled with the property records every year. Organizations are required to maintain documentation to illustrate a physical inventory was performed.
2. Organizations performing a physical inventory are required to submit a certification verifying such inventory has been conducted (see Appendix A). The certification form should be sent to the Director of Accounting no later than 31 days following the close of the fiscal year. Any adjustments, found necessary during the property inventory process, to update an organization's capital assets must be made by June 30. This includes updating any skeletons in the FAAS that have not been completed.

## VI. ACQUIRING A CAPITAL ASSET

1. Capital assets must be recorded at their acquisition cost which includes the vendor's invoice (plus the value of any trade-in), plus sales tax, initial installation cost (excluding in-house labor), modifications, attachments, accessories, or apparatus necessary to make the asset usable and render it into service. Acquisition cost also includes freight and transportation charges, site preparation costs, and professional fees. Capital assets must be entered into the Capital Asset Subsystem by the agency or school district paying for the item. If the agency processing the payment is not the custodial agency, the asset must be entered by the purchaser and then transferred to the appropriate custodial agency using a transfer document.
2. Donated or confiscated capital assets should be reported at their estimated fair value at the time of acquisition plus ancillary charges, if any. Donations are defined as voluntary contributions of resources to a governmental entity by a non-governmental entity. The donated items must have a valuation by a professional to support the fair market value added to the capital asset accounting system. The cost of the valuation is to be added to the value of the asset when entering it into the system. The in service date will be the date the asset was donated.

## VII. RETIREMENT OF A CAPITAL ASSET

1. "All equipment, supplies and material, including vehicles, purchased in whole or in part with State-appropriated funds shall be considered as assets of the State and not of the State agency which holds or uses the material. When material so held or used is determined by a State agency to be in excess of its needs, it shall be reported by memorandum to the Office of Management and Budget, Government Support Services Section for appropriate reallocation or disposal." (Title 29, Del. C. § 7002)
2. State organizations must initiate the appropriate transaction to transfer or dispose of the asset from the organization's records. Organizations are responsible for maintaining documentation to support the retirement of an asset of any value. **Note:** The Division of Accounting will be requesting support for disposals throughout the year.
3. State organizations receiving property from another State organization must record the carrying value of the property with accumulated depreciation recognized from the original date the property was placed into State service. Any fees or other monetary consideration between State organizations for transfer of state owned property would not be capitalized.

**Note:** This transaction would be considered a transfer – not a disposal – on one agency and a purchase on the other.

## VIII. IMPAIRMENTS

According to GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, asset impairment is defined as a significant, unexpected decline in the service utility of an asset. The term *significant* refers to the magnitude of the impairment when compared to the service utility of the asset. An *unexpected decline* refers to a decline in the net book value of an asset that exceeds the amount expected through accumulated depreciation. The *service utility* of a capital asset is the usable capacity that at acquisition was expected to be used to provide service, as distinguished from the level of utilization, which is the portion of the usable capacity that is currently being used.

The determination of whether a capital asset has been impaired is a two-step process. First, capital assets that have experienced events or changes in circumstances that could potentially indicate impairment should be identified. Then, assets so identified should be tested to determine if actual impairment has occurred. In GASB 42, the emphasis is on events or changes in circumstances that are prominent and known to the government. In other words, state agencies are not required to perform additional procedures to identify impairment beyond those already performed as part of normal operations.

The five most common indicators of potential impairment include:

- ◆ Physical damage, such as a building damaged by fire or flood, which requires significant costs to restore the asset's service utility.
- ◆ Changes in laws or regulations that limit or curtail the use of a capital asset, such as a new water treatment plant that does not meet and cannot be modified to meet new standards.
- ◆ Technological development or evidence of obsolescence.
- ◆ A change in a manner or expected duration of use of a capital asset, such as closure of a school prior to the end of its useful life.
- ◆ Construction stoppage due to lack of funding.

A decrease in the use of capital assets is not, in itself, considered a separate indicator of impairment unless it is associated with one of the items listed above.

The amount of impairment for capital assets that are permanently impaired and remain in service must be calculated, net of insurance recoveries, and recognized as an expense. The carrying value must also be decreased by the calculated amount of the asset's impairment. Assets that are impaired and taken out of service permanently should be carried at the lower of carrying value or fair value, with no further annual depreciation expense. GASB 42 discusses several methodologies for calculating the amount of a capital asset's impairment. The following are the methods for measuring impairment:

- ◆ **Restoration cost approach** – Under this approach, the amount of impairment is derived from estimated costs to restore the utility of the capital asset. The estimated

restoration cost can be converted to historical cost either by restating the estimated cost using an appropriate cost index or by applying a ratio of estimated restoration cost over estimated replacement cost to the carrying value of the capital asset.

- ◆ **Service units approach** – This approach isolates the historical cost of the service utility of the capital asset that cannot be used due to the impairment event or circumstance. The amount of impairment is determined by evaluating the service provided by the capital asset before and after the event or change in circumstance.
- ◆ **Deflated depreciated replacement cost approach** – This approach replicates the historical cost of the service produced. A current cost for a capital asset to replace the current level of service is estimated. This estimated current cost is depreciated to reflect the fact that the capital asset is not new, and then is deflated to convert it to historical cost dollars.

The relationships between the types of impairment and the methodology used to calculate the impairments are outlined below:

Type of Impairment	Method Used to Calculate the Amount of the Impairment
Physical Damage	Restoration cost approach
Changes in legal or environmental factors	Service units approach
Technological change	Service units approach
Change in manner or duration of use	Service units approach or deflated depreciated replacement cost approach

Impaired capital assets that will no longer be used should be reported at the lower of carrying value or fair value. Capital assets impaired from construction stoppage should also be reported at the lower of carrying value or fair value.

State agencies should assess their capital assets at least annually to determine if they have any impaired capital assets with material carrying values. The DOA must be notified if any assets have been determined to be impaired by the common indicators above. The DOA will make the determination on which method to use to calculate and report the values in the State's CAFR.

**Appendix A**

**MEMORANDUM**

**TO:** Director  
Division of Accounting

**FROM:** \_\_\_\_\_

**DEPT:** \_\_\_\_\_

**SUBJECT: PROPERTY INVENTORY RECONCILIATION - FY 2009**

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I certify that a physical inventory has been performed and reconciled with the annual "GAAP Report of Fixed Assets" (F25F2705) as of \_\_\_\_\_, and conducted in accordance with the Budget and Accounting Policy Manual (Section XV,V,A(1)).

Furthermore, the Fixed Asset Accounting Subsystem (FAAS) has been updated to reflect all purchases and acquisitions as well as deletions during the past year.

Signed: \_\_\_\_\_  
Responsible Official

Date: \_\_\_\_\_

This form is due in the Division of Accounting by **July 31, 2009**.  
(FAX number 302-739-1304)

**Appendix B**

**SUMMARY of  
CONSTRUCTION WORK IN PROGRESS (CWIP)  
AT JUNE 30, 2009**

**Document H-3A**

<b>GAAP Fund (1)</b>	<b>CWIP Ending June 30, 2008 (2)</b>	<b>Adjustments to Beginning Balance + or (-) (3)</b>	<b>Additions + (4)</b>	<b>Projects Completed (Deletions) (-)(5)</b>	<b>CWIP Ending June 30, 2009 = (6)</b>
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
<b>TOTAL Agency Construction Work In Progress as of June 30, 2009 (7)</b>					\$

COMMENTS:

**This Form MUST BE COMPLETED AND ENTERED ON DFMS IN THE GMEN PROGRAM by ALL agencies. If the form does not apply to your agency, complete the header information and check the N/A block. If you have any questions, please contact Dawn Haw-Young at 302.672.5516**

**RETAIN A COPY OF THIS FORM WITH YOUR GAAP PACKAGE WORKPAPERS.**

**Appendix C**

*SUMMARY of  
SOFTWARE WORK IN PROGRESS (SWIP)  
AT JUNE 30, 2009*

**Document H-3B**

<b>GAAP Fund (1)</b>	<b>SWIP Ending June 30, 2008 (2)</b>	<b>Adjustments to Beginning Balance + or (-) (3)</b>	<b>Additions + (4)</b>	<b>Projects Completed (Deletions) (-) (5)</b>	<b>SWIP Ending June 30, 2009 = (6)</b>
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
\$	\$	\$	\$	\$	\$
<b><i>TOTAL Agency Computer Software In Progress as of June 30, 2009 (7)</i></b>					\$

COMMENTS:

**This Form MUST BE COMPLETED AND ENTERED ON DFMS IN THE GMEN PROGRAM BY ALL agencies. If the form does not apply to your agency, complete the header information and check the N/A block. If you have any questions, please contact Dawn Haw-Young at 302.672.5516**

**RETAIN A COPY OF THIS FORM WITH YOUR GAAP PACKAGE WORKPAPERS.**

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## Appendix D

### GLOSSARY

**Ancillary charges** – Necessary charges to place an asset in its intended location for utilization such as freight, installation costs, set-up expenses, etc.

**Appurtenances** – An item added to an asset of greater importance or value.

**Capitalization** – The recording of assets of a governmental entity and reported at the entity-wide perspective in the Statement of Net Assets at historical cost less accumulated depreciation. A capital asset will be capitalized if it meets the threshold criteria established by the governmental entity and have an estimated life of more than one year.

**Construction-Work-In-Progress (CWIP)** – A balance sheet classification which represents a temporary capitalization of labor, materials, and equipment of buildings or other capital assets that are under construction. When completed, CWIP is reclassified to land, building, or land/building improvement and included in the State's Capital Asset Accounting System.

**Software-Work-In-Progress (SWIP)** – A balance sheet classification which represents a temporary capitalization of accumulated costs under the application development stage of software. When completed, SWIP is reclassified to the software classification and included in the State's Fixed Asset Accounting System (FAAS).

**Depreciation** – The systematic allocation of the cost of a capital asset over its estimated economic life to the periods that benefit from the asset.

**Donated Property** - Donated or confiscated property should be recorded at the estimated value at the date of receipt.

**Fair Market Value (FMV)** - Fair Market Value is the estimated amount at which the property might be expected to exchange between a willing buyer and a willing seller, neither being under compulsion, each having reasonable knowledge of all relevant facts.

**Capital Assets** – 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. The term capital asset is used for financial reporting purposes and is not related to the budget process or for recording expenditures in the State's accounting system.

**Generally Accepted Accounting Principles (GAAP)** - Conventions, rules, and procedures necessary to describe accepted accounting practices at a particular time. The importance of reporting entities following generally accepted accounting principles in the preparation of their financial statements is embodied in Rule 203 of the AICPA's Code of Professional Conduct. The AICPA Council has designated the Governmental Accounting Standards Board (GASB) as the body to establish accounting principles for state and local governments.

**Governmental Accounting Standards Board (GASB)** – The authoritative accounting and financial reporting standard-setting body for government entities.

**Governmental Accounting Standards Board Statement No. 34** – GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* significantly affects how governmental entities prepare their external financial statements. The State of Delaware is required to integrate the standards required by GASB 34 effective with the June 30, 2002 financial statements.

**Historical Cost** - The actual cost of a property to the present owner – not necessarily the original cost as of the date the property was first constructed and originally placed in service. All property must be reported at its "Historical Cost," unless the property was donated (see definition of donated property), the amount actually paid for the asset plus all other costs reasonable and necessary to place the asset into operation. Examples of other costs would be closing costs, surveys, architectural or engineering fees, and any modifications and/or installation charges necessary before use.

**Intangibles**-Intangibles are items that are not physical in nature but are still deemed to be assets to the State. This would include rights of way, easements and computer software.

**Organization** – Includes all State agencies and school districts including charter schools and higher education.

**Original Cost** - The actual or normal cost of new property in accordance with market prices as of the date the property was first constructed and originally installed.

**Public Appeal** - Items that are easily misplaced or stolen such as laptop computers, printers, tools, office equipment, etc. and require greater administrative control over than other assets such as land and buildings. Each organization should establish their own threshold for inclusion of these items in their property inventory listing.

**Qualified Opinion** – A qualified opinion is issued when the auditor expresses reservations about the fair presentation of the financial statements in conformity with GAAP. A common reason that the auditors qualify their opinions on financial statements is that the government's underlying records may not be sufficient to support some of the data contained in the financial statements.

**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.

**Tangible** – Tangible property has a physical existence and its value is intrinsic, that is the property has value in and of itself. Examples include machinery, vehicles, buildings, furniture, etc.