

Capital Asset Management

**From CIP to Fixed Asset to Disposition:
Booking a Capital Asset Through it's Life Cycle**

GFOA of Missouri

Allen, Gibbs & Houlik, L.C.

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TOPICS

1. Basics
2. PBC's (audit schedules)
3. Life Cycle/General Ledger/JE's
4. Ownership/Impairments
5. Audit Standards & Procedures

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Basic Definitions

1. *Asset are defined as:*
 - *Resources with a present service capacity that the government presently controls*
2. Capital assets are assets that:
 - Are used in operations, and
 - Have an initial useful life *beyond a single reporting period.*



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Basic Definitions

3. Capital assets are broken down:

- Tangible (physical substance)
 - Land & Improvements, Buildings, Equipment
 - Natural resources such as mineral deposits, oil & gas, timber
- Intangible (without physical substance)
 - Water rights, easements, patents, copyrights, trademarks

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Major Capital Asset Classes

1. Capital assets not being depreciated
inexhaustible:
 - Land
 - Construction in Progress
2. Capital Assets (net of accumulated depreciation):
 - Buildings
 - Improvements Other Than Buildings
 - Machinery and Equipment
 - Infrastructure
 - Other Capital Assets



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Statement of Net Assets

1. Exceed by far the amounts reported for all other types of assets combined.
2. Found only on financial statements prepared using the economic resources measurement focus and the full accrual basis of accounting (Statement of Net Assets)
3. Are not financial assets, and are therefore not found in financial statements of governmental funds.

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Capital Assets Presentations and Disclosures in Financial Statements

1. MD&A
2. Statement of Net Assets
3. Notes
 - SSAP
 - Capital threshold
 - Useful lives
 - Tables
 - Roll forward



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Audit Schedules

1. Comparison of Capital Outlay to total Expenditures within a Fund
 - Identifies items to be capitalized (capital outlay)
2. Total capital outlay recon to capital asset additions on capital assets roll forward schedules
3. Capital Assets Roll Forward
 - Beginning balances
 - Additions
 - Disposals
 - Ending Balances



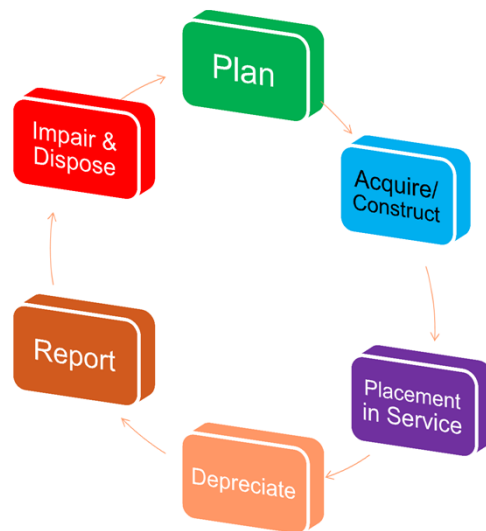
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Life Cycle



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Capital Project Life Cycle Capital Improvements Plan (CIP)

1. Capital Project Life Cycle Starts in the CIP
2. The CIP is a planning document, a multi year rolling projection of the City's capital needs as well as the future financing requirements.
3. CIP is often linked to City financial and strategic plans.
4. CIP does not impart any spending authority.

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TRANSPORTATION PROJECTS

Project Name	Project #	2015	2016	2017	2018	2019	Total	Page
119th and Black Bob Geometric Improvements	3-C-030-XX	75,000	420,000	-	-	-	495,000	26
127th Street, Black Bob to Pflumm	30401C	-	-	-	-	-	-	27
135th & Greenwood Turn Lanes	3-C-073-XX	-	148,000	497,500	-	-	645,500	28
143rd Street, Pflumm to Quivira	3-C-037-13	685,000	935,000	8,945,000	-	-	10,545,000	29
151st Street and Mur-Len Geo Imp with Signal	3-C-105-12	-	-	515,000	3,320,000	-	3,835,000	30
159th Street, Old 56 Hwy to I-35	3-C-002-13	8,150,000	7,780,500	-	-	-	15,930,500	31
Bridge Repair	3-G-000-15	250,000	270,000	250,000	445,000	250,000	1,465,000	32
College Boulevard Landscaping, Ridgeview to Renner	3-C-004-XX	150,000	-	-	-	-	150,000	33
College Boulevard, Ridgeview to Renner	3-C-022-10	-	-	-	-	-	-	34
College Boulevard, Lone Elm to Woodland	3-C-001-XX	1,880,000	5,020,000	-	-	-	7,000,000	35
Compressed Natural Gas Fueling Station	8-C-006-12	1,833,500	460,000	-	-	-	2,293,500	36
Geometric Improvement Projects	3-C-083-XX	-	-	1,615,000	1,615,000	1,616,000	4,846,000	37
Ridgeview & K-10 (Gateway Project)	3-C-071-14	500,000	-	-	-	-	500,000	38
Santa Fe and Black Bob Geometric Improvements	3-C-106-XX	-	-	-	257,000	543,000	800,000	39
Santa Fe, Clairborne to Mur-Len	3-C-025-XX	200,000	-	-	-	-	200,000	40
Streetlight Buy-Back	3-C-009-13	5,555,000	-	-	-	-	5,555,000	41
Streetlight LED Conversion	3-C-009-XX	370,000	395,000	440,000	380,000	300,000	1,865,000	42
Street Preservation Program	3-P-000-15	13,010,000	12,820,000	13,246,000	13,677,000	14,108,000	66,862,000	43
Street Reconstruction Program	3-R-000-15	550,000	935,000	1,450,000	1,750,000	1,750,000	6,435,000	44
Traffic Signals	3-C-004-13	-	250,000	-	250,000	250,000	750,000	45
US 169/K-7 and 159th Geometric Improvements	3-C-043-11	-	-	-	-	-	-	46
TOTAL		33,288,500	29,433,500	26,958,500	21,674,000	18,818,000	130,172,500	

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Capital Project Life Cycle Capital Budget

1. Operating Budget - imparts spending authority for capital projects.
2. Includes capital projects with budgets **appropriated by specific City Council action.**
3. Appropriated project by project, multi-year basis, or
4. May run concurrently with the operating budget fiscal year.

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TRANSPORTATION FUNDING SOURCES

Budget Item	2015	2016	2017	2018	2019	Total
CARS	2,500,000	2,260,000	1,500,000	1,000,000	-	7,260,000
CIP Fund	2,075,000	2,200,000	2,400,000	2,600,000	2,800,000	12,075,000
City of Lenexa	75,000	-	-	-	-	75,000
City of Overland Park	322,500	455,000	1,825,000	-	-	2,602,500
GO Bonds 10 yr	14,302,495	3,645,000	19,302,500	6,964,500	7,190,000	51,404,495
KLINK 1-R Resurfacing	200,000	-	-	-	-	200,000
Other Funds	-	1,851,667	1,851,666	1,851,667	-	5,555,000
Other Jurisdictions	100,000	250,000	-	-	-	350,000
Solid Waste Fund	1,833,500	210,000	-	-	-	2,043,500
Street Escrow	-	-	164,924	-	-	164,924
Street Excise Tax	497,500	148,000	578,076	-	-	1,223,576
Surface Transportation Program (STP)	4,260,000	368,000	3,500,000	-	-	8,128,000
Temporary Notes	(7,542,495)	11,072,500	(11,358,000)	1,837,500	(676,000)	(6,666,495)
Transportation Sales Tax	8,610,000	8,825,000	9,046,000	9,272,000	9,504,000	45,257,000
TOTAL	27,233,500	31,285,167	28,810,166	23,525,667	18,818,000	129,672,500

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Capital Projects General Ledger

1. Result - display information on capital assets by major asset class either on face of the financials or in the Notes.
2. Separate display for:
 - Capital assets that are not being depreciated (land)
 - Capital assets that are being depreciated (buildings, equipment, etc)

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txtAssetNbr	Description	IU #	FixedAssetAccount	LocationDesc	Year
5065	Public Works - Streets - 2003-2004 Fiscal Year Additions		2239227	Public Works	2004
6015	Water Department - 2001 Sanitary Sewer Improvements		50-50-8300	Water	2012
5064	Engineering Costs for 211th St Interchange		2239227	Public Works	2013
4029	2011 Sanitary Sewer Improvements (2013)		51-51-8310	Sewer Department	2013
5071	Sidewalks- 2004-2005 Fiscal Year Additions		2239227	Public Works	2005
5087	FY 2012 Street Resurfacing		2239227	Public Works	2012
1002	City Hall Admin Portion 40% (Shared with Sewer & Water)	Parcel # 70516000000058002	2228265	City Hall	2008
1002.1	City Hall Sewer 30% (Shared with Admin & Water)	Parcel # 70516000000058002	51-51-8310	City Hall	2012
1002.2	City Hall Water 30% (Shared with Admin & Sewer)	Parcel # 70516000000058002	50-50-8300	City Hall	2012
5090	Public Works- Streets right of way 2005-2006		2239227	Public Works	2006
6014	Water Department - Broadway Main Replacement		50-50-8300	Water	2012
3002.1	Police Garage	22715 Joe Holt Parkway, Peculiar	2228265	Police Garage	1998
3001.3	Police Annex Building Roof Replacement		2231918	Police Annex	2013
19	Public Works Dump Truck	Vin 9123 (Last 4 digits)	2239227	Public Works	2012

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Make	Model	Class SubCl	New Or Used	Department Desc	Purch Date	Purchase Price	Salvage Value
		7500	New	Public Works	03/31/13	\$1,954,500.00	\$0.00
		7500	New	Water	09/01/12	\$1,786,103.17	\$0.00
		7500	New	Public Works	09/30/13	\$750,000.00	\$0.00
		7500	New	Sewer	08/28/13	\$718,247.94	\$0.00
		7500	New	Public Works	03/31/14	\$299,880.00	\$0.00
		7500	New	Public Works	06/01/12	\$262,522.42	\$0.00
		4500	New	Administrative	09/01/12	\$209,085.84	\$0.00
		4500	New	Sewer	09/01/12	\$156,814.38	\$0.00
		4500	New	Water	09/01/12	\$156,814.38	\$0.00
		3500	New	Public Works	03/31/14	\$128,800.00	\$0.00
		7500	New	Water	02/01/12	\$112,049.88	\$0.00
		4500	New	Law Enforcement	12/01/13	\$100,000.00	\$0.00
		4500	New	Law Enforcement	01/31/13	\$90,005.40	\$0.00
International	7300 SFA Dump	6500	New	Public Works	01/01/12	\$82,000.00	\$0.00
		3500	New	Law Enforcement	12/01/13	\$80,000.00	\$0.00
Ford	Explorer AWD 4dr	6500	New	Law Enforcement	12/01/13	\$52,310.00	\$0.00

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Costs to Capitalize

1. Purchase and/ or construction costs.
2. Ancillary charges necessary to place the asset into its intended location and condition for use.
3. Include only costs incurred after it has become probable that an asset will be acquired.
4. Cost of a feasibility study is not capitalizable, because cost was incurred prior to determination of feasibility.

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Recording - Generally

1. At cost in accordance with the cost principle,
 - At cost is measured by cash paid or by the cash equivalent price when non-cash (exchange/trade)
 - Cash equivalent price = estimated fair market value of asset

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Recording - Land

- Cost of Acquired Land
 - Purchase price
 - Closing cost – title and legal fees
 - Commissions – broker
 - Property taxes and other liens
- Necessary to make the land ready for “intended use”

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Recording – Land Question

- City A acquired land for \$100,000 for a park. The land purchased a building on it that was going to cost \$5,000 to remove. Legal fees and commissions necessary to acquire the land were \$2,000.

• Cash price	\$100,000
Removal	\$5,000
Legal & Commission	<u>2,000</u>
	<u>\$107,000</u>

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Recording – Vehicle Question

- City A acquired police car for \$24,000. Lettering and painting cost \$750.

Cash price	\$24,000
Legal & Commission	<u>750</u>
	<u>\$24,750</u>

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Recording – Infrastructure

- City A building water tank for \$1,500,000

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Recording Journal Entry

Account Type	Description	Dr	Cr
Expenditure	Capital Outlay – Construction - Public Works	1,500,000	
Current Asset	Cash		1,500,000
	Capital Projects Fund - Construction Costs		
Capital Asset	Construction in Progress	1,500,000	
Expenditures	Capital Outlay – Construction - Public Works		1,500,000
	Convert capital outlay from functional activities to capital assets		

Capitalized Interest

1. An ancillary charge.
2. Limited to capital assets reported in enterprise funds.
3. Interest rate = weighted average rate for all outstanding interest bearing liabilities of that particular enterprise fund.
4. Capitalization period = begins at the start of preconstruction activities and ends when asset is substantially complete and ready for use.

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Capitalized Interest

- Non-externally restricted tax-exempt debt (does not warrant offsetting interest expense against interest earnings)
- \$4M Bonds @ 5%
- Average accumulated expenditures = \$600K
- Capitalized interest = $\$600\text{K} \times 5\% = \$30,000$
- Accrued interest = $\$4\text{M} \times 5\% = \$200,000$

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Capitalized Interest

- Average accumulated expenditures = \$600K

Payment On	Expenditure		Weighted Ave. Accum. Expend.
July 1	\$600,000	6/12	\$300,000
Sept 1	\$900,000	4/12	\$300,000
	<u>\$1,500,000</u>		<u>\$600,000</u>

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Capitalized Interest

- Non-externally restricted tax-exempt debt (does not warrant offsetting interest expense against interest earnings)
- \$4M Bonds @ 5%
- Average accumulated expenditures = \$600K
- Capitalized interest = \$600K x 5% = \$30,000
- Accrued interest = \$4M x 5% = \$200,000

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Capitalized Interest JE

Account Type	Description	Dr	Cr
Capital Asset	Construction in Progress	30,000	
Expense	Interest Expense	170,000	
Liability	Accrued Interest Payable		200,000

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Project Placed in Service JE

Account Type	Description	Dr	Cr
Capital Asset	Infrastructure - Water Distribution System	1,530,000	
Capital Asset	Construction in Progress		1,530,000
	Record completion of elevated water storage tank placed in service Oct-2013		

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Depreciation

- Allocating cost of capital asset over its useful (service) life in a rational/systematic manner
- Matching principle –
 - Revenues (benefits) = expense
- Factors –
 1. Cost
 2. Useful Life
 3. Residual Value

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Depreciation JE

Account Type	Description	Dr	Cr
Expense	Depreciation	51,000	
Contra-Asset	Accumulated Depreciation		51,000
	Record FY 13 Depreciation expense (1,530,000 / 30 years = 51,000)		

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Disposition

FY 2033 water tank is sold for scrap metal
 Proceeds at auction \$20,000

Net Asset Value

- Original Cost \$1,530,000
- Accumulated Depreciation 20 years @ \$51,000 = \$1,020,000
- Net Book Value = \$510,000
- Loss on Disposal \$490,000

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Disposition JE

Account Type	Description	Dr	Cr
Current Asset	Cash	20,000	
Capital Asset	Infrastructure – Water Distribution System		1,530,000
Contra Asset	Accumulated Depreciation	1,020,000	
Non-Operating Income	Loss on Disposal	490,000	
	Record dismantling and sale of elevated storage tank		

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Ownership

1. Can be reported on one and only one set of financial statements (FS).
2. Reported on the FS of the government that owns them.
 - Title generally establishes ownership
 - Capital lease exception “use and enjoyment”
3. When ownership cannot be established
 - Belongs to the government responsible for managing the capital asset
 - Key responsibility is maintenance

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Impairment

1. GASB 42: A capital asset is considered impaired when its service utility has declined significantly and unexpectedly.
2. Required to evaluate “prominent events” or changes in circumstances affecting capital assets



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Impairment

- Considered impaired if both:
- a) Decline in service utility of capital asset is **large in magnitude**, and
 - b) The event or change is outside the normal life cycle of the capital asset

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Impairment



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Impairment

Building

- Original cost \$35M
- Accumulated depreciation \$17.5M
- Book value \$17.5M
- Loss in service capacity 20% ($\$17.5M / 5 = \$3.5M$)
- Restoration costs \$6M
- Insurance recovery \$4.5M

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Impairment JE Proprietary Fund

Account Type	Description	Dr	Cr
Current Asset	Cash	4,500,000	
Contra asset	Accumulated depreciation		3,500,000
Non Op Income	Gain on impairment		1,000,000
	<i>Record net effect of insurance recovery for storm damage</i>		
Capital Asset	Building	6,000,000	
Current Asset	Cash		6,000,000
	<i>Capitalize restoration costs</i>		

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Impairment JE Governmental Fund

Account Type	Description	Dr	Cr
Current Asset	Cash	4,500,000	
Other financing source	Insurance recovery		4,500,000
	<i>Record insurance recovery for storm damage</i>		
Expenditures	Capital outlay	6,000,000	
Current Asset	Cash		6,000,00
	<i>Record restoration costs</i>		

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Impairment JE Government-wide Conversion

Account Type	Description	Dr	Cr
Capital Asset	Building	6,000,000	
Other financing source	Insurance recovery	4,500,000	
Contra asset	Accumulated depreciation		3,500,000
General revenue	Gain on impairment		1,000,000
Expenditures	Capital outlay		6,000,000

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Auditing standards

- SAS 106– Audit Evidence
- SAS 107 – Audit Risk & Materiality in Conducting an Audit

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Risk analysis definitions

1. Inherent risk (IR) the susceptibility of a relevant assertion to a misstatement that could be material, either individually or when aggregated with other misstatements, **assuming that there are no related controls**.
2. Control risk (CR) is the risk that a misstatement that could occur in a relevant assertion and that could be material, either individually or when aggregated with other misstatements, **will not be prevented or detected on a timely basis by the entity's internal control**.
3. Detection risk (DR) is the risk that the **auditor will not detect a misstatement that exists in a relevant assertion** that could be material, either individually or when aggregated with other misstatements.

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Audit Procedures

Analytical Procedures

- Ratios:
 - depreciation expense to total depreciable fixed assets
 - repairs and maintenance exp to total depreciable fixed assets
- Comparisons:
 - of actual capital expenditures with capital budget
 - maintenance accounts with operating budget



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Audit Procedures (cont'd)

Substantive Testing

- Observing asset inventory and vouching of current-year additions and disposals;
- Searching for unrecorded disposals and tracing assets to and from asset listings;
- Reviewing:
 - lease agreement for capital leases;
 - other agreements for intangible assets;
 - maps and other engineering documents for completeness of infrastructure assets;
 - repairs and maintenance account transactions;
 - documentation for potential asset impairments;
 - estimated useful lives and depreciation methods;
- Recalculating:
 - depreciation expense; and
 - capitalized interest.



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Applicable problem areas

1. Charged to the wrong account or **not recorded at all**.
2. Used for purposes other than those for which they were intended.
3. Fail to include certain intangible assets and infrastructure.
4. Adequately safeguard capital assets from weather, loss, or misuse.
5. No procedures in place to identify and record intangible assets or infrastructure.
6. Segregation of duties:
 1. the individual responsible for asset accountability and the person who accounts for the assets is not adequate.
7. Periodic inventories of the capital assets are not performed.
8. Periodic counts of the capital assets are performed, but the custodian makes adjustments to the asset listing without obtaining the proper approvals.

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Applicable problem areas (cont'd)

8. Capital assets have been charged to repairs and maintenance or not recorded at all.
9. Entity is using improper lives or methods for calculating depreciation charges.
10. Material amounts of assets no longer in service are included in the capital asset amounts and have not been separately identified or removed from the books.
11. Asset impairments are not periodically evaluated.

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Final Thoughts

Capital Asset Policies

- Additions
- Accurate Records
- Depreciation
- Existence
- Disposal
- Funding

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Questions?

Benjamin O. Hart
(316) 267-7231

Benjamin.hart@aghlc.com
www.linkedin.com/in/benjaminhartcpa

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