POLICY NO. P14-01

CITY OF COLDWATER, MICHIGAN
& COLDWATER BOARD OF PUBLIC UTILITIES

CAPITAL ASSETS POLICY

I. Purpose of the Policy

The purpose of this policy is to identify, classify and capitalize all capital assets of the City of Coldwater (City) and Coldwater Board of Public Utilities (CBPU). The basic goal and objective of this policy is to define and describe a set of standard procedures and policies necessary to record and control the changes in the capital assets system in accordance with generally accepted accounting principles. In addition, a capital assets policy is necessary to:

- Ensure that the asset is adequately protected from loss, theft, etc.
- Provide necessary documentation for the effective use, maintenance, management and reporting of the asset.
- Facilitate the calculation and recording of deprecation.
- Provide necessary documentation for insurance purposes.
- Provide information useful for capital planning.

In order to achieve these purposes, the capital assets system must be maintained on a current basis and the information must be complete, accurate, and consistent. The accounting policies defined below will assist the City/CBPU in achieving these purposes.

A. Capital Asset Definition

Capital assets are those assets of a long-term character which are used in the operation of the City/CBPU and are intended to be held or used for an extended period of time, such as land, land improvements, buildings and improvements, vehicles, machinery and equipment, furniture and fixtures, construction in progress, and infrastructure.

A capital asset must meet all of the following criteria:

- It must be tangible in nature.
- It must meet or exceed the capitalization thresholds established by Council and Board (see Section I, Paragraph C below)
- It normally has a useful life of five (5) years or longer. One exception to this is special purpose vehicles with a high level of use such as police cruisers. This category of vehicle must have a useful life of at least three (3) years.

B. Classifications of Capital Assets

The City/CBPU classifies capital assets in either the General Fixed Assets Account Group or within individual proprietary funds. Capital assets whose ownership rests with the City/CBPU, which are purchased from general, special revenue, or capital project funds and which are used by governmental fund departments are accounted for in the governmental account group. Capital assets purchased from enterprise funds or purchased from other sources and contributed to an enterprise fund are accounted for in the individual enterprise fund. Capital assets are added if received by June 30 (fiscal year end) no matter when encumbered or paid for.

The common capital asset categories are defined as follows:

1) Land – Any land owned by the municipality whether vacant or not, including building sites, parking lots, parks, etc. Land is to be capitalized but not depreciated. It is recorded at historical cost and remains at the cost until disposal. If there is a gain or loss on the sale of land, it is reported as a special item in the statement of activities.

2) Land Improvements – Land improvements consist of betterments, site preparation and site improvements (other than buildings) that ready land for its intended use. The costs associated with improvements to land are added to the cost of the land. Site improvements include improvements such as excavation, non-infrastructure utility installation, driveways, sidewalks, parking lots, flagpoles, retaining walls, fencing, outdoor lighting, and other non-building improvements intended to make the land ready for its intended purpose.

3) Buildings – A building is a structure that is permanently attached to the land, has a roof, is partially or completely enclosed by walls, and is not intended to be transportable or moveable. Buildings should be recorded at either their acquisition cost or construction cost. The cost of new construction should be carefully evaluated. Usually projects consist of major components such as land, land improvements, building construction (including professional fees and permits), furniture, fixtures, and equipment. In addition, buildings include components (e.g. roof, air conditioner system, etc.) that should be recorded separately when significant because these building components have different useful lives. The value of each component needs to be determined and placed within its own category.

4) Building Improvements – Building improvements are capital events that materially extend the useful life of a building or increase the value of a building, or both. A building improvement should be capitalized as a betterment and recorded as an addition of value to the existing building if the expenditure for the improvement is at the capitalization threshold, or the expenditure increases the life or value of the building by at least 25 percent of the original life period or cost. Examples of building improvements include major energy conservation projects, remodeling, replacing major building components, and building additions. The cost of these improvements will not be added to the existing asset cost, but will be capitalized and depreciated separately.

    Note regarding replacement: For a replacement to be capitalized, it must be a part of a major repair or rehabilitation project that increases the value and/or useful life of the building, such as renovation. A replacement may be capitalized if the new item/part is of significantly improved quality and higher value compared to the old item/part, such as replacement of an old shingle roof with a new fireproof tile roof. Replacement or restoration to original utility level would not qualify as a capitalized asset and should be recorded as maintenance expense. Determinations must be made on a case-by-case basis.

5) Vehicles – These are self-explanatory but they should have a certificate of title and a license plate and be used to drive on roads. Certain items such as backhoes, pay loaders, and trailers should be classified as equipment.

6) Machinery and Equipment – Those items not belonging in a specific category but meeting the definition of a fixed asset.

7) Furniture and Fixtures – Items used to furnish a building and fixtures such as shelving, cabinetry, etc.

8) Construction in Progress – Construction in progress should be capitalized and not depreciated. These are costs for projects not completed during the year. When the project is completed and put into use by the City/CBPU, it should be capitalized in the proper category. If construction costs are funded in part or in whole by a debt instrument, the interest paid on said debt prior to the asset being booked shall be capitalized as part of the construction.

9) Infrastructure – Infrastructure assets are long-lived capital assets, normally stationary in nature, and can be preserved for a significantly greater number of years than most capital assets. Infrastructure assets include roads, bridges, signage, light system (traffic, outdoor, street, etc.), curbs and gutters, streets and sidewalks, drainage systems, water pipelines, sewer pipelines, lighting systems, fiber optic cables, radio, television and electric transmission system and other similar assets that are immovable and of value only to the City/CBPU.

10) Infrastructure Improvements – Infrastructure improvements are capital events that materially extend the useful life or increase the value of the infrastructure, or both. Infrastructure improvements are capitalized as a betterment and recorded as an addition of value to the infrastructure if the improvement or addition of value is at the capitalization threshold or increases the life or value of the asset by at least 25 percent of the original cost or life period.

    a. Additions and Improvements – Additions and improvements are those capital outlays that increase the capacity or efficiency of the asset. A change in capacity increases the level of service provided by an asset. For example, additional lanes can be added to a highway or the weight capacity of a bridge could be increased. A change in efficiency maintains the same service level, but at a reduced cost. For example, a heating and cooling plant could be reengineered so that it produces the same temperature changes at reduced cost. The cost of additions and improvements should be capitalized.

    b. Preservation Costs – Preservation costs are generally considered to be those outlays that extend the useful life of an asset beyond its original estimated useful life but do not increase the capacity or efficiency of the asset. Preservation costs should be capitalized.

    c. Maintenance Costs – Maintenance costs allow an asset to continue to be used during its originally established useful life. Maintenance costs are expensed in the period incurred.

11) Leased Assets – Prior to entering into a lease agreement for an item that meets capital asset criteria, a determination should be made as to whether it is an operating lease or a capital lease. The underlying issue in making the distinction is whether the benefits and risks of ownership are transferred from the lessor to the lessee. Another measurement is whether the lease is merely an extended rental agreement or actually an installment purchase in the form of a capital lease. Usually a lease is a capital one if the lease transfers ownership to the lessee at the end of the lease term; the lease contains a bargain purchase option; the lease term is 75% or more of the estimated useful life of the property; or, the present value at the beginning of the lease term of the minimum lease payments equals or exceeds 90% of the fair value of the leased property. Any questions regarding the nature of a particular lease should be directed to the Finance Director.

C. Capitalization Thresholds

Standard capitalization thresholds for capitalizing assets are established for each major class of assets, and all departments are required to use the following thresholds:

Class of Asset	Threshold
Land/land improvements	Capitalize All
Building/building improvements	$10,000
Vehicles	$10,000
Machinery and Equipment	$10,000
Furniture and Fixtures	$10,000
Infrastructure/infrastructure improvements	$50,000
Telecommunication assets	$10,000
Leased assets	$10,000

D. Methods of Valuing Capital Assets

The general policy for valuation of assets is that all assets which are capitalized should be recorded at historical cost. Historical cost includes not only the purchase prices or construction costs, but also ancillary charges like freight and transportation fees, site preparation expenditures, professional fees, legal claims, etc., necessary to place the asset in its intended location and condition for use. However, there are instances in which historical cost information is not available or inappropriate for valuation purposes.

- Historical Cost Information Unavailable – Should valuation problems arise when attempting to establish accurate historical costs for items acquired in the past, the City/CBPU will employ whichever of the following valuation methods is deemed to be most appropriate to the asset being examined.
    - Historical Price Estimated Method – To be employed if the date of acquisition is known and manufacturer/retailer prices are available; or

    - Price Deflation Method – To be employed if such historic prices are unknown or known to be inappropriate given unique, local purchase circumstances. In this case, present prices are deflated to the year in which the asset was acquired, using the consumer price index as prepared by the United States Bureau of Labor Statistics.

- Gifts and Donations – For assets acquired through gifts or donations, the estimated fair value at the time of the receipt of the assets will be the capitalized value. Under normal circumstances, fair value can be determined from source documents involved in the acquisition transaction – purchase prices, contracts, court judgment awards, etc. However, where source documents are unavailable or incomplete, two valuation methods are appropriate:

    - Historic Price Estimate Method – To be employed if the date of acquisition is known and manufacturer retail prices are available; and

    - Appraisal Method – To be exercised if mandated as a condition of the City/CBPU's acceptance of the asset or if other valuation methods seem inappropriate.

- Eminent Domain – Assets acquired through exercise of eminent domain powers are often subject to the compensation determined by a court of competent jurisdiction, most frequently resulting in a single-stage transaction not unlike a regular purchase. The carrying value, then, will be the cost of compensating the property owner(s), plus such ancillary costs as legal and title fees, surveying fees, appraisal and negotiation fees, damage payments, site preparation costs (clearing, filling, leveling), and demolition of unwanted structures.

E. Asset Life

Asset life is the amount of time (reported in years) the City/CBPU is expected to receive benefit from the asset. Asset life is generally determined by past practice, historical records of improvement replacements, and generally accepted standards by the majority of municipalities. City/CBPU use the following table of asset life:

Description	Governmental Activities Estimated Lives	Business-type Activities Estimated Lives
Land Improvements	5-20 years	5-20 years
Buildings/building improvements	20-40 years	20-40 years
Vehicles	5-10 years	5-10 years
Machinery and Equipment	5-25 years	5-25 years
Furniture and Fixtures	5-15 years	5-15 years
Infrastructure/infrastructure improvements	25-60 years	25-60 years
Telecommunication assets	3-15 years	3-15 years
Leased assets	5-25 years	5-25 years

F. Depreciation

The City/CBPU uses the straight-line method of depreciation. The cost of the assets is divided by the estimated life to come up with the annual depreciation. The City/CBPU uses the full-month convention for assets purchased during the year. Under a full-month convention, property placed in service at any time during a given month is treated as if it had been placed in service on the first day of that month. This allows depreciation to be taken for the entire month in which the asset is placed in service. If the property is disposed of before the end of the estimated useful life, no depreciation is allowed for the month of disposition.

G. Capital Asset Retirements and Transfers

Retirements

City/CBPU capital assets are retired through either disposal, trade-in, sale or loss. The manner of removing assets from the capital asset subsystem records differs for those assets appearing in the governmental account group, as compared to those within proprietary fund types.

If an asset is sold, traded or in retired, the appropriate record is removed from the account group, along with applicable accumulated depreciation. The cash received is posted to the appropriate governmental fund as current revenue. For assets exchanged for replacements, the purchase price of the new asset is reduced by the trade-in value given for the old. The latter is then removed from the capital asset records along with accumulated depreciation.

Retirement of assets within proprietary fund types incorporates gains and losses due to the profit-oriented nature of proprietary funds. All losses incurred through retirement are recognized immediately as such. Gains realized through the sale of capital assets are recognized. Any gains recognized in exchanges of capital assets are credited to the value of the new asset.

Transfers

Transfers of property between any fund types may be a current account transaction or a capital contribution. The asset should be valued at cost or at the fair market value of the transferred asset on the date of the transfer. Transfers among enterprise funds should be treated as current account transactions with gains/losses on sale/disposition of assets recorded.

II. Fixed Asset Recording Procedures

A. Fixed Asset Purchases

City Department Heads/CBPU Superintendents are to purchase fixed assets valued over the thresholds listed in Paragraph I.A. above from capital line items only. The Finance Director will review capital line items during the year to determine which assets need to be set up in the fixed asset database.

B. Fixed Asset Database

At the time a capital asset has been received by the City/CBPU and/or placed into service, the invoice and related paperwork will be entered into the fixed asset database. Information recorded on each asset will be: description of the asset, department, location, cost, serial and model numbers, useful life and date of purchase. At the end of each year, the Finance Director, or designee, will prepare a print-out of asset additions and deletions during the year, along with a listing of capital assets as of the end of the year.

III. Annual Insurance Appraisal

At the end of each year, the Finance Director, or designee, will prepare an updated list of assets valued for insurance purposes to ensure that the assets of the City /CBPU are properly insured.

IV. Annual Asset Inventory

Because of the high volume of asset-related transactions, sometimes even the best internal controls cannot always capture every change. For that reason, at least once per calendar year departments will receive a listing of the fixed assets on record for that department from the Finance Director. The assigned departmental employee should check the listing and note any additions, changes, or deletions that need to be made. Also, periodically the Finance Director may authorize a physical inventory to be done by a representative of the Finance Department. That representative will then conduct a physical inventory of the designated department's assets using the current fixed asset inventory records to ensure that the information is both accurate and inclusive. Following such physical inventory, the Finance Director will notify the Department Head of any adjustments that may need to be made.

V. Responsibilities of Department Heads

Departments are responsible for the proper use, care and maintenance of fixed assets in their possession. If repairs are required, they should be performed expeditiously to keep assets in good working condition. In addition, departments must insure that all assets are maintained in a secure manner to minimize loss, damage and unauthorized use.

Department Heads are responsible to identify and report all non-purchase capital assets acquisitions of the Finance Department. Such acquisitions could be obtained as the result of a gift, grant, transfer, legal confiscation or manufacture by the department.

Department Heads are also responsible to notify the Finance Director if a capital asset item is destroyed or damaged, so that the Finance Director can delete these items from the asset listing and notify the City/CBPU's insurance agent in order to report a claim and/or remove the asset from the City/CBPU's insurance policy.