

RESOLUTION NO. 3478

A RESOLUTION TO ADOPT A CAPITAL ASSET POLICY FOR THE CITY OF RED LODGE, MONTANA.

WHEREAS, the Department of Administration began requiring local governments to begin the implementation of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* beginning with the fiscal year ending June 30, 2003.

WHEREAS, the City of Red Lodge implemented GASB Statement No. 34 early, beginning with the fiscal year ending June 30, 2004.

WHEREAS, two key implementation challenges the new reporting model presents are infrastructure reporting and depreciation accounting.

WHEREAS, it is the objective of the City to (1) accurately account for and report capital assets in financial reports issued to external reporting agencies, granting agencies and the public, and (2) to adequately safeguard the City's capital assets from loss or theft for which the City has a fiduciary responsibility to establish systems and procedures to protect these capital assets.

WHEREAS, the City Clerk has the responsibility for maintaining the inventory and accounting records of capital assets that pertain to the City's operations.

BE IT RESOLVED by the Council of the City of Red Lodge to adopt the following CAPITAL ASSET POLICY for the CITY OF RED LODGE.

The criteria for capitalization of the CAPITAL ASSET program, as well as the distinction between and treatment of assets not meeting the criteria for capitalization, are provided as follows:

I. Capital Asset Definition and Guidelines

A capital asset of the City of Red Lodge must be real or personal property that has a value equal to or greater than the capitalization threshold for the particular classification of the asset and must have an estimated useful life of greater than one year.

The City has invested in a broad range of capital assets that are used in the City's operations, which may include:

- Land, including Land and Improvements
- Buildings
- Improvements Other than Buildings
- Machinery and Equipment (general plant for water and sewer)
- Infrastructure (streets, curbs, sidewalks, water and sewer lines, wells, pumps, and treatment plant)
- Construction Work in Progress

Capital Asset Classification

Assets purchased, constructed or donated that meet or exceed the City's established capitalization threshold or minimum reporting requirements must be uniformly classified utilizing the uniform statewide BARS Chart of Accounts.

Capitalization Thresholds

The capitalization threshold is applied to **individual units** of capital assets. For example, ten desks purchased through a single purchase, each costing \$1,000, will not qualify for capitalization even though the total (\$10,000) exceeds the threshold of \$5,000.

For purposes of capitalization, the threshold will generally not be applied to **components** of capital assets. For example, a keyboard, monitor and central processing unit purchased as components of a computer system will not be evaluated individually against the capitalization threshold. The entire computer system will be treated as a single capital asset.

Class of Asset	Threshold
Land/Land Improvements	Capitalize all
Buildings/Building Improvements	\$10,000
Improvements other than buildings	\$5,000
Machinery and equipment	\$5,000
Infrastructure	\$25,000
Library books/materials	Will not capitalize; Library will maintain own records.

Capital Asset Acquisition Cost

Capital assets should be recorded and reported at their historical costs, which include 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. Historical costs also include ancillary charges such as freight and transportation charges, site preparation costs and professional fees. The cost of capital assets recorded in **governmental activities** will not include capitalized interest. However, for proprietary funds, interest is capitalized on:

- Assets that are constructed or otherwise produced for the City's own use (including assets constructed or produced for the enterprise by others for which deposits or progress payments have been made)

Capital Asset Donation

Assets donated should be reported at their fair market value on the date the donation is made.

Leased Equipment

Equipment should be capitalized if the lease agreement meets any one of the following criteria:

- The lease transfers ownership of the property to the lessee by the end of the lease term.
- The lease contains a bargain purchase option.

- The lease term is equal to 75 percent or more of the estimated economic life of the leased property.
- The present value of the minimum lease payments at the inception of the lease, excluding executory costs, equals at least 90 percent of the fair value of the leased property.

Leases that do not meet any of the above requirements should be recorded as an operating lease and reported in the notes to the financial statements.

Depreciating Capital Assets

Capital assets should be depreciated over their estimated useful lives. The **straight-line depreciation method** (historical cost less residual value, divided by useful life) will be used by the City. The useful estimated life may be determined using general guidelines obtained from professional or industry organizations, information for comparable assets of other governments. In determining useful life, the City will consider the asset's present condition and how long it is expected to meet service demands.

Depreciation will be calculated and recorded in the City's capital asset records for each eligible asset. Accumulated depreciation should be summarized and posted to the accounting general ledger.

Residual Value

In order to calculate depreciation for an asset, the estimated residual value, if any, must be declared before depreciation can be calculated. The use of historical sales information becomes invaluable for determining the estimated residual value. Proceeds from sale of assets must be netted against residual value in computing net gain or loss from sale.

Controlled Assets

Controlled assets are assets that must be secured and tracked as inventory. Controlled assets with an acquisition cost of more than \$1,000 and less than \$5,000 will not be capitalized or depreciated for general purpose external financial reporting purposes. Department heads are responsible for inventorying controlled assets and maintaining adequate records within their own department. Department heads on an annual basis should compare the City Finance Administrator's detailed records with their inventory. The department head must perform a physical inventory annually.

II. Capital Asset Categories

Land and Land Improvements – BARS Asset Account No. 181000

Land Definition – Land is the surface, which can be used to support structures, and may be used for growing grass, shrubs, and trees. Land is characterized as having an unlimited life (indefinite).

Land Improvement Definition – 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.

Depreciation Methodology – Land and land improvements are inexhaustible assets and do not depreciate over time.

Capitalization Threshold – All acquisitions of land and land improvements will be capitalized.

Examples of Expenditures to be Capitalized as Land and Land Improvements

- Original purchase price or fair market value at time of gift
- Commissions
- Professional fees (title searches, architect, legal, engineering, appraisal, surveying, environmental assessments, etc.)
- Land excavation, fill, grading, drainage
- Demolition of existing buildings and improvements (less salvage)
- Removal, relocation, or reconstruction of property of others (railroad, telephone and power lines)
- Interest on mortgages accrued at time of purchase
- Accrued and unpaid taxes at date of purchase
- Other costs incurred in acquiring the land
- Water wells (include initial cost for drilling, the pump and its casing)
- Right-of-way

Buildings and Building Improvements – BARS Asset Account No. 182000

Building Definition – A building is a structure that is permanently attached to the land and is not intended to be transportable or moveable.

Building Improvement Definition – 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 meets or exceeds the capitalization threshold, or the expenditure increases the life or value of the building by 25% of the original life period or cost.

Depreciation Methodology – The straight-line depreciation method (historical cost – residual value)/useful life) will be used for buildings and building improvements. Subsequent improvements that change the use or function of the building shall be depreciated.

Capitalization Threshold – The capitalization threshold for buildings and building improvements is \$10,000.

Examples of Expenditures to be Capitalized as Buildings:

Purchased Buildings

- Original purchase price
- Expenses for remodeling, reconditioning or altering a purchased building to make it ready to use for the purpose for which it was acquired

- Environmental compliance
- Professional fees (legal, architect, inspections, title searches, etc.)
- Payment of unpaid or accrued taxes on the building to date of purchase
- Cancellation or buyout of existing leases
- Other costs required to place or render the asset into operation

Constructed Buildings

- Completed structure costs
- Interest accrued during construction (proprietary activities only)
- Cost of excavation or grading or filling of land **for a specific building**
- Expenses incurred for the preparation of plans, specifications, blueprints, etc.
- Cost of building permits
- Professional fees (architect, engineer, management fees for design and supervision, legal)
- Costs of temporary buildings used during construction
- Unanticipated costs such as rock blasting, piling, or relocation of the channel of an underground stream
- Permanently attached fixtures or machinery that cannot be removed without impairing the use of the building
- Additions to buildings (expansions, extensions, or enlargements)

Examples of Expenditures to be Capitalized as Improvements to Buildings

Note: For a replacement to be capitalized, it must be a part of a major repair or rehabilitation project, which meets or exceeds the capitalization threshold, or the expenditure increases the life or value of the building by 25 percent of the original life period or cost. A replacement may also 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. Determinations must be made on a case by case basis.

- Conversion of attics, basements, etc., to usable office space
- Structures attached to the building such as garages
- Installation or upgrade of heating and cooling systems
- Installation/upgrade of wall or ceiling covering such as carpeting, tiles, paneling, or parquet
- Structural changes such as reinforcement of floors or walls, installation or replacement of beams, rafters, joists, steel grids, or other interior framing
- Installation or upgrade of window or door frames, upgrading of windows or doors, built-in closet and cabinets
- Interior renovation associated with casings, baseboards, light fixtures, ceiling trim, etc.
- Exterior renovation such as installation or replacement of siding, roofing, masonry, etc.
- Installation or upgrade of plumbing and electrical wiring

- Installation or upgrade of phone systems, fiber optic cable, wiring required in the installation of equipment (that will remain in the building)
- Other costs associated with the above improvement

Building Maintenance Expense

The following are examples of expenditures not to capitalize as improvements to buildings. Instead, these items should be recorded as maintenance expense.

- Adding, removing and/or moving of walls relating to renovation projects that are not considered major renovation projects and do not increase the value of the building
- 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 decoration, such as draperies, blinds, curtain rods, wallpaper
- 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
- 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
- Any other maintenance-related expenditure which does not increase the value or useful life of the building

Improvements Other Than Buildings – BARS Asset Account No. 184000

Definition - Assets (other than general use buildings) built, installed or established to enhance the quality or facilitate the use of land for a particular purpose. Depreciable improvements made to land that should be capitalized as a betterment if the improvement is at the capitalization threshold.

Depreciation Methodology – The straight-line depreciation method (historical cost less residual value, divided by useful life) will be used for improvements other than buildings.

Capitalization Threshold – The capitalization threshold for improvements other than buildings is \$5,000.

Examples of Expenditures to be Capitalized as Improvements Other than Buildings

- Fencing and gates
- Landscaping
- Parking lots/driveways/parking barriers
- Outside sprinkler systems
- Recreation areas and athletic fields (including bleachers)

- Golf courses, swimming pools, tennis courts, basketball courts
- Paths and trails
- Septic systems
- Fountains, plazas and pavilions
- Retaining walls

Machinery and Equipment – BARS Asset Account No. 186000

Definition – Tangible property of more or less permanent nature, other than land, buildings, or improvements, which is useful in carrying on operations. Improvements or additions to existing machinery and equipment that exceeds capitalization threshold or increases the value or life of the asset by 25 percent of the original cost or life should be capitalized as a betterment and recorded as an addition of value to the existing asset.

Note: Costs of extended warranties and/or maintenance agreements, which can be separately identified from the cost of the equipment, should not be capitalized.

Depreciation Methodology – The straight-line depreciation method (historical cost less residual value, divided by useful life) will be used for machinery and equipment.

Capitalization Threshold – The capitalization threshold for machinery and equipment is \$5,000. Machinery and equipment with a cost of at least \$1,000 and under \$5,000 will be accounted for as inventory but will not be capitalized.

Examples of Expenditures to be Capitalized as Machinery and Equipment

- Machinery, tools
- Trucks, cars
- Furniture, furnishings
- Original contract or invoice price
- Freight, handling and storage charges
- In-transit insurance charges
- Sales tax imposed on the acquisition
- Installation charges
- Charges for testing and preparation for use
- Costs of reconditioning used items when purchased
- Parts and labor associated with the construction of equipment

Infrastructure – BARS Asset Account No. 187000

Infrastructure Definition – Assets that are 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.

Infrastructure Improvements – are capital events that materially extend the useful life and/or increase the value or capacity of the infrastructure. A change in capacity increases the level of service provided by infrastructure. For example, additional lanes can be added to a highway or the weight capacity of a bridge could be increased.

Infrastructure improvements should be capitalized as a betterment and recorded as an addition of value to the infrastructure in the improvement is at the capitalization threshold or increases the life or value of the asset by 25 percent of the original cost or life period.

Maintenance Costs – allow infrastructure to continue to be used during its originally established useful life. Maintenance costs are expenses in the period incurred.

Depreciation Methodology – The straight-line depreciation method (historical cost less residual value, divided by useful life) will be used for improvements.

Capitalization Threshold – The capitalization threshold for improvements is \$25,000. Infrastructure already capitalized will remain capitalized.

Jointly Funded Infrastructure – paid for jointly by the City and other governmental entities should be capitalized by the entity responsible for future maintenance.

Examples of Expenditures to be Capitalized as Infrastructure

- Highways (including Rest Areas)
- Roads and Streets (Including Curbs, Gutters, Sidewalks, Signage and Fire Hydrants)
- Bridges
- Drainage Systems
- Lighting Systems
- Fiber Optic Distribution Systems (Between Buildings)

Utility Plant – BARS Asset Account No. 189000 – Proprietary Funds

Utility Plant Definition – type of infrastructure asset accounts that are specific to the recording of water and sewer systems. A further breakdown of Utility Plant follows:

- **Source of Supply – BARS Asset Account No. 189100**

A fixed asset account that reflects the acquisition value of property used to supply the water and sewer system of a governmental unit.

Examples of Expenditures to be Capitalized as Source of Supply Infrastructure

- Wells, springs, reservoirs, and supply mains.

- **Pumping Plant – BARS Account No. 189200**

A fixed asset account which reflects the pumping process of the water or sewer system.

Examples of Expenditures to be Capitalized as Pumping Plant Infrastructure

- Electric pumps, steam pumps, diesel pumps, boiler plant equipment and hydraulic pumping equipment.

- **Treatment Plant – BARS Account No. 189300**

A fixed asset account which reflects the acquisition value of property used in the treatment of the water and sewer system.

Examples of Expenditures to be Capitalized as Treatment Plant Infrastructure

- Chlorinator injector equipment and other water treating equipment; sewage storage lagoons, and any equipment relating to treatment.

- **Transmission and Distribution – BARS Account No. 189400**

A fixed asset account which reflects the acquisition value of property used in the distribution process of the water and sewer systems.

Examples of Expenditures to be Capitalized as Transmission and Distribution Infrastructure

- Fire mains, hydrants, transmission and distribution mains, meters, and standpipes.

- **General Plant – BARS Account No. 189500**

A fixed asset account which reflects the acquisition value of property used in the general operation of the water and sewer systems.

Examples of Expenditures to be Capitalized as General Plant Infrastructure

- Transportation equipment, stores equipment, land, tools and laboratory equipment.

Construction in Progress – BARS Asset Account No. 188000

Definition – Construction in Progress reflects the economic construction activity status of buildings and other structures, infrastructure (roadways, distribution, collection and treatment systems, etc.), additions, alterations, reconstruction, installation, and maintenance and repairs, which are substantially incomplete.

Depreciation Methodology – Depreciation is not applicable while assets are accounted for as Construction in Progress. See appropriate capital asset category when asset is capitalized.

Capitalization Threshold – Construction in Progress assets should be capitalized to their appropriate capital asset categories upon the earlier occurrence of execution of substantial completion contract documents, occupancy, or when the asset is placed into service.

The Council further orders the City Mayor to amend and/or adjust the current capital asset detailed records and the accounting records to reflect the capitalization threshold, except for those assets that are exempt from the increase.

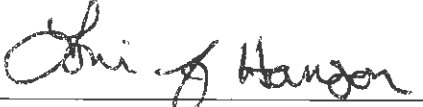
PASSED AND APPROVED BY THE RED LODGE CITY COUNCIL on this 26th day of June, 2018.

City of Red Lodge:




William Larson, Mayor

Attest:



Loni Hanson, City Clerk



Rebecca Narmore, City Attorney