

3. ACCOUNTING

3.3 Capital Assets

3.3.8 Capital Assets Management

3.3.8.10 Definitions

Capital assets are real and personal property and intangible assets, above a specified value, the government intends to use or keep for more than one year. Capital assets include land and land rights; buildings, their furnishings, fixtures, and furniture; equipment, machinery, vehicles, and tools.

Capitalize means to report an expenditure for real and personal property or intangible assets as a capital outlay. These expenditure transactions are coded to 594 and 595 account codes.

Accountability means the obligation to demonstrate good management of or control over those matters for which the government is responsible.

Capital assets management system is the set of written policies and procedures used to control a government's capital assets and demonstrate accountability.

Capitalization threshold is a dollar amount set in a formal policy defining when an item with more than one or more years of usefulness will be classified as a capital asset.

Physical inventory is a procedure where the existence of assets on the inventory list is confirmed by physically observing the assets at their location in the field.

3.3.8.20 Reporting Capital Asset Transactions

Cash basis accounting only reports inflows and outflows of cash. When a capital asset is purchased the entire expenditure is recognized in the period when the cash outflow occurs. Because the entire asset cost is reported when it was purchased the reporting of depreciation accounts is not appropriate.

Determination of when a purchased item is classified as a capital asset will depend upon the capitalization policy of the government. Each government should establish a formal policy that includes a capitalization threshold. The amount of the capitalization threshold is up to the government and may vary. Many governments have set their policy at \$5,000.

The cash basis financial reporting requirements for capital assets are limited; however, this does not remove the responsibility of the government from its stewardship of public resources. Entities must have policies and procedures in place to track, demonstrate accountability and insure security of their capital assets.

3.3.8.30 General Tracking Requirements

Specific capital asset tracking requirements of the State Auditor's Office are contained on the subsequent pages. In addition, the federal government has issued property management requirements that apply to all governments that receive federal assistance. Each federal agency has published a Federal Agency Implementation of the Common Rule. Excerpts from the Common Rule have been included in this section. Note that these requirements involve broad stewardship responsibilities and specific accounting records.

Establishing Capital Assets Policies

Local governments with capital assets should develop policies and procedures for management of these public resources. At a minimum the policies should be reviewed and approved by the governing body.

The duty to make certain that public property is adequately protected and that its use is properly managed is one of the fundamental responsibilities of government officials. The government has several broad responsibilities with respect to capital assets. The following are items the government must consider when developing policies for tracking and safe guarding their capital assets.

- 1) **Capitalization Threshold.** Entities must set the dollar amount at which the purchase of an asset with a useful life of more than one year will be classified as a capital asset. The cost of maintaining the information versus the benefit of the information should be evaluated when setting the threshold.
- 2) **Information.** What information is available and how the government will gather it?
- 3) **Custody.** The responsibility for custody means having the answers to such questions as:
 - a) What property and equipment does this government own?
 - b) Where is it?
 - c) What condition is it in?
 - d) Who is responsible for the asset and is it protected from loss and unauthorized use?
- 4) **Insurance.** Another major responsibility for capital assets is providing adequate insurance. A capital asset accounting system should provide adequate records to prove any losses. Location, inventory, and maintenance records will confirm that a lost or damaged asset has been in use recently, which will support the validity and timeliness of a theft or damage report.
- 5) **Maintenance and Repair.** As a steward of public property, a government has the obligation not only to safeguard assets from loss but also to ensure that they are not neglected or wasted.
- 6) **Planning.** Another general category of responsibility is planning for future asset needs both short and long-term. Here a government needs answers to questions such as:
 - a) How well is the government using the facilities and equipment it already has?
 - b) Which items must be replaced, when and at what cost?
 - c) When will additional facilities or equipment be needed and at what cost?
 - d) Which facilities or equipment will not be needed, and what cost reductions in maintenance, insurance, and security will result from liquidating them?
- 7) **Small and Attractive Assets.** An additional responsibility is to assure that equipment and personal property below the capitalization threshold is also adequately safe guarded from misuse or loss. This will require management to answer questions such as:
 - a) What small and attractive property and equipment does this government own?
 - b) Where is it?
 - c) Is it protected from loss and unauthorized use?
 - d) How will it be tracked and monitored?

3.3.8.50 **The Capital Asset Tracking System**

When a government has capital assets it must establish and maintain a tracking system for them. It may be maintained using either a computerized or manual system. At a minimum it should include the following.

- 1) The tracking system must adhere to the formal asset policies approved by the governing body.
- 2) It must contain the following information:
 - a) Inventory list containing capital assets owned by the government.
 - b) Individual information record for each capital asset:
 - i. Location of the asset
 - ii. Cost of the asset/source of funding (federal grant, etc.)
 - iii. Estimated life
 - iv. Condition of the asset
 - v. Identifying number for the asset
 - vi. Disposal – date and method used to determine disposal value
- 3) Reconciliation of asset records and performance of a physical inventory.
- 4) Maintain a method with controls over additions and deletions to the capital asset tracking system.
- 5) Have a method to track changes in custody and assigned responsibility for the assets.

3.3.8.60 **Physical Inventory/Reconciliations**

All governments should have a method to perform a physical inventory to verify the existence and condition of their capital assets. Policies and procedures governing the taking of regular physical inventories should be documented. These policies should require an inventory or inventories to be taken at a reasonable interval based on the nature of assets, number of assets and extent of decentralization. Policies should also conform to any statutory or regulatory requirements, such as the requirement for counties to annually inventory all capital assets per RCW [36.32.210](#) or the requirement for all assets over \$5,000 per unit purchased with federal grant funds to be inventoried at least once every two years per the OMB Circular A-102 Common Rule. The policy should define the categories or types of assets to be inventoried, the threshold of such assets to be inventoried, state who is responsible for performing the physical inventory or inventories, is responsible for following up on any missing assets and how often the inventory or inventories must take place.

If possible the physical inventory should be conducted by personnel other than those charged with custody of the assets. Discovery of damaged or missing assets should be immediately followed up on and documented. Losses of public resources are required to be reported to our office. The capital assets list and individual asset records should be compared/reconciled. This is to assure the addition of new assets and removal old ones are updated in both sets of records. Reconciliations should be performed at least once per year.

FEDERAL COMMON RULE – PROPERTY MANAGEMENT

3.3.8.70 Capital assets purchased with federal funds are subject to federal compliance requirements. The requirements are known as the federal common rule for property management. They apply whether the assets are purchased in whole or in part with federal resources and are in addition to the accountability requirement prescribed by our office. The federal rules are in effect during the time the asset is owned by the government until official disposition has occurred.

3.3.8.80 All federal agencies administering programs that involve grants issue a common grants management rule (Common Rule). The requirements listed below are the general rules; however, some federal agencies may publish deviations from the Common Rule due to statutory requirements.

1) **Real property**

- a) **Title.** Subject to the obligations and conditions set forth in this section, title to real property acquired under a grant will vest upon acquisition with the government.
- b) **Use.** Except as otherwise provided by federal statutes, real property will be used for the originally authorized purpose as long as needed for that purpose, and the government will not dispose of or encumber its title.
- c) **Disposition.** When real property is no longer needed for the originally authorized purpose, the government will request disposition instructions from the awarding agency. The instructions will provide for one of the following alternatives:
 - **Retention of Title.** Retain title after compensating the awarding agency. The amount paid to the awarding agency will be computed by applying the awarding agency's percentage of participation in the costs of the original purchase to the fair market value of the property. However, in those situations where a government is disposing of real property acquired with grant funds and acquiring replacement real property under the same program, the net proceeds from the disposition may be used as an offset to the cost of the replacement property.
 - **Sale of Property.** Sell the property and compensate the awarding agency. The amount due to the awarding agency will be calculated by applying the awarding agency's percentage of participation in the cost of the original purchase to the proceeds of the sale after deduction of any actual and reasonable selling and fixing-up expenses. If the grant is still active, the net proceeds from the sale may offset against the original cost of the property. When a government is directed to sell property, sales procedures will be followed that provide for competition to the extent practicable and result in the highest possible return.
 - **Transfer of Title.** Transfer title to the awarding agency or to a third party designated/approved by the awarding agency. The government will be paid an amount calculated by applying the government's percentage in participation in the purchase of the real property to the current fair market value of the property.

2) **Equipment**

- a) **Title.** Subject to the obligations and conditions set forth in this section, title to the equipment acquired under a federal grant will vest upon acquisition in the government.
- b) **Use**
- Equipment will be used by the government in the program or project for which it was acquired as long as needed, whether or not the project or program continues to be supported by federal funds. When no longer needed for the original program or project, the equipment may be used in other activities currently or previously supported by a federal agency.
 - The government will also make equipment available for use on other projects or programs currently or previously supported by the Federal Government, providing such use will not interfere with the work on the projects or program for which it was originally acquired. First preference for other use will be given to other programs or projects supported by the awarding agency.
 - The government must not use equipment acquired with grant funds to provide services for a fee to compete unfairly with private companies that provide equivalent services, unless specifically permitted by federal statute.
 - When acquiring replacement equipment, the government may use the equipment to be replaced as a trade-in or sell the property and use the proceeds to offset the cost of the replacement property, subject to the approval of the awarding agency.
- c) **Management Requirements.** Procedures for managing equipment (including replacement equipment), whether acquired in whole or in part with federal grant funds, until disposition takes place will, at a minimum, meet the following requirements:
- Property records must be maintained that include:
 - A description of the property
 - A serial number or other identification number
 - The source of the property
 - Who holds title
 - The acquisition date and cost of the property
 - Percentage of federal participation in the cost of the property
 - The location, use and condition of the property
 - Any ultimate disposition data including the date of disposal and sales price of the property
 - A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years.

- A control system must be developed to ensure adequate safeguards to prevent loss, damage, or theft of the property. Any loss, damage, or theft will be investigated.
 - Adequate maintenance procedures must be developed to keep the property in good condition.
 - If the government is authorized or required to sell the property, proper sales procedures must be established to ensure the highest possible return.
- d) **Disposition.** When original or replacement equipment acquired under a federal grant is no longer needed for the original project or program or for other activities currently or previously supported by a federal agency, disposition of the equipment will be made as follows:
- Items of equipment with a current per-unit fair market value of less than \$5,000 may be retained, sold or otherwise disposed of with no further obligation to the awarding agency.
 - Items of equipment with a current per-unit fair market value in excess of \$5,000 may be retained or sold and the awarding agency will have a right to an amount calculated by multiplying the current market value or proceeds from sale by the awarding agency's share of the equipment.
- e) **Federal Equipment.** In the event a government is provided federally-owned equipment:
- Title will remain vested in the federal government.
 - Governments will manage the equipment in accordance with federal agency rules and procedures, and submit an annual inventory listing.
 - When the equipment is no longer needed, the government will request disposition instructions from the federal agency.
- f) **Right to Transfer Title.** The federal awarding agency may reserve the right to transfer title to the federal government or a third party named by the awarding agency when such a third party is otherwise eligible under existing statutes. Such transfers will be subject to the following standards:
- The property will be identified in the grant or otherwise made known to the grantee in writing.
 - The federal awarding agency will issue disposition instructions within 120 calendar days after the end of the federal support of the project for which it was acquired. If the federal awarding agency fails to issue disposition instructions within the 120 calendar-day period, the government will follow the proceeding guidelines provided in subsection (d) *Disposition*.

3) **Supplies**

- a) **Title.** Title to supplies acquired under a grant will vest, upon acquisition, in the government.
 - b) **Disposition.** If there is a residual inventory of unused supplies exceeding \$5,000 in total aggregate fair market value upon termination of completion of the award, and if the supplies are not needed for any other federally sponsored programs or projects, the government will compensate the awarding agency for its share.
- 4) **Copyrights.** The federal awarding agency reserves a royalty-free, non exclusive, and irrevocable license to reproduce, publish or otherwise use, and to authorize others to use, for federal government purposes:
- a) The copyright in any work developed under a grant; and any rights of a copyright to which a government or a contractor purchases ownership with grant support.