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# City of Somerset

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## MEMORANDUM

TO: SOMERSET CITY COUNCIL

FROM: EDDIE GIRDLER, MAYOR *EM*

SUBJECT: CAPITAL ASSET POLICY

DATE: September 29, 2015

Enclosed is a Capital Asset Management Policy that revises how the city determines depreciation and capitalization of items. Our regular auditors have recommended that the policy be changed and this was prepared and approved by the city CFO. This is part of updating our policies and this type of policy requires council approval. The revision changes the capitalization from \$5,000 to \$10,000. Our auditors suggested \$25,000 but we are going to phase in the amount for capitalization purposes.

If you have any questions, please do not hesitate to contact us.

# CITY OF SOMERSET, KENTUCKY

## CAPITAL ASSET MANAGEMENT POLICY

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1. **PURPOSE:** The purpose of this policy is: (1) to describe the policies and procedures utilized in the City's capital asset management system; (2) put in place guidelines for accounting for and depreciating the City's capital assets.

The primary goals of this policy are:

- To ensure that the City's capital assets are accounted for in conformance with generally accepted accounting principles; and
- To establish a consistent and cost-effective method for accounting of the City's capital assets.

This capital asset policy is in accordance with generally accepted accounting principles and closely conforms to capital asset accounting practices as recommended by the Government Finance Officers Association. The Government Finance Officers Association (GFOA) recommends that every state and local government consider the following applicable guidelines in establishing capitalization thresholds for capital assets:

- Capital assets should be capitalized only if they have an estimated useful life of at least two years following the date of acquisition.
  - Capitalization thresholds should be applied to individual assets rather than to groups of similar items (e.g., desks, tables). (For assets that qualify for capitalization and depreciation under the "group method" however, see third paragraph under the heading "THRESHOLD" for discussion of the appropriate threshold application).
  - As a general rule, capitalization thresholds should be designed to encompass approximately 80% of a government's total non-infrastructure assets.
  - In no case should a government establish a capitalization threshold of less than \$5,000 for any individual item.
  - Governments should exercise control over their non-capitalized capital assets by establishing and maintaining adequate internal control procedures at the department level.
2. **AUTHORITY:** The City of Somerset Executive Authority which is vested in the Mayor.
  3. **APPLICATION:** This policy applies to all City Department heads and agencies operating under service agreements and contracts with City of Somerset, Kentucky.

4. **RESPONSIBILITY:** The Chief Financial Officer or their designee shall be responsible for implementation of this policy.

5. **DEFINITIONS:** See attachment entitled “Glossary of Terms”.

6. **POLICY:**

6.1. **Threshold**

Effective July 1, 2014, the City will capitalize individual assets other than Buildings, Building Improvements and Land Improvements, and Infrastructure that cost \$10,000 or more and have an estimated useful life of at least two (2) years. The capitalization threshold for Buildings and Building Improvements shall be \$50,000 and for Utility Line and Land Improvements the capitalization threshold shall be \$25,000.

However, assets acquired with debt proceeds may be capitalized regardless of cost. In addition, assets acquired prior to July 1, 2014 and capitalized at a lower threshold, may continue to be depreciated on the basis of past practice.

Individual assets that cost less than \$10,000, but that operates as part of a network system may be capitalized in the aggregate, using the group method, if the estimated average useful life of the individual asset is at least two years. A network is determined to be where individual components may be below \$15,000 but are interdependent and the overriding value to the City is on the entire network and not the individual assets (e.g. computer systems and telephone systems).

6.2. **Valuation**

In accordance with generally accepted accounting principles, the City will value its capital assets at historical cost. Historical cost includes the cost or estimated cost at the time of acquisition, freight charges, installation and site preparation charges, and the cost of any subsequent additions or improvements, excluding repairs. If a capital asset is donated to the City the asset will be valued based on the fair market value at the time the asset is donated.

6.3. **Capital Assets Inventory Report**

As part of the financial audit, the Finance Department shall submit a capital asset report to the City’s external auditor on an annual basis. This report will include the following information:

- Type of asset (i.e. land, building, infrastructure)
- Date of acquisition
- Acquisition cost
- Estimated useful life
- Annual depreciation
- Accumulated depreciation

6.4. Depreciation

The City will use the Straight-Line Method as its “basic approach” (standard approach) to depreciate capital assets.

6.5. Estimated Useful Lives

The following ranges are guidelines in setting estimated useful lives for depreciating assets with examples and suggestions listed in the tables below.

Building and Structures	20-50 Years
Vehicles	04-15 Years
Other Equipment	03-25 Years
Infrastructure	20-100 Years

<b>Major Class Short</b>	<b>General Description (Short Desc. for Minor Class)</b>	<b>Life in Years</b>	<b>SALVAGE Percentage</b>
AMBULANCE	AMBULANCE	05-00	10
AUTOS & TRUCKS	AUTO	05-00	10
AVIATION - ALL	AIRPLANE, HELECOPTER	06-00	10
BUS - ALL SIZES	BUS	08-00	10
CONSTRUCTION VEH	CONST. VEH.	05-00	10
CONSTRUCTION EQU	BOOM TRUCK, BACKHOE, DOZER, CRANE, EXCAVATOR, LOADER, ETC	08-00	10
FIRE TRUCK	FIRE TRUCK, ALL PUMPERS, RESCUE, SUPPORT	07-00	10
POLICE VEHICLES	DETECTIVE, PATROL	05-00	10
SANIT, VEHICLES	SANIT VEH.	04-00	10
SANIT, VEHICLES	REF DUMPER	09-00	10

SANIT, VEHICLES	ROLL ON/OFF	06-00	10
SANIT, VEHICLES	SWEEP MACH	05-00	10
TRUCK, GENERAL	SNOW PLOW	08-00	10
TRUCK, GENERAL	TOW TRUCK	08-00	10
TRAILER, GENERAL	TRAILER - 2WHL, 4WHL, BRUSH, CLOSED TOP	06-00	5
TRAILER, GENERAL	5TH WHEEL, LOWBOY, OPEN TOP	08-00	5
TRAILER, GENERAL	PLATFORM	10-00	5
DATA PROCESSING	PLOTTER, SCANNER,	08-00	10
FOOD PROCESSING	OVEN/STOVE, REFRIGTN	15-00	0
PAVING & SURFACING	PAVING	15-00	0
PAVING & SURFACING OFF- STREET PARKING FAC.	PARKING	15-00	0
PAVING & SURFACING SIDEWALKS & COURTYARD	SIDEWALKS	15-00	0
PAVING & SURFACING GRAVEL LOT	GRAVEL LOT	15-00	0
SITE APPURTENANCES	SITE APPUR	25-00	0
SITE APPURTENANCES	RET WALL	20-00	0
TANKS (STORAGE) TANK - ABOVE GROUND	TANK ABVGR	20-00	0

TANKS (STORAGE) TANK - UNDERGROUND	TANK UNDGR	25-00	0
TANKS (STORAGE) - WATER TANK	WATER TANK	30-00	0
PARKS	PARKS	00-00	0
PARKS UNDEVELOPED PARK	PARK UNDEVL	00-00	0
PARKS	PARK DEVL	20-00	0
AMPHITHEATRE	AMPHTHTRE	20-00	0
COURTS	COURTS	20-00	0
PLAYING FIELDS	PLYNG FLDS, RUNNING	20-00	0
MULTI USE PARK	PARK MULTI	20-00	0
RECREATIONAL	RECR AREA	20-00	0
RECREATIONAL WATER ACTIVITIES	POOL OUTDR, WATERPARK RIDES, SPASH PADS	12-00	0
GOLF COURSE	GOLF CRSE	20-00	0
FOUNTAINS	FOUNTAINS	20-00	0
PICNIC PAVILION	PICNIC PAV	20-00	0
OTHER STRUCTURES	LEAN TO & POLE BARN	20-00	0
TOWER WATER	WATER TWR	20-00	0

#### 6.6. Capital vs. Repair and Maintenance Expense

The following criteria are the basis for distinguishing costs as either capital or repair and maintenance expense:

1. With respect to improvements on non-infrastructure and infrastructure capital assets, under the **Basic Approach**, costs should be capitalized if the useful life of the asset is substantially extended, or the cost results in a substantial increase in the capacity or efficiency of the assets.
  - i. Otherwise, the cost should be expensed as repair and maintenance.

#### 6.7. Inventory

For internal control purposes, the City may maintain an inventory listing of certain assets (controlled equipment) that do not meet the above reference capitalization amounts. Controlled equipment includes items that should be specifically accounted for and inventoried periodically due to the high re-sale value of the equipment and potential risk of theft. Controlled equipment may include items such as computers, construction equipment, and other office equipment.

Each Department Head is responsible for all controlled equipment within their areas of responsibility.

#### 6.8. Disposal and Transfer of City's Assets

Disposition of City assets will be performed in accordance with applicable City policies and procedures.

### 7. **ADMINISTRATIVE PROCEDURES:**

The Chief Financial Officer with the approval of the Mayor is authorized to adjust this policy where necessary.

## City of Somerset

### Capital Asset Management Policy

#### Glossary of Terms

1. **Capital Assets:** Capital assets include land, land improvements, buildings, building improvements, construction in progress, machinery and equipment, vehicles, infrastructure, casements, intangible assets (such as computer software), and works of art and historical treasures.
2. **Capitalization:** Capitalization of an asset occurs when the cost of the asset meets the “threshold” and the “estimated useful life” set in the organizational guidelines. Under capitalization, the cost of an item is initially recorded as an asset rather than an expense.
3. **Depreciation:** Depreciation is the process of allocating the cost of property over a period of time, rather than recognizing the cost as an expense in the year of acquisition. Generally, at the end of an asset’s life, the sum of the amounts charged for depreciation in each accounting period (accumulated depreciation) will equal the original cost less salvage value.
4. **Donated Capital Asset:** Donated assets are those assets contributed to the City. The donated assets are treated like a capital asset (using the fair market value).
5. **Estimated Useful Life:** Estimated useful life means the estimated number of months or years that an asset will be able to be used for the purpose for which it was purchased. In determining useful life, consideration is given to the asset’s present condition, use of the asset, construction type, maintenance policy, and how long it is expected to meet service demands.
6. **Fair Market Value:** The amount that would be paid if the item were sold currently in a transaction between a willing buyer and a willing seller.
7. **Historical Cost:** The historical cost of a capital asset includes the cost or estimated cost at the time of acquisition, freight charges, installation and site preparation charges, and the cost of any subsequent additions or improvements, excluding repairs.
8. **Infrastructure Assets:** Infrastructure assets are long-lived capital assets that normally can be preserved for a significant greater number of years than most capital assets (non-infrastructure assets). Infrastructure assets are normally stationary in nature and are of value only to the government entity. Examples include the City sewer system, streets, or sidewalks.



9. **Salvage Value:** The salvage value of an asset is the value it is expected to have when it is no longer useful for its intended purpose. In other words, the salvage value is the estimated amount for which the asset could be sold at the end of its useful life.
10. **Straight-Line Method:** The straight-line method is the simplest and most commonly used for calculating depreciation. It can be used for any depreciable property. Under the straight-line method, the basis of the asset is written off evenly over the useful life of the asset. The same amount of depreciation is taken each year. In general, the amount of annual depreciation is determined by dividing an asset's depreciable cost by its estimated life.
11. **Threshold:** The threshold is the dollar amount that an asset must equal or exceed if that asset is to be capitalized. Otherwise, the item would be considered as an expense at the time of acquisition.

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