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State of Louisiana

Division of Administration

Office of Statewide Reporting and Accounting Policy

September 27, 2011

OSRAP MEMORANDUM 12-07

TO: Fiscal Officers
All State Entities

FROM: Afranie Adomako, CPA
Director

SUBJECT: Revision to Capitalization Guide

The Office of Statewide Reporting and Accounting Policy (OSRAP) has updated its capitalization guide to include capitalization thresholds and useful lives for various intangible assets. Governmental Accounting Standards Board (GASB) Statement No. 51 (GASB 51), "Accounting and Financial Reporting for Intangible Assets" requires that all intangible assets subject to the provisions of this statement be classified as capital assets. The revised capitalization guide is attached.

For more information on GASB 51, see OSRAP Memo 09-34. If you have any questions, please contact Ms. Inga Kimbrough at (225) 342-1088 or at Inga.Kimbrough@la.gov. All OSRAP memorandums and forms may be accessed through our home page at http://www.doa.louisiana.gov/osrap/index.htm.

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Attachment

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Guide for Capitalization and Depreciation of Capital Assets
Prepared by the Office of Statewide Reporting and Accounting Policy

The following information has been revised to include intangible assets and is provided as guidance for the capitalization and depreciation of capital assets. This guide includes capital assets categories and descriptions, definitions, capitalization threshold levels, useful lives, and the chosen method of depreciation and is only intended to provide some high level guidance and awareness of the decisions that have been made on these topics. More details on specific procedures and instructions will be provided to the appropriate entities at a later date.

I. Background:

GASB 34 states that capital assets should be reported at historical cost. The cost of a capital asset should include any charges necessary to put the asset into place. Donated capital assets should be reported at their estimated fair value at the date of donation. Capital assets include moveable property (furniture & fixtures, machinery & equipment, automobiles, etc.), land, land improvements, buildings, building improvements, leasehold improvements, infrastructure, historical treasures & works of art, and all other tangible or intangible assets that are used in operations that have initial useful lives beyond a single reporting period.

II. Quick Facts:

1. Capitalization threshold levels and useful lives for capital assets are as follows:

Capital Asset	Threshold	Useful Life
Movable Property (not including computer software)	$5,000	Varies – see table
Purchased or Licensed Computer Software (including modification costs clearly in the application development phase)	$1,000,000	3 years
Internally Generated Software	$1,000,000	7 < $10 million 10 > $10 million
Buildings & Improvements	$100,000	40 Years
Leasehold Improvements	$100,000	< of 20 or 40 years or lease term
Land and Non-Depreciable Land Improvements	N/A - capitalize all	No useful life assigned for inexhaustible assets
Depreciable Land Improvements	$100,000	20 Years
Infrastructure	$3,000,000	40 Years

Historical Treasures & Works of Art	N/A	No useful life – inexhaustible
Water Rights	100,000	40 or contract life if specified
Timber Rights	100,000	40 or contract life if specified
Mineral Rights	100,000	40 or contract life if specified
Trademarks	100,000	40 or actual life
Copyrights	100,000	100
Easements	any	Indefinite
Patents	100,000	17 or actual life

2. The straight-line depreciation method will be used for depreciation of all depreciable capital assets.
3. A full year of depreciation is taken in the year assets are placed into service. Any remaining depreciation will be taken in the year of disposal if the asset is not fully depreciated upon disposal.
4. No salvage value will be included in the depreciation calculation.

III. Identifying the different categories and classes of capital assets:

1. Movable Property

Movable property consists of those capital assets that are not fixed or stationary in nature. They are those assets that are not land, land improvements, buildings, building improvements, or infrastructure. In general, movable property includes furniture & fixtures, machinery and equipment, and automobiles. For more detailed examples of movable property, see the table of capital assets and useful lives in Section IV below.

2. Intangibles

An intangible asset should be recognized only if it is identifiable, capable of being separated and sold, transferred or licensed. Assets that arise from contractual or other legal rights, regardless of whether or not the rights are separable, are also considered intangible assets. Intangible assets follow the measurement guidance for capital assets: historical cost, or if donated, estimated fair value at the date of donation.

Computer Software and Internally Generated Software
Computer software is an intangible asset subject to capital assets reporting pursuant to GASB 51, *Accounting and Financial Reporting for Intangible Assets. Websites are included as computer software*. If the website meets the software capitalization threshold and the description of internally generated computer software, then outlays associated with its development should be capitalized.

Computer software should be considered internally generated if it is developed in-house by the government's personnel or by a third party contractor on behalf of the government. Also, commercially available software that is purchased or licensed by the government and modified using more than minimal incremental effort before being put into operation should be considered internally generated. Any of the following activities would satisfy the “modified using more than minimal incremental effort” criterion: changing code, changing fields, adding special reporting capabilities, and testing for any changes. Licensed financial accounting software that the agency modifies to provide special reporting capabilities would be considered internally generated.

Activities involved in developing and installing internally generated software are defined by three stages:

- Preliminary Project Stage: includes the conceptual formulation and evaluation of alternatives, the determination of the existence of needed technology, and final selection of alternatives for development of software. Outlays associated with activities in this stage <u>should be expensed as incurred</u>.
- Application Development Stage: includes the design of the chosen path (consisting of software configuration and interfaces), coding, installation to hardware, and testing (including parallel processing). Also includes licensing of commercially available software (GASB 51, paragraph 65).
- Post-Implementation/Operation Stage: includes application training and software maintenance. Outlays associated with activities in this stage <u>should be expensed as incurred</u>.

Outlays related to activities in the application development phase should be capitalized only upon the occurrence of all the following:

a) Determination of the specific objective of the project and the nature of the service capability to be provided by the asset.
b) Demonstration of the technological feasibility for completing the project.
c) Demonstration of the current intention, ability, and presence of the effort to complete or continue development of the asset.

The activities within the three stages of development may occur in a different sequence. The recognition guidance for outlays associated with internally generated computer software should be applied based on the nature of the activity, not the timing of its occurrence. For example, outlays associated with application training activities that occur during the application development stage should be expensed as incurred.

If an agency is developing a system such as ERP with multiple modules, the guidance for reporting outlays based on the stages of software development should be applied for each individual module of the system rather than the system as a whole.

<u>Modification of Internally Generated Software</u>

Outlays associated with an internally generated modification of software that is already in operation should be capitalized when all internally generated software intangible assets criteria have been met. A modification to existing computer software must do at least one of the following to qualify for capitalization:

a. Increase the software’s functionality
b. Increase the software’s efficiency, or
c. Extend the software’s estimated useful life

If the modification does not result in any of the above outcomes, the modification should be considered maintenance, and the associated outlays should be expensed as incurred.

<u>Other Intangibles</u>

Ownership of land includes the right to control its use and therefore embodies a bundle of rights such as water, timber mineral, right-of-way, etc. The individual rights that come with land ownership should be valued in the aggregate and reported as the tangible asset—land. Land use rights that do not include ownership of the underlying property should be valued and reported as intangible assets. If an agency actually owns the associated land and the recorded land valuation already includes the "land use rights," the intangible asset's portion associated with the land should not be reported separately as it is already included in the land valuation.

Easement/Right of Way – The right to use the land of another party for a particular purpose.

Water Rights – The right to draw water from a particular source, such as a lake, irrigation canal, or stream.

Timber Rights – The right to cut and remove trees from the property of another party.

Mineral Rights – The right to draw minerals from a particular source, such as a lake or stream.

Patent – The right to exclude others from making, using, offering for sale, selling or importing an invention. Patents are issued by the U.S. Patent and Trademark Office.

Copyright – A form of protection provided to the authors of "original works of authorship" including literary, dramatic, musical, artistic, and certain other intellectual works, both published and unpublished. Copyrights are registered by the Copyright Office of the Library of Congress.

Trademark – A word, name, symbol or device which is used in trade with goods to indicate the source of the goods and to distinguish them from the goods of others. Trademarks used in interstate or foreign commerce may be registered with the U.S. Patent and Trademark Office.

3. Buildings and Building Improvements

<u>Buildings</u> are permanent structures erected above ground, together with fixtures attached to and forming a permanent part of the building, for the purpose of sheltering persons or personal property. The cost of buildings includes all labor, materials, and professional services required to construct the building, and any other costs to put the building into its intended use.

<u>Building improvements</u> are major repairs, renovations, or additions to a building that increase the future service potential of the building and benefit future periods. The buildings and the improvements become one and inseparable. Examples of building improvements include major repairs, renovations, or additions such as addition of a new wing or a new air conditioning system.

4. Leasehold Improvements

Leasehold Improvements are improvements made by the lessee to leased property such as land and buildings. The lessee has the right to use such facilities and improvements during the life of the lease, but the improvements made to the property would revert to the lessor at the expiration of the lease. For this reason, the useful life of the leasehold improvement cannot be longer than the remaining lease term. The useful life of the leasehold improvement would be the lesser of 20 years (if a depreciable land improvement), 40 years (if a building improvement), or the remaining lease term. These improvements to leased property are treated as separate capital assets and are capitalized and depreciated if they are above the threshold for capitalization for the particular type of leased capital asset. Some examples of leasehold improvements would be new buildings or structures built on leased land and attachments or improvements made to existing leased buildings or structures.

5. Land and Non-Depreciable Land Improvements

Land is an inexhaustible asset that has an unlimited life and therefore is not depreciated.

Non-depreciable land improvements are those betterments, improvements, and site preparations that ready land for its intended use. Like the land itself, these improvements are inexhaustible and therefore not depreciated. Some examples of non-depreciable land improvements would be excavation, filling, grading, demolition of buildings existing on a parcel of land that was purchased with the intent of demolishing those buildings in order to prepare the land for its intended use, and removal or relocation of other property (telephone or power lines).

6. Depreciable Land Improvements

Depreciable land improvements are defined as improvements made to land that have determinable estimated useful lives and deteriorate with use or passage of time. These improvements are built or installed to enhance or facilitate the use of the land for a particular purpose. Depreciable land improvements may include walking paths and trails, fences and gates, landscaping, sprinkler systems, fountains, and beaches. These are unlike non-depreciable land improvements and land since the useful life of the improvement is determinable.

7. Infrastructure

Infrastructure is defined as long-lived capital assets associated with governmental activities that normally are stationary in nature and can be preserved for a significantly greater number of years than most capital assets. Examples include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems. Although these assets are long-lived, useful lives are assigned to these assets and they are depreciated.

8. Historical Treasures & Works of Art

Historical treasures & works of art are items which are considered inexhaustible and held for public exhibition, educational purposes, or research in enhancement of public service instead of financial gain. Examples are paintings, sculptures, photography, maps, manuscripts, musical instruments, recordings, film, furnishings, artifacts, tools, weapons, and other memorabilia. Generally, collections of historical treasures & works of art will be considered inexhaustible, and would therefore not be depreciated. However, special rules apply for the capitalization of these assets. If a collection was capitalized as of June 30, 1999, the collection must continue to be capitalized, along with all additions to the collection. However, if the collection was not capitalized as of June 30, 1999, do not capitalize the collection.

IV. Classes of capital assets and their useful lives are as follows:

Description of Asset and Examples	Useful Life
Movable Property	
1. High mileage automobiles Examples: state police cars	3
2. Hogs, breeding	3
3. Over-the-road tractor units	4
4. Medical equipment	5
5. Computers & peripheral equipment Examples: hard drives, printers, monitors, keyboards, disc drives, scanners	5
6. Automobiles	5
7. Light general purpose trucks (< 13,000 lbs.)	5
8. Sheep & goats, breeding	5
9. Office machinery & equipment other than computers: Examples: typewriters, calculators, adding machines, copiers and other duplicating equipment	6
10. Construction equipment	6
11. Heavy general purpose trucks (13,000 lbs. or more)	6
12. Airplanes	6
13. Radio & television broadcasting equipment (excluding towers, see infrastructure)	6
14. Trailers and trailer mounted containers	6

15. Dairy cattle, breeding	7
16. Buses	9
17. Office furniture & fixtures Examples: desks, file cabinets, safes	10
18. Agricultural assets Examples: agricultural machinery & equipment, grain bins, and fences used for agricultural production	10
19. Assets used in research and experimentation	10
20. Printing and publishing equipment	10
21. Recreation assets used in the provision of entertainment services for a fee such as bowling alleys, billiards and pool halls, theaters, concert halls, and miniature golf courses.	10
22. Telephone station equipment Examples: telephones, booths, teletypewriters, and private exchanges	10
23. Horses, breeding or work	10
24. Horses, not breeding or work	12
25. Telephone central office equipment Examples: central office switchboards and related equipment	18
Buildings and Improvements	
Buildings and improvements other than those listed below	40
Farm buildings other than single purpose structures Examples: Houses, barns, garages, warehouses	25
Single purpose agricultural or horticultural structures Examples: any building or enclosure used specifically for housing, raising, and feeding a particular type of livestock and it’s produce and necessary equipment; greenhouses	15
Service station buildings and related land improvements	20

Depreciable Land Improvements	
Land improvements that are depreciable & other improvements other than buildings Examples: sidewalks, paths and trails, sprinkler systems, fences & gates, landscaping, fountains, and beaches that are not considered infrastructure (see infrastructure examples listed below)	20
Infrastructure Examples: interstates, highways, roads, bridges, tunnels, sidewalks, curbs, gutters, street signage, street lamps, traffic signals, drainage systems, water and sewer systems, lighting systems, railroad tracks, trestles, canals, waterways, spillways, locks, dams, levees, seawalls, boat ramps, boat docks, piers, wharfs, boardwalks, radio or television towers, airport runways and taxiways	40

*Note - This table is only a list of some of the more common and probable assets that are in your possession. If there are any assets not on this list that may be required to be capitalized and depreciated, refer to IRS Publication 946 - Appendix B "Table of Class Lives and Recovery Periods" for further listing of assets.

V. Method of depreciation:

For simplicity and consistency, the straight-line depreciation method (cost divided by useful life) will be used for depreciation of all depreciable capital assets. In addition, it will be assumed that the capital assets will have no salvage value. A full year of depreciation will be taken in the year assets are placed in service. Regardless of the actual date an asset is placed into service, the asset is treated as being placed into service at the beginning of the fiscal year, allowing a full year's depreciation in the year of acquisition. In the year of disposal, any remaining depreciation will be taken if the asset is not fully depreciated at the time of disposal.

VI. Exception to Statewide Capitalization and Depreciation Policy:

LSU Health Sciences Centers at New Orleans and Shreveport, and LSU Health Care Services Division are allowed to use the medical industry capitalization and depreciation provisions for use in financial statement preparation and for federal cost recovery reporting. The LSU system should disclose these capitalization and depreciation policies in their Annual Financial Reports as part of their significant accounting policies. Additional information on the capitalization policy of LSU Health Sciences Centers at New Orleans and Shreveport, and LSU Health Care Services Division can be found at http://www.lsuhospitals.org/policies/2500-fiscal%20services.html.