

## **WEST CHICAGO PUBLIC LIBRARY DISTRICT**

### **FIXED ASSET/CAPITALIZATION POLICY**

Administration and execution of this policy are the responsibility of the Treasurer and Chief Financial Officer, and, by designation, the Administrative Librarian acting under the authority of the Library Board of Trustees.

The Library will maintain an inventory of fixed assets and a record of capital expenditures.

The Library will maintain an inventory for external financial statement purposes of all fixed assets. Fixed assets are property, plant, furniture and equipment with an initial acquisition cost of \$5,000 or more per item. Initial cost is the cash outlay, or its equivalent, made to acquire the asset and put it in operating condition.

Fixed assets will be inventoried, using the historical cost of the asset. A record which includes item name, description, inventory ID number, location, manufacturer, vendor, historical cost, replacement cost, serial number and estimated replacement date, will be maintained.

Capital expenditures do not include (1) ordinary repairs that do not increase the value or extend the life of the asset; (2) routine operating costs such as annual maintenance contracts.

Retirement procedure: A retirement record will be maintained as items are withdrawn or retired.

Review procedure: The inventory should be reviewed on an annual basis.

#### **Asset Classification**

Fixed assets should be categorized into the following:

- land;
- land improvements and infrastructure;
- buildings;
- equipment

#### **General Policy for Capitalization**

Fixed assets should be capitalized as follows:

- all land acquisitions;
- all building acquisitions;
- building renovations and improvements projects costing more than \$100,000;
- land improvements and infrastructure projects costing more than \$100,000;
- equipment costing more than \$5,000 with a useful life beyond a single reporting period (generally one year);

## **Land**

The recorded cost of land includes (1) the contract price; (2) the costs of closing the transaction and obtaining title, including commissions, options, legal fees, title search, insurance, and past due taxes; (3) the costs of surveys; and (4) the cost of preparing the land for its particular use such as clearing and grading. If the land is purchased for the purpose of constructing a building, all costs incurred up to the excavation for the new building should be considered land costs. Removal of an old building, clearing, grading and filling are considered land costs because they are necessary to get the land in condition for its intended purpose. Any proceeds obtained in the process of getting the land ready for its intended use, such as salvage receipts on the demolition of the old building or the sale of cleared timber, are treated as reductions in the price of the land. Capitalization of land costs include, but are not limited to, the following:

- original contract price;
- brokers' commissions;
- legal fees for examining and recording title;
- cost of title guarantee insurance policies;
- cost of real estate surveys;
- cost of an option when it is exercised;
- special paving assessments;
- cost of excavation, grading or filling of land and razing of an old building;
- cost of cancellation of unexpired lease; and
- payment of noncurrent taxes accrued on the land at date of purchase, if payable by purchaser.

## **Buildings**

Capitalization of building costs include, but are not limited to, the following:

- original contract price of cost of construction;
- expenses incurred in remodeling, reconditioning, or altering a purchased building to make it available for the purpose for which it was acquired;
- expenses incurred for the preparation of plans, specifications, blueprints, etc.;
- cost of building permits;
- payment of noncurrent taxes accrued on the building at date of purchase, if payable by purchaser;
- architects' and engineers' fees for design and supervision; and
- costs of temporary buildings used during the construction period.

Each building or addition of square footage to an existing building acquired or constructed is divided into ten major building components. The components are as follows:

1. General construction;
2. Site preparation (this component is classified as land on the financial statements);
3. Roof and drainage;

4. Interior construction;
5. Plumbing;
6. Heating, ventilation, and air conditioning;
7. Electrical;
8. Fire protection;
9. Elevators; and
10. Miscellaneous.

The total cost of the building or additional square footage is then allocated among the 10 major building components. For projects such as building construction, include in the fixed asset of the building, the cost of professional fees (architect and engineering), permits and other expenditures necessary to place the asset in its intended location and condition for use.

Furthermore, the cost of interest incurred during building construction should be capitalized. The capitalization period begins when the following three considerations are present:

1. Expenditures for the capital asset have been made;
2. Activities necessary to get the capital asset ready for its intended use are in progress; and
3. Interest costs are being incurred.

The amount capitalized should be an allocation of the interest cost incurred during the period required to complete the asset. The interest rate for capitalization purposes is to be based on the rates on The Library's outstanding borrowings. If a specific new borrowing can be identified with the asset, the rate on that borrowing should be used as the basis for allocating the interest cost for the asset. A weighted average of the rates on other borrowings is to be applied to expenditures not covered by specific new borrowings.

### **Building Renovations/Rehabilitation**

A building renovation is defined as enhancements made to a previously existing building component. Any renovation to a building must, at a minimum, meet the following criteria to qualify as a fixed asset:

1. The total project cost must be more than \$100,000; and
2. The renovation must extend the useful life or capacity of the asset.

## **Building Improvements**

An improvement to a building is defined as adding a new component where one did not previously exist. The improvement must cost more than \$100,000 and have an initial useful life extending beyond a single reporting period (generally one-year).

## **Land Improvements and Infrastructure**

Land improvements include items 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. Land improvements can be further categorized as non-exhaustible and exhaustible. Expenditures for land improvements that do not deteriorate with use or passage of time are additions to the cost of land and are generally not exhaustible, and therefore not depreciable.

Infrastructure assets are defined as long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets. Examples of infrastructure assets include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems. Improvements to infrastructure or land improvements which extend the useful life or capacity of the asset and meet capitalization thresholds will be capitalized as a separate asset/component and depreciated over its estimated useful life.

## **Equipment and 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 Library 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; and
- The present value of the 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.

Capitalization of equipment costs include but are not limited to, the following:

- original contract or invoice cost;
- freight, import duties, handling and storage costs;
- specific in-transit insurance charges;
- sales, use and other taxes imposed on the purchase;
- costs of preparation of foundations and other costs in connection with making a proper site for the assets;
- installation charges; and
- costs for reconditioning used equipment to make it usable for the purpose it was purchased.

Improvements to existing equipment assets which extend the useful life or capacity of the asset and meet capitalization thresholds will be capitalized as a separate asset/component and depreciated over its estimated useful life.

### **Capitalization of Computer Software Costs**

Computer software costing more than \$5,000 with a useful life beyond a single reporting period (generally one-year) should be capitalized. For software developed or obtained for internal use, The Library will follow the guidance in Statement of Position SOP 98-1 as follows:

The software must be acquired, internally developed, or modified solely to meet internal needs and there must not be a substantive plan to market the software externally to other organizations. Software development generally involves three phases. These phases and their characteristics are as follows:

- Preliminary project phase - when conceptual formulation of alternatives, the evaluation of alternatives, determination of existence of needed technologies and final selection of alternatives is made;
- Application development phase - Design of chosen path including software configuration and software interfaces, coding, installation of computer hardware and testing, including parallel processing phase; and
- Post-implementation/operation phase - training and application maintenance activities.

Costs associated with the preliminary project and the post-implementation/operating phases should be expensed as incurred. Internal and external costs associated with the application development phase should be capitalized. Costs to develop or obtain software that allows for access or conversion of old data by new information systems should also be capitalized. General and administrative costs and overhead expenditures associated with software development should not be capitalized as costs of internal use software.

Upgrades and enhancements are defined as modifications to existing internal-use software that result in the ability for the software to perform tasks that it was previously incapable of performing. In order for costs of specified updates and enhancements to internal-use computer software to be capitalized, it must be probable that those expenditures will result in additional functionality.

### **Depreciation**

Depreciation is the process of allocating the cost of tangible property over a period of time, rather than deducting 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 will equal original cost less the salvage value.

### **Information Needed to Calculate Depreciation**

To calculate depreciation on a fixed asset the following five factors must be known:

1. the date the asset was placed in service;
2. the asset's cost or acquisition value;
3. the asset's salvage value;
4. the asset's estimated useful life, and
5. the depreciation method.

### **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 acquired. Eligible fixed assets should be depreciated over their estimated useful lives.

### **Depreciation Method**

The Library has established the straight-line methodology for depreciating all fixed assets. Depreciation will begin in the month the asset is placed in service. Under the straight-line depreciation method the basis of the asset is written off evenly over the useful life of the asset. The amount of annual depreciation is determined by dividing an asset's cost reduced by the salvage value, if any, by its estimated life. The total amount depreciated can never exceed the asset's historic cost less salvage value. At the end of the asset's estimated life, the salvage value will remain.

### **Asset Retirement**

Retiring an entire asset or building component – remove the entire asset and related accumulated depreciation from the fixed asset file. Any undepreciated balance will be reported as a disposal expense net of any value received.

Generally with a building rehabilitation or renovation only a section of the asset is retired (partial retirement) for the piece of the asset being renovated. To determine the value of the asset being renovated, The Library's methodology is based on the current costs of the renovation and discounting back to the date of the asset being renovated. An escalation table (discounting rates) is used which reflects annual escalation (de-escalation) factors developed using industry data and other relevant information.

The process that will be employed for determining the value of the component/asset being retired/renovated is as follows:

1. Establish amount being capitalized (by component) and the year;
2. Identify the oldest component for that asset/building;
3. Determine the de-escalation factor and multiply the amount being capitalized by 100 and divide by the factor. This provides the dollar value of the component to be retired; and

4. Reduce the existing asset by this dollar amount or if this amount is greater than the dollar amount of the existing asset component – determine the next “layer” for that asset component.

Approved by Board of Library Trustees: November 28, 2005

Approved by Board of Library Trustees: September 22, 2008