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ALAN M. ARAKAWA
Mayor

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OFFICE OF THE MAYOR

DANILO F. AGSALOG
Director

MARK R. WALKER
Deputy Director

COUNTY OF MAUI
DEPARTMENT OF FINANCE
200 S. HIGH STREET
WAILUKU, MAUI, HAWAII 96793

September 21, 2017

Honorable Alan M. Arakawa
Mayor, County of Maui
200 South High Street
Wailuku, Hawaii 96793

For Transmittal to:

Honorable Riki Hokama, Chair
Budget and Finance Committee
200 South High Street
Wailuku, Hawaii 96793

APPROVED FOR TRANSMITTAL
9/21/17
Mayor Date

Dear Chair Hokama,

SUBJECT: AMENDING FISCAL YEAR 2018 BUDGET: DEPARTMENT OF ENVIRONMENTAL MANAGEMENT (WASTEWATER ADMINISTRATION PROGRAM – SEWER FUND, WASTEWATER OPERATIONS PROGRAM – SEWER FUND) (BF-74)

We are in receipt of your letter dated September 18, 2017 requesting additional information regarding the Department of Environmental Management's proposed budget amendment for the replacement of three switchgears at the Lahaina Wastewater Reclamation Facility. Please find our responses to your requests below.

1. Provide a copy of the draft capital asset policy.

   Response: Attached please find a copy of the draft "Capital Asset Accounting Manual" for your information and use.

2. Explain the rationale for replacement equipment to be appropriated in category B (operations) instead of category C (equipment) or as a capital improvement project. Identify the criteria to make such a determination.

Response: The rationale for placing the three switchgears in category B versus category C is based on Generally Accepted Accounting Practices (GAAP) and more specifically GASB 34 and are as follows:

- *The switchgears are part of a larger sewer system. A sewer system is classified as infrastructure which means that normally it is an asset that can be preserved for a significantly greater number of years than most capital assets. Other examples of assets that would fall into the infrastructure classification are; roads, bridges, tunnels, water &drainage systems and lighting systems.*

- *Repairs versus Improvements or category B versus category C. Generally, expenditures that increase the economic value of the asset, increase the useful life beyond the original useful life, or increase the productive capability (use, scope, etc.) should be capitalized (category C). On the other hand, expenditures made to restore or maintain an asset at its original condition are expensed and not capitalized (category B).*

  Given the above, it is the judgment of both the Budget Office and the Department of Finance that the subject switchgears should be categorized as repairs and maintenance and accounted for in category B.

3. Was $1,659,979 transferred from the Wastewater Administration Program – Sewer Fund, Category B to the Countywide Sewer Capital Improvement Reserve Fund for Fiscal Year 2018? If so, when was the transfer made?

   Response: Yes, $1,659,979 was transferred from Wastewater Administration Program – Sewer Fund to the Countywide Sewer Capital Improvement Reserve Fund via journal entry on July 31, 2017.

Thank you for the opportunity to respond to your query. Should you require any additional information please feel free to contact me at extension 7475. Thank you.

Sincerely,

for DANILO F. AGSALOG
DIRECTOR OF FINANCE

cc: Lynn Araki-Regan, Budget Director
Steve Tesoro, Accounting System Administrator

COUNTY OF MAUI

DEPARTMENT OF FINANCE
ACCOUNTS DIVISION

CAPITAL ASSET ACCOUNTING MANUAL

Effective Date
Revised as of Date

Table of Contents

Chapter 1. Introduction

Overview

Purpose

The purpose of the County of Maui's capital asset accounting manual is to provide auditable information for the Comprehensive Annual Financial Report (CAFR), and to help ensure that property, plant, and equipment are acquired, controlled, and disposed of in the best interests of the County. This manual applies to all departments and agencies of the County of Maui. It does not supersede the policies and procedures set forth in the County of Maui Charter, Maui County Code, and other state or federal laws and regulations.

Responsibility

The Accounts Division under the Department of Finance is responsible for maintaining and updating the Fixed Asset (FA) and General Ledger (G/L) records of the County's Integrated Financial Accounting System (IFAS). This includes inputting all fixed assets acquired and disposed by the departments within the fiscal year and recording the capital asset balances.

Random Reviews

The Department of Finance may conduct random reviews to ensure compliance with the established Capital Asset Accounting Manual (CAAM). The Department of Finance will coordinate all review activities with the department/agency heads or authorized custodian as not to disrupt the routine of the department. The review will determine the adequacy or effectiveness of the County's financial system by evaluating the reliability and integrity of asset information and the means used to identify value, classify and record associated information. It will further identify the department's compliance with the policies and procedures contained on this manual.

Accuracy of Capital Asset Presentation

Accurate historical asset values and depreciation information are imperative to accurate financial reporting, and this accuracy relies on the following:

- Funding amount presented as historical cost (GAAP) should be accurate and supported by appropriate source documents. Refer to xx.
- Acquisition date must be accurate. Assets should be added to the FA system during the fiscal year acquired. Additionally, reasonable estimates of useful life and salvage value must be made and entered into the FA record. Refer to xx.

- Periodic review and update of the methodology for assigning asset useful lives. Consideration of actual use patterns for different types of assets and take into account the actual length of time the different assets were used over time in the past. This is to ensure that the useful life closely mirrors the actual life of the asset. Refer to xx.
- Periodic review and update of the methodology for estimating salvage value based on the asset type, its obsolescence and degree of usefulness at disposal and the nature of the disposal process. The estimate of useful life should also be a factor in estimating salvage value. Salvage value is a field in FA system. Refer to xx.
- When an asset has been disposed, the book value must be removed from the appropriate capital asset General Ledger balances. Departments should periodically review capital asset information contained in the FA system to ensure that assets that are no longer under the control of the department have been properly disposed in FA system. Disposal date must be accurate, as should the other disposal-related information. Disposals should be recorded in FA system during the fiscal year in which an asset was actually disposed. Refer to xx.

Legal Requirements on Real Property Acquisition and Donations

Real Property Acquisition

Maui County Code (MCC), Chapter 3.44 defines "real property" as land and structures or fixtures permanently attached thereto. MCC, Chapter 3.44 provides laws and regulations for the acquisition and disposition of real property. The department acquiring a real property must ensure that the laws and regulations provided on this code are being complied with.

Any acquisition of real property by the County of Maui, whether by agreement, purchase, exchange, gift, devise, eminent domain, or otherwise, shall be accomplished in accordance with the provisions of MCC, Chapter 3.44. If a real property has a purchase price that exceeds $100,000, the County Council must authorize the acquisition by the passage of a resolution, approved by a majority of its members[1].

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[1] Provided that, Council approval is not required for the purchase of housing units for less than $150,000 pursuant to repurchase options and other buy-back provisions granted to the County as follows: 1. Deed restriction in a County housing project was developed (secured final subdivision approval or certificate of occupancy) prior to January 1, 1999; and 2. Agreement that was executed by and between the County and the developer of a housing project prior to January 1, 1999 under a County housing program.

Real Property Donation

Prior to acceptance of gifts or donated real property or any interest in real property, a resolution must be passed and approved by a majority of the County council's members[2].

Legal Requirements on Disposal, Sale, Exchange, and Grant of Personal Properties

Policy and Procedures on Disposal

Chapter 2.72 of the Maui County Code (MCC) provides laws and regulations for disposing County's personal properties. Personal property is defined in the code as "all property other than real property or fixtures permanently attached thereto."

The following procedures must be followed by all departments disposal any County's real personal properties:

1. The department must submit to the Accounts Division a Request to Dispose of County Property and Removal from Inventory Forms when a department having the control of personal property needs to sell, exchange, grant, or otherwise dispose a personal property. The Request to Dispose of County Property form must be signed by the department/agency head and notarized.

2. Upon receipt of the forms, the Finance Director will review the forms and supporting documents for approval or disapproval, or may authorize another method of disposal. If the Finance Director finds that it is advantageous to the County to sell the personal property, an estimate of its fair market value will be provided, set an upset price, and offer it for sale. The department may be required to estimate the fair market value and cost of sale of the personal property being disposed. If an estimate of fair market value is required and the department director/head finds that it is not advantageous to obtain an independent or expert appraisal, the estimate must be based on an investigation that it is reasonable under the circumstances. Factors considered in making the estimate must be in writing, along with the estimate.

3. Certified statements must be submitted by the department/agency disposing the personal property, to the Finance Director, Attn: Accounts Division immediately after the disposal of personal property.

4. An annual report must be submitted by the Finance Director to the County Council, which contains a detailed statement of the

[2] See MCC, Chapter 3.44.015.

Finance Director's action with reference to the disposition of any personal property.

Other Disposal

Under the provisions of MCC Chapter 2.72.056, the Finance Director may authorize the disposal of personal property that is worthless, including personal property with an estimated fair market value that is less than the estimated cost of selling it.

Policy and Procedures on Sale

The Finance Director is authorized to offer personal property for sale by a public auction or call for sealed bids, unless sale by public auction or call for sealed bids is waived by a veto of at least six Council members, in which case the sale of personal property without public auction or without calling for sealed bids is authorized.

All monies received from the sale of any property will be deposited into the appropriate fund as determined by the Finance Director. The records of all proceedings of the disposition of any personal property must be kept in the office of the Finance Director.

Policy and Procedures on Exchange

The Finance Director may authorize the trade-in of personal property when procuring goods. Authorization is granted by the Council Chair for legislative branch procurements. Personal property offered for trade-in must be identified in the procurement documents.

Policy and Procedures on Grant

The Finance Director may authorize the grant of personal property that the County no longer uses, to a non-profit organization, school, or government entity. The personal property must be granted pursuant to a grant agreement contract recommended by the department or agency that has custody or control of the personal property, subject to approval by the Mayor for executive branch or Council Chair for legislative branch. The department/agency must submit the information and documents pertaining to the grant to the Finance Director. Information on the grant must also be included in the annual report submitted by the Finance Director to the County Council.

Internal Control

General

The Finance Department is responsible for the implementation and administration of this Manual.

Department heads are responsible for maintaining an adequate system of internal controls within the department. Such system includes authorization for making vendor payments and other expenditures of County funds and includes granting security access to the County's IFAS.

Departments should establish adequate and cost beneficial internal control systems to ensure that:

- Capital assets are acquired for use in further the department's programs and missions;
- Those assets that are within the required capitalizable limits are recorded in IFAS;
- Proper stewardship and control over assets is carried out, including periodic inventories;
- Financial records reflect proper capital asset balances;
- Assets are reasonably protected from theft;
- Internal procedures are documented in writing; and
- Proper segregation of duties is maintained.

Chapter 2. Definitions

Accumulated Depreciation	The total depreciation expense aggregated since a capital asset was acquired or placed in service through the current reporting period.
Ancillary Costs	Costs, in addition to purchase of construction costs, related to placing a capital asset into its intended use or state of operation. Normally, ancillary costs are to be included in the capitalized cost of a capital asset.
Acquisition Date	The date the County took ownership of the asset.
Book Value	The total cost of a capital asset less than the accumulated depreciation recorded to date.
Buildings	A building is a structure that is permanently attached to the land, has a roof, is partially or completely enclosed by walls, and is not intended to be transportable or moveable. Certain buildings or structures that are an ancillary part of infrastructure networks, such as rest area facilities and pumping stations should be reported as infrastructure rather than as buildings.
Building Improvements	Capitalized costs that materially extend the useful life of a building or increase the value of a building, or both, beyond one year. Building improvements should not include maintenance and repairs done in the normal course of business.
Capital Assets	Major assets that are used in operations and have initial useful lives in excess of one year. Capital assets with an original cost of greater than or equal to the County's capitalization threshold of $5,000 for equipment, $100,000 for improvements to existing land, buildings, and infrastructure or $250,000 for new construction and acquisition, will be capitalized for financial accounting purposes. Examples include, among other things, land, land improvements, buildings, building improvements, furniture and fixtures, vehicles, machinery, equipment, infrastructure, and all other tangible or intangible assets.
Capital Outlay	Outflow of funds (expenditures) which result in the acquisition of or addition to capital assets.
Capitalization Threshold	The dollar value at which a government elects to capitalize tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period.

Capitalize

To record a cost as a long-term asset. The amount recorded is the costs to acquire or construct the asset, plus all costs necessary to get the asset ready for its intended use (see ancillary costs).

Construction Work in Progress

Construction work in progress reflects the economic construction activity status of buildings and other structures, infrastructure (highways, pipelines, etc.), additions, alterations, reconstruction, and installation, which are substantially incomplete.

Depreciation

In accounting terms, 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 amount charged for depreciation in each accounting period (accumulated depreciation) will equal original cost less salvage value. Good accounting and financial management practices require that a government entity take both the cost expiration and the declining value of an asset into consideration. The cost expiration of a government entity's assets must be recognized if the cost of providing services is to be realistically reported. Also, the decline in the value of those assets must be considered if the government entity's net assets are to be stated correctly.

Depreciation Method

The method used to calculate the allocation (depreciation) of the cost of a capital asset over its estimated useful life. The most commonly use method is straight-line depreciation, which allocates the cost evenly over the life of the asset. Other methods are double-declining balance, sum-of-the-year's-digits, and activity-based depreciation.

Fair Market Value

The estimated value of the asset for which it would be exchanged between a willing buyer and seller when neither is forced into the exchange. In addition, both parties should acknowledge of all facts and consider it an equitable exchange. This is generally used in place of historical cost in a donated asset situation.

Furniture and Equipment

Include fixed or movable tangible assets to be used for operations, the benefits of which extend beyond one year from date of receipt and when placed into service. Examples are machinery, computers, printers, radios, and vehicles, etc.

Historical Cost

The value placed on the asset at the time of acquisition, including ancillary costs (value of trade-ins, shipping costs, installation costs, etc.)

Infrastructure	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 assets are often linear and normally stationary in nature. Examples include roads, bridges, tunnels, drainage systems, water systems, and dams. Infrastructure assets do not include buildings, driveways, parking lots or any other examples given above that are incidental to property or access to the property.
Infrastructure Improvements	Capital costs that materially extend the useful life or increase the value of the infrastructure, or both. Infrastructure improvements should be capitalized and recorded as an addition of value to the infrastructure if the improvement or addition of value is at the capitalization threshold and increases the life or capacity of the asset.
Intangible Asset	Long-term assets that have no physical substance and are used in operations to produce products or services. Intangible asset cost must be systematically allocated to expenses over their useful life. Capitalized computer software is considered depreciable.
Land	Land is the surface or crust of the earth, which can be used to support structures, and may be used to grow crops, grass, shrubs, and trees. Land is characterized as having an unlimited life (indefinite).
Land Improvements	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. Land improvements can be further categorized as inexhaustible and exhaustible. ***Inexhaustible*** – expenditures for improvements that do not require maintenance or replacement, expenditures to bring land into condition to commence erection of structures, expenditures for improvements not identified with structures, and 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. ***Exhaustible*** – other improvements that are part of a site, such as parking lots, landscaping and fencing are usually exhaustible and are therefore depreciable. Depreciation of site improvements is necessary if the improvement is exhaustible.

Preservation Costs — Costs that are infrastructure-related outlays that extend the useful life of an asset beyond its original estimated useful life, but do not increase the capacity or efficiency of the asset. Preservation costs should be expended under the modified approach and capitalized under the deprecation approach (improvements).

Salvage Value — The subsequent value of the asset at the end of its useful life.

Useful Life — The period of time the asset will be of service to the County.

Chapter 3. Asset Acquisition

Acquisition Method

Overview

The purpose of this section is to establish the policies by which departments account for asset acquisitions. There are various methods by which assets can be acquired. The asset acquisition method determines the basis for valuing the asset.

Asset items that meet the criteria for inclusion in FA system can be acquired in the following ways:

- New purchases
- Donations/Exchanges
- Transfers from other County departments
- Federal or state grants
- Internal/external construction
- Lease purchases
- Trade-ins, and
- Forfeiture or condemnation.

Policies

In acquiring assets, departments must adhere to the laws and regulations in the County's MCC, Chapter 3.44, the procurement law outlined in the Hawaii Revised Statutes Chapter 103D and detailed in the Administrative Rules, the County's procurement process published by the Division of Purchasing, Department of Finance, and policies and procedures outlined on this Capital Asset Manual. Further information on the procurement process can be accessible via the County's intranet, Purchasing Policies and Procedures .

Procedures

Timing of Recordation

All recordable assets, except constructed assets, should be recorded in IFAS as soon as possible after title passes. **Except in unusual circumstances, assets should be posted within *30* days after receipt and acceptance of the asset. Asset acquisitions should be posted to FA system in the fiscal year the asset was acquired. Similarly, asset disposals should be posted to FA system in the fiscal year the disposal occurred.**

Equipment Purchases

Title is considered to pass at the date the equipment is received. Similarly for donated assets, title is considered to pass at market value when the asset is available for the department's use and when the department assumes responsibility for maintaining the asset. For further information, see xx.

Constructed Assets

Constructed assets are transferred from the Construction Work in Progress (CWIP) account to the related building, infrastructure, or equipment accounts when they become operational. Constructed buildings, for example, are assumed to be operational when an authorization to occupy the building is issued, regardless of whether or not final payments have been made on all the construction contracts. For further information, see xx.

New Purchases

New purchases must be recorded in the FA system if the asset meets the capitalization criteria. For further information, see xx.

Donations

GASB Statement No. 33, *Accounting and Financial Reporting for Non-Exchange* Transactions, defines a donation as a voluntary non-exchange transaction entered into willingly by two or more parties. Both parties may be governments, such as the federal, state, county or one party may be a non-governmental entity.

PLEASE NOTE: A voluntary contribution of resources between County departments is not considered as a donation but as a capital transfer. See xx below.

The County of Maui's assets are recorded at historical cost or estimated historical cost, if purchased on constructed. Donated capital assets are recorded at estimated fair value at the date of acquisition, using a reasonable market study. The method used to appraise the value computed for donations should be based on a reasonable assessment. This method must be fully documented and maintained on file to support the value.

Transfers Between County Departments

Governmental Accounting Standards Board Statement No. 48, *Sale and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, requires that an asset transfer between County departments be treated as a related party transaction. This requires the asset be recorded at the book value of the transferring entity. The easiest way to accomplish this task is to record the asset at the original historical cost and acquisition date of the disbursing department.

Federal and State Grants

These are assets (usually equipment) acquired from Federal and State grants. The department managing the grant program is responsible for inspecting, tagging, and reporting the physical data of the acquired property.

Lease Purchases

Assets may be lease-purchased through installment purchases (an agreement in which title passes to the department) or through lease financing arrangements (an agreement in which title may or may not pass). Assets acquired through installment purchases should be entered into FA system. Assets that are leased should be entered into the xx, refer to xx.

Trade-Ins

Departments may acquire assets using a trade-in. For information on determining the value of trade-in-assets, see xx.

Forfeiture or Condemnation

On occasion, the County may take title to property forfeited by a taxpayer in lieu of payment of taxes. For information on determining the value of assets obtained by forfeiture, see xx.

Acquisition Valuation

Overview

The purpose of this section is to provide guidance in establishing accurate costs to be recorded for asset acquisitions. Once an asset has been acquired, under an approved method, it must be recorded at an appropriate value in order to properly control, management, maintain and report on it.

Policy and Procedures

General

It is the responsibility of each County department to ensure that all asset acquisitions are recorded at the asset's proper value. Documentation must be maintained in support of each asset value assigned.

Each fiscal year, the CAFR of the County is prepared by the Accounts Division and audited by an independent auditor. The County's FA system is the source for much of the capital asset information that is included in the CAFR. Detailed information on the Infrastructure is tracked in a comprehensive spreadsheet. Accordingly, it is important that the capital assets of the County are properly valued and accurately recorded in the County's IFAS.

Accounting information should be based on source documents. The voucher that represents payment to the vendor or a series of invoices supporting payment to a contractor are the primary forms of source documentation. The underlying sources documentation "vouches for" or confirms what an asset actually costs and provides an auditable means of verifying historical costs, which is required for compliance with GAAP. To provide an audit trail, copies of relevant source documents must be retained.

Acquisition Cost

Capital assets are recorded and reported at their historical costs. Historical cost includes the vendor's invoice (less the value of any trade-in), 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 basic cost or value to be recorded for each type of acquired asset is shown below. Add any appropriate associated cost detailed above to the basic value.

PLEASE NOTE: The book value of assets recorded at historical costs should never be increased to reflect appraised value, insurance value, replacement cost, etc.

- **Purchased assets** – recorded at invoice or contract price plus all other ancillary costs expenditures charged to the appropriate IFAS G/L account. *Software and other intangible assets should be recorded at cost or estimated cost as specified in* xx.

  Ensure that the acquisition cost reported on the xx, does not represent a partial payment. Procedures should be developed to that the listing of capital assets match with records of outstanding purchase orders for capital asset item.

  Recognize acquisition cost based on individual unit prices. Assets should not be grouped. For example, in acquiring equipment, if three air conditioning (a/c) units are required at $3,500 each, this would not be a capital asset of $10,500 consisting of 3 a/c units. Instead, it would be 3 separate acquisitions of $3,500. Each a/c unit would be entered into FA system if the cost per unit is S5,000 or above, as a separate fixed asset ID item.

- **Donated Assets –** Recorded at the fair market value.

- **Transfer from Other County Departments** – Should be treated as a transfer between related departments/agencies at its original historical cost and acquisition date.

- **Federal and State Grant Property** – The acquisition value of property is the current purchase price of the item, include any costs associated with making the asset operational.

- **Internal/External Construction** – All costs directly related to the construction and charged to related IFAS or G/L account (i.e. the value of labor, materials and other costs associated with the construction and installation of the item and/or all contract related costs). Such charges should include all associated costs plus the following:

    - Insurance premiums
    - Interest expense[3] incurred during construction
    - Engineering, architectural and other fees
    - Reasonably allocated overhead for heavy equipment used in construction, and
    - Adjustments resulting from final payments on construction contracts that were recorded as assets at the time they became operational.

<u>**NOTE:**</u> Amounts that are determined to be capitalizable should be recorded in CWIP quarterly until the project is complete. Upon completion, the total capitalizable costs should be transferred to the appropriate capital asset account. See Chapter 6.

- **Lease Purchase** – For assets acquired using installment purchases, record at the present value of all installment payments at the rate of interest implicit in the transaction.

- **Trade-ins** – The cost of the new asset is the sum of the cash expended plus the cash equivalent of the value of old asset given in exchange. Value placed on the old asset may be book value, trade-in allowance or estimated fair value at the time of trade-in.

- **Forfeiture** – The lesser of 1) the asset's fair market value at the date of forfeiture or 2) the amount owed by the borrower together with costs incurred by the County to obtain the forfeiture and to put the asset into service.

[3] The costs of capital assets for ***governmental activities*** do not include capitalized interest. Interest, however, is capitalized on assets that are constructed for an agency's enterprise fund or otherwise produced for an enterprise fund's own use (including assets constructed or produced for the enterprise by others for which deposits or progress payments have been made), and assets intended for sale or lease that are constructed or otherwise produced as discrete projects (i.e. real estate developments).

- Software and other intangible assets should be recorded at cost or estimated cost as specified in xx.

In addition to the presentation of capital assets valued at historical cost, the CAFR includes accumulated depreciation and depreciation expense for these assets. It is also important to accurately record the acquisition date and ensure that a reasonable estimated useful life is assigned and a reasonably estimated salvage value (if any) is recorded. Useful life for an asset is determined based on the appropriate asset type. Refer to xx.

When assets have been disposed of, it is important to record the disposal in FA system in a timely manner and with an accurate disposal date. Disposal removes the asset and accumulated depreciation balances from FA system and provides an audit trail for disposals. Refer to xx.

Valuation Methods

The desired method of valuation is actual (historical) cost. Locate this data by retrieving original invoices, purchase orders, check copies, contracts, minutes, or other applicable documentation. However, if the department is unable to establish actual cost after a reasonable expenditure of effort, rely upon estimated cost data. Some methods available for ascertaining estimated cost are:

- Engineering studies
- Catalogue prices
- Vendor price lists
- Deflation indices
- External appraisal
- Matching to previously "costed" items

Salvage Value

The salvage value of an asset is the estimated value it will have when it reaches the end of its useful life. Some assets are not likely to have a salvage value at the end of their useful life. This is particularly true for assets that are subject to obsolescence such as information technology related assets. For example, due to continuous changes in technology, computers are often worthless at the time of replacement, and therefore, have no salvage value.

On the other hand, some types of assets, vehicles, for example, are often still in working order when replaced and generally are sold or auctioned for some value.

Departments should develop and periodically update a methodology for estimating salvage value that is based on the type of asset, its obsolescence and degree of usefulness at disposal and the nature of the disposal process. Assets that are typically sold or auctioned at the time of replacement should be assigned a reasonable salvage value. The estimate should be based on actual values received. ***Do not enter a salvage value that is equal to the total cost of the asset.***

The estimate of useful life chose to indicate normal replacement policy should also be a factor in estimating salvage value.

Avoid Overstating Asset Balances

When it becomes evident that obsolete material or damaged assets are recorded as capitalized assets in IFAS, reduce the value reported in IFAS to the asset's net realizable value in order to avoid overstating asset balances. This may entail changing the status of the asset from capitalized to controlled. Also consider, given the type of asset and/or the occurrence that led to the decline in value, whether additional action is necessary to ensure that asset values are not overstated. Such action would involve reviewing the status and condition of similar assets or assets impacted by a similar event. Materially overstated assets should be written down to net realizable value.

Impairment of Capital Assets

Any capital asset impairment that represents a significant and unexpected decline in the **service utility** of the asset (as defined by Governmental Accounting Standards Board Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*) should be reported to Accounts Division as soon as possible for the appropriate treatment in IFAS. Routing costs incurred to maintain the asset in an operating condition are expensed and not included in the FA system in IFAS.

GASB No. 42 provides three methods for calculating the asset impairment amount. A detailed description of each method is available in GASB NO. 42. The method used depends on the reason behind the impairment. Any department that believes it may have asset impairment should notify Accounts Division as soon as possible for the appropriate treatment of the impairment.

Pollution Remediation

Governmental Accounting Standards Board Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, requires pollution remediation activities to be capitalized when goods are received in certain circumstances when obligation events occur. Under certain conditions, pollution remediation related expenditures should be capitalized when incurred. Obligating events are defined as the following:

1. The government is compelled to take pollution remediation action because of an imminent endangerment to health, welfare or the environment.
2. The government violates a pollution prevention-related permit or license.
3. The government is named, or evidence indicates that it will be named, by a regulator as a responsible party or potentially responsible party for remediation, or as government responsible for sharing costs.
4. The government is named, or evidence indicates that it will be named, in a lawsuit to compel participation in pollution remediation.
5. The government commences or legally obligates itself to commence pollution remediation.

Any department having an obligating event related to pollution remediation should contact the Accounts Division for guidance on capitalizing assets associated with the pollution remediation.

Chapter 4. Asset Categorization

Overview

The purpose of this topic is to provide guidance on the proper categorization of capital assets for input into the County's IFAS. Once an asset has been classified as capitalized, it is important that it be further defined into the proper detailed category in the County's Fixed Asset (FA) system within IFAS.

In addition to the FA system, the Department of Finance, Real Property Manager maintains a system for real estate transactions, accessible via the website http://countyintranet/RP_Finance/. The County-Related Property Management System (CRPMS) records and reports information on the physical aspects of land and buildings.

The assignment of proper category ensures compliance with generally accepted accounting principles (GAAP) when preparing agency financial statements and County's CAFR. It is also important in applying appropriate depreciation rates based on the useful life in order to properly report net asset values.

Capital Asset Type and Estimated Useful Life

Capital Asset Type and Estimated Useful Life

The County has invested in wide variety of capital assets used in County operations. These assets are broadly classified with estimated useful lives as follows:

Asset Type	Useful Lives
• Land	Indefinite
• Buildings and systems	20-45 years
• Improvements other than buildings	5-20 years
• Machinery and Equipment	5-10 years
• Infrastructure:	
o Landfill	5 years
o Sewer Systems	20-50 years
o Roadway Systems	15-20 years
o Drainage Systems	50 years
o Bridges	50-75 years
• Construction in Progress	N/A

The asset type is used to organize capital assets in the broad classifications above. An essential function of the asset type is to establish a link between the asset master record and the related posting to the accounting general ledger. Therefore, assets purchased, constructed or donated that meet or exceed the capitalization threshold, or minimum reporting requirements, must be uniformly classified, utilizing the existing asset type structure. Each asset type is further detailed into the fixed asset catalog codes. The fixed asset catalog code breaks the asset class into groups of similar items and contains the recommended estimated useful life (expressed in years) for the group of assets.

Policies

Both capitalizable and controllable property is subject to all requirements regarding security, maintenance, and utilization. Whereas information regarding capitalizable assets is entered for both control and required financial reporting, information regarding controllable assets is entered primarily for management purposes. These assets are flagged with a control indicator in order to distinguish them from capitalized assets.

Capitalized Assets

A capitalized asset is a capital asset that has an expected useful life of more than one year and the asset individually has a value equal to or greater than the capitalization threshold established in the County's CAFR. Capitalized assets are reported for financial reporting purposes[4].

The memo dated October 1, 2002 from the Accounts System Administrator allowed the cost relating to training is included in the cost to be recorded in the fixed asset record. However, the Government Finance Officer's Association's *Accounting of Capital Assets*, published in 2008 provides a guideline that the cost of training employees to utilize a newly acquired capital asset should *not* be capitalized. Therefore, the training cost should not be added as the cost of the fixed asset.

Capitalization Thresholds

The County's capitalization threshold for capitalizing assets for each category is as follows:

Category	Threshold
• Machinery and Equipment	$5,000
• Improvements on Existing Asset	$100,000
• New Construction and Acquisition	$250,000

[4] Equipment valued at $5,000 or more, with the exceptions of certain types of equipment as provided above.

Exceptions

The following categories of items are to be considered equipment and accounted in the County's fixed asset record, regardless of the purchase price or individual value:

1. Computers (i.e. desktop computer, CPU, laptop computers, etc.)
2. Computer peripherals over $500 (i.e. monitors, printers, etc.)
3. All vehicles (including off-road and ocean craft)

Controlled Assets

A controlled asset is an asset that has an expected useful life of more than one year and the asset individually is valued at $1,000 - $4,999. Controlled assets are reported in the FA system and excluded from accounting calculations, depreciation, and certain financial reports produced for financial disclosure purposes.

Proper stewardship must be maintained over all departmental capital assets, including those valued at $1,000 - $4,999 (referred to as controllable assets). The department has the discretion to develop an internal policy regarding controlling or tracking assets valued at less than $5,000.

Component Cost

A component part is that part of a unit of equipment that cannot be used independently of the remaining piece of equipment or is physically connected to the major asset. This definition applies even though the component part may meet the capitalization criteria by itself.

For example, a personal computer (PC) consists of a Central Processing Unit (CPU), monitor, and keyboard. This is considered to be one unit consisting of three parts, none of which can be used independently. Therefore, the total cost of the PC should be included in the FA system with a tag attached to the CPU and the asset depreciation showing a PC consisting of a CPU, monitor, and keyboard. Under normal conditions, if one of the pieces had to be replaced, it would either be covered under a maintenance contract and no cost will be incurred, or the replacement piece would be purchased and the change would be considered as an expense and not capitalized.

Component Cost Example 1

Certain types of equipment may be used with a large number of other types of equipment. For example, a telephoto camera lens may be used on any of a number of cameras separately inventoried and tagged by the department/agency. ADP equipment is another area in which there would be equipment components, such as printer connected to a mainframe.

The key difference here is that these items can operate on many different pieces of equipment, and the equipment to which they are attached can operate independent of the component (i.e. the camera can operate without the telephoto lens and the mainframe can operate without the printer). Therefore, the items is not a constituent element (or component) of the system. It is a separate piece of equipment. If the item meets the capitalization criteria as an individual item, it should be separately recorded and tagged as a capital asset equipment item.

Component Cost Example 2

Another example would be panels associated with providing an open office workstation. If fifteen panels were required to create an office area, and the aggregate cost met the capitalization criteria, but the individual cost per panel did not, the panel item(s) would not be capitalized. This is because the per-unit cost must be considered when this is the normal billing procedure. An office consisting of 15 panels is not being purchased. Instead, 15 panels are being purchased to build an office. If the individual cost of one panel meets the capitalization criteria, then 15 distinct assets would be setup and **not** one asset consisting of 15 panels.

However, if a department or agency replaces or installs multiple office cubicles as a single project, (herein referred to as an "office cubicle system"), then the entire "office cubicle system" should be recorded as a capital asset whenever the total costs is equal to or exceed $5,000. "Office cubicle system" projects typically involve extensive construction costs such as new lighting, new wiring (both electrical and IT networking installation), new carpet, etc., in addition to the actual installation cost of the new office cubicles. Construction in Progress should be recorded during the construction phase and then reversed when the new "office cubicle system" is completed and recorded as a capitalizable asset.

Capital Asset Categories and Procedures

Land

Land is defined as the surface or crust of the earth, which may be used to support structures or grow crops, grass, shrubs, and trees. Land is capitalized; however, it is characterized as having an inexhaustible life, and therefore, it is not depreciated. All expenditures made to acquire land and to ready it for its intended use should be considered as part of the land cost.

The cost of land should include the following examples:

- Purchase price or, if donated, fair market value at time of donation
- Commissions
- Professional fees (title searches, architect, legal, engineering, appraisal, surveying, environmental assessments, etc.)
- Permanent landscaping such as land clearing, excavation, fill, grading, drainage (includes movement of earth in preparation for water impoundment)
- Demolition of existing buildings and improvements (less salvage)
- Removal, relocation, or reconstruction of property of others on the land so that the land may be used differently (i.e. railroad, telephone and power lines)
- Interest on mortgages accrued at date of purchase
- Accrued and unpaid taxes at date of purchase
- Other costs incurred in acquiring the land
- Water wells (includes initial cost for drilling, the pump and its casing)
- Right-of-way (permanent)

Please refer to Chapter 1 of this manual for legal requirements on real property.

The cost of land does **not** include expenditures in connection with land improvements that are considered exhaustible (that deteriorate with use or passage of time) or are part of an infrastructure asset such as paving, parking lots, and fencing. These costs are set up in a separate asset category, *"Infrastructure"*, and are depreciated. Unlike land, these items have finite lives and are depreciable.

Land Improvements

Land improvements are defined as attachments to the land that have limited lives and therefore, are recorded separately and are depreciable.

Examples of improvements to land include the following:

- Fencing and gates
- Landscaping of non-temporary nature
- Parking lots/driveways/parking barriers/roadway
- Outside sprinkler systems
- Recreation areas and athletic fields (including bleachers)
- Golf courses
- Paths and trails
- Septic systems
- Swimming pools, tennis courts
- Fountains
- Plazas, pavilions
- Retaining walls

- Lighting systems
- Water impoundment structures or attachments (dam, liner, other water control structures)

Some costs relating to landfill, wastewater, drainage and highways are setup in a separate asset category called *"Infrastructure,"* and are depreciated outside the County's FA system.

Buildings and Building Improvements

A building is defined as a structure that is permanently attached to the land, has a roof, is partially or completely enclosed by walls, and is not intended to be mobile.

Building improvements are defined as capital events that increase the value of a building, materially extend the useful life of a building, or both. A building improvement should be capitalized as a sub-asset of the building and recorded as an addition of value to the existing building if the expenditure for the improvement is at the capitalization threshold and the expenditure increases the life or value of the building by 25 percent of the original life period or cost.

The cost of the purchased or constructed buildings should include the following:

PURCHASED BUILDINGS:
- Original purchase price
- Expenses for remodeling, reconditioning, or altering a purchased building to make it ready for use for the purpose for which it was acquired
- Environmental compliance (i.e. asbestos abatement)
- Professional fees (sales commission, legal, architect, inspection, appraisal, title search, etc.)
- Payment of unpaid or accrued taxes on the building at the date of purchase
- Cancellation or buyout of existing leases on the building
- Other costs required to place or render the asset into operation

CONSTRUCTED BUILDINGS:
- Completed project costs
- Interest accrued during construction for enterprise type activities
- 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[5], engineer, management fees for design and supervision, legal)
- Costs of temporary buildings used during and for the construction
- Unanticipated costs such as rock blasting, piling, or relocation of the channel of an underground stream)
- Conversion of attics, basements, etc., to usable office, research or other space

BUILDING IMPROVEMENTS[6]*:*

- Structures *attached* to the building such as covered patios, sunrooms, garages, carports, enclosed stairwells, etc.
- Original installation/upgrade of heating and cooling systems, including ceiling fans and attic vents
- Original installation/upgrade of wall or floor 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, other interior framing
- Installation or upgrade of windows or door frames, upgrading of windows or doors, built-in closets 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 or closed circuit television systems, networks, fiber optic cable, wiring required in the installation of equipment (that will remain in the building)
- Permanently attached fixtures or machinery that cannot be removed without impairing the use of the building
- Additions to the buildings (expansions, extensions, or enlargements)
- Other costs associated with the above improvements

The main criteria for capitalizing building improvements is whether the expenditures significantly extend the useful life or significantly

[5] Architect fees are expensed if a decision is made to **not** proceed with the construction of the building.

[6] For a replacement to be capitalized, it must be a part of a major repair or rehabilitation project that increases the value and/or useful life of the building (i.e. renovation of a recreation center) and meets the capitalization threshold. A replacement may also be capitalized if the new item or part is of significantly improved quality and higher value compared to the old item or part (such as replacement of an old shingle roof with a new fireproof tile roof). Replacement or restoration of an item to its original utility level is not capitalized. Determinations must be made on a case-by-case basis.

enhance the value of the individual building. *Please refer to the Decision Tree outlined in Chapter 3 or Chapter 7 of this manual for determining whether expenditures can be capitalized.*

Furthermore, to determine whether the value has been significantly impacted, the County of Maui uses the CAFR capitalization threshold of $100,000 for existing improvements. As such, the following criteria should be used to determine when an improvement to an existing may be capitalized:

- If the building improvement is greater than or equal to $100,000, then the improvement may be capitalized as a separate "Building" asset.
- Expenditures not meeting the capitalization criteria should be expensed.

Equipment, machinery, vehicles, furniture

Equipment[7] is defined as fixed or movable tangible assets to be used for operations. Improvements or additions to existing equipment that constitute a capital outlay or increase the value or life of the asset by 25 percent of the original cost or life should be capitalized and recorded as a sub-asset of the existing asset.

A vehicle is a fixed asset that can move itself under its own power. Cars and trucks should be classified as vehicles. The County has three types of vehicle classification: 1) cars/trucks – light-weight vehicles; 2) other vehicles – heavy vehicles/trailers/other vehicles, and; 3) off-road – vehicles with no road exposure or license issued by the Division of Motor Vehicles. Certain vehicles are subject to the County's Motor Vehicle Policy. Department must ensure that all policies and guidelines provided in the *County's Motor Vehicle Policy* are followed prior to purchasing vehicles. The policy is accessible via the County's intranet[8].

The costs of equipment, machinery, vehicles, and furniture include the following:

- Original contract or invoice price
- Freight charges
- Import duties
- Handling and storage charges
- In-transit insurance charges
- Sales, use, and other taxes imposed on the acquisition

[7] If incidental items, such as extended warranties or maintenance agreements, are included with the capital asset upon receipt and are not listed as a line item on the purchase order or on the invoice, then the incidental charges are considered as part of the capital asset.

[8] Website address is http://intranet.co.maui.hi.us/index.aspx?NID=769.

- 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

Determine whether an item is a 1) separate piece of equipment having its own recorded cost and depreciation, or 2) component and included as part of the cost and description of the overall asset. The majority of items are usually separate pieces of equipment. Similar to buildings, County uses CAFR equipment capitalization threshold. If the improvement results in an improvement or replacement of existing equipment and is greater than or equal to $5,000, the new asset may be capitalized as a separate "Equipment" asset. Any items not capitalized should be expensed.

Infrastructure

Long-lived capital assets that normally are: 1) stationary in nature and 2) can be preserved for a significantly greater number of years than most capital assets.

Examples of infrastructure assets include the following:

- Highways and rest areas
- Roads, streets, curbs, gutters, sidewalks, fire hydrants
- Bridges, railroads, trestles
- Canals, waterways, wharfs, docks, sea walls, bulkheads, boardwalks
- Dam, drainage facility
- Radio or television transmitting tower
- Electric, water, and gas (main lines and distribution lines, tunnels, etc.)
- Fiber optic and telephone distribution systems (between buildings)
- Light system (traffic, outdoor, street, etc.)
- Signage
- Airport runway, strip, taxiway or apron

Infrastructure assets are depreciable, and the total acquisition or construction cost must be considered for capitalization.

Maintenance to an infrastructure asset that does not extend the asset's useful life or expand its capacity should be expensed (not capitalized). On the other hand, costs incurred that do extend the asset's useful life or expand its capacity should be capitalized.

Capital Leases

Capital leases transfer virtually all rewards and risks that accompany ownership of property to the lessee. A capital lease is a means of financing property acquisitions and has the same economic impact as a purchase made on an installment plan. Thus, the lessee in a capital lease must record the leased property as an asset and the lease obligation as a liability.

A lease agreement entered into by a County department is a capital lease and should be capitalized only if the lease agreement meets **one** of the following criteria

- The lease transfer 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 administrative costs, equals at least 90 percent of the fair value of the leased property.

Leases that do not meet any of the proceeding criteria should be recorded as an operating lease.

Leasehold Improvements

Leasehold improvements are defined as improvements made to leased property that will revert to the lessor at the expiration of the lease. Leasehold improvements include construction of new buildings or improvements made to existing structures by lessee, who has the right to use these leasehold improvements over the term of the lease. Moveable equipment or office furniture that is not attached to the leased property is not considered as a leasehold improvement. For leasehold improvements, the useful life is the estimated service life of the leasehold improvements, or the remaining term of the lease, whichever is shorter.

Intangible Assets

The Governmental Accounting Standards Board issued Statement No. 51, *Accounting and Financial Reporting for Intangible Asset*. Governments are required to implement this standard for periods beginning after June 15, 2009. Governments possess many different types of assets that may be considered intangible assets, including easements, water rights, timber rights, patents, patents, trademarks, and computer software (including licenses).

Characteristics

Statement No. 52 identifies an intangible asset as having the following three required characteristics:

1. It lacks physical substance – in other words, you cannot touch it, except in cases where the intangible is carried on a tangible item (i.e. software on a DVD).

2. It is nonfinancial in nature – that is, it has value, but is not in a monetary form like cash or securities, nor is it a claim or right to assets in a monetary form like receivables, nor a prepayment for goods or services.
3. Its initial useful life extends beyond a single reporting period.

Asset Types

There are two types for intangible assets, which are as follows:

1. Depreciable Intangible Assets. The asset is depreciated over the useful life of the asset which is determined by contractual, technological, or other factors that put limit to the asset.
2. Non-Depreciable Assets. If parameters do not exist and it is reasonable for the asset to have an indefinite life, then for financial reporting purposes, the intangible asset would not be depreciated.

Easements

An easement is defined as an interest in land owned by another entity that entitles its holder to a specific limited use or enjoyment (right to use the land). Easements are typically used to access another property. The useful life of an easement is determined by the contract in place. If an easement has an indefinite life, then for financial reporting purposes, it would not be depreciated. If an easement has a limited life, then for financial reporting purposes, it would be depreciated over the life of the asset (contract).

Department must ensure that laws and regulations as prescribed in the MCC, Chapter 3.44.015 are followed as it relates to the acceptance of conveyance of real property interests to the County of Maui's Department of Water Supply, Department of Public Works, and Department of Parks and Recreation.

Internally Generated Computer Software

Internally generated computer software is:

- Created or produced by the government or an entity contracted by the government; or
- Acquired from a third party, but requires more than minimal effort to achieve expected service capacity.

Costs incurred in creating an internally generated intangible asset are either expensed or capitalized depending on the stage in the asset's development. Therefore it is important that personnel involved in the project carefully track outlays and categorize them into one of the following three stages, based on the nature of the activities, not the timing:

1. Preliminary project stage – ***Expense***
    a. Conceptual formulation and evaluation alternatives
    b. Determination of existence of needed technology
    c. Final selection of alternatives
2. Application development stage – ***Capitalize***
    a. Design of the chosen path
    b. Coding
    c. Installation to hardware
    d. Testing and parallel processing
    e. Software purchase
3. Post-implementation/operation stage – ***Expense*** (even if the timing of the outlay occurs while application development is still in progress)
    a. Application user training
    b. Software maintenance

Data conversion is an activity of the application development stage only if it is necessary to make the software operational; otherwise, it is an activity of the post-implementation/operation stage. Data conversion activities include:

- Purging/cleansing of existing data
- Conversion of data from one system to new system
- Reconciliation of data from one system to data in new system

Modifications of software that is already in operation are capitalized only under certain conditions if any of the following occur:

- An increase in the functionality of the software
- An increase in the efficiency of the software
- An extension of the estimated useful life of the software

If the modification does not result in one of the above, associated outlays are considered maintenance and must be expensed.

Depreciation

General Guidelines

Depreciation is a 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.

Calculating Depreciation

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

1. Date the asset was placed in service
2. Asset's cost or acquisition value
3. Asset's salvage value
4. Asset's estimated useful life, and
5. 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. Please refer to the Capital Asset Type and Estimated Useful Life section of this chapter for the County's schedule of estimated useful lives by type of asset. When an asset is added to the County's Fixed Asset system, depending upon the type of fixed assets selected, a corresponding estimated useful would be assigned.

Depreciation Method

The County of Maui has established a 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 the annual depreciation is determined by dividing an asset's cost reduced by the salvage value, if any, by its estimated life. The total depreciation amount 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.

Chapter 5. Capitalize vs. Operating Expense

Determining whether a capital project is to be capitalized or expensed

General Guidelines

In determining whether expenditures are related to a maintenance ***item*** or whether it is related to a capital project, the following guidance is offered:

Care is sometimes needed to distinguish actions that lengthen the useful life of an asset from those that merely avoid shortening it.

Assume, for example, that a new building is expected to have a useful life of 80 years, but will need to have its roof replaced in just half that time. Further assume that the cost of the roof is included in the cost of the building (i.e. rather than treated as a separate capital asset in its own right).

It might be tempting to argue that since the building's useful life would be just 40 years if the roof were not replaced, the replacement extends the building's useful life and so qualifies as an improvement. In substance, however, the replacement of the roof does not lengthen the building's originally estimated useful life of 80 years, but simply avoids cutting it in half. That is, the roof replacement ***maintains*** rather than ***extends*** the originally estimated useful life of the building, and therefore should be treated as a repair (i.e. maintenance) rather than as a replacement[9].

- The area of capitalizing or expensing capital expenditures including repairs and maintenance requires judgement and has significant flexibility. If the expenditures are to be capitalized, then the sob-object code that begins with "7" should be used. If personnel are directly hired for the project (such as a project manager), these costs need to be capitalized as well.

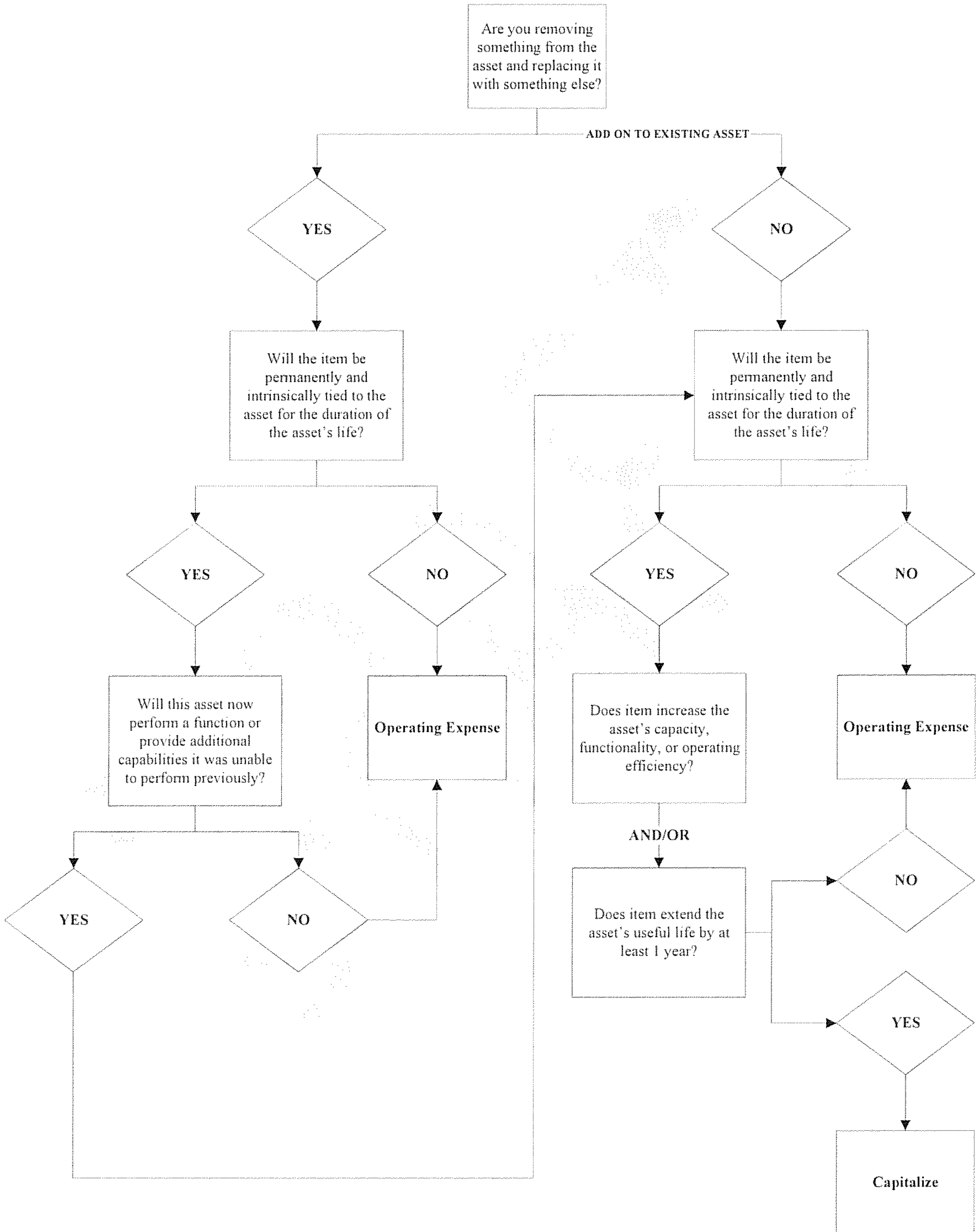
- Generally, expenditures that **increase the economic value** of the asset **increase the useful life beyond the original useful life**, or **increase the productive capability** (uses, scope, etc.) should be capitalized.

- Expenditures made to **restore or maintain** an asset at its original condition are expensed and not capitalized.

[9] Source: *Accounting for Capital Assets: A Guide for State and Local Governments*.

Decision Tree

Below is a decision tree that a department must use to determine if an item relating to building improvements qualifies as a capital asset[10]:



[10] For financial reporting purposes, the threshold requirement must also be met for an item to be capitalized.

Accounting for Supplies Expense

Equipment

Equipment with acquisition price of $1,000 or more per unit should be coded to a sub-object code beginning with "7" number for tracking purposes. For inventory purposes, assets equal to or greater than $1,000 in cost are recorded in the Fixed Asset, whether it is depreciable or non-depreciable asset. Please refer to Chapter 4 for detailed guidelines and examples of equipment and other related costs that should be included in the total cost.

Supplies

Supplies are expendable and/or disposable items which may or may not have a useful life in excess of one year, but are less than $1,000.

Any equipment with purchase price of less than $1,000 per unit should be coded to a sub-object code "6060 – Small equipment under $500" or other related sub-object code that begins with "6" number.

Accounting for Repairs/Maintenance Expense

Repairs/Maintenance Expense

Maintenance costs allow an asset to continue to be used during its originally established useful life. Maintenance costs are expensed in the period incurred.

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

Examples
• Adding, removing, and/or moving of walls relating to renovation projects that are not considered major rehabilitation 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 examination, 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, etc. • 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 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 of the building

Procedures

Expenditures that qualify as repairs and maintenance must be posted to an operating index code which normally begins with "9" or "1" for grant funds **and** sub-object code that begins with "6".

Departments are responsible for ensuring that repairs and maintenance expenditures are properly recorded. If expenditure that qualifies as capital asset is posted incorrectly to an operating account, it will result in the costs being expensed in the current period, an understatement of assets and current and future years' depreciation, overstatement of operating costs, and impacts the budget to actual schedules of the County's Comprehensive Annual Finance Report (CAFR).

For further guidance on determining whether expenditure qualifies as a capital or repairs/maintenance expense, please contact the Financial System Analyst prior to initiating a purchase requisition or request for proposal (RFP).

If a department identifies an expenditure that has been paid or partially paid and it was incorrectly posted to an operating account, please submit a Demand Request form. This form and the instructions to complete the form are accessible via the County's intranet website or by clicking on this link, Demand Request Form. **NOTE: It is important that this form is completed within the same fiscal year that the expenditure was incurred.**

Chapter 6. Construction Work in Progress (CWIP)

General Guidelines

Construction Work in Progress (CWIP) consists of construction projects subject to capitalization, either tangible or intangible in nature, but not yet completed. These projects are coded with index codes that begin with "3" and subject codes that begin with "7". Departments must ensure that all projects that may qualify as capital assets are properly accounted in the County's financial system.

When a capital asset project is completed within one fiscal year, the related asset is added directly to County's fixed assets before fiscal year end. If a project is not completed within one fiscal year, that portion of accumulated costs which is capitalizable should be reported and recorded as CWIP at fiscal year-end. CWIP that meets the criteria for a capital asset is reported in the County's CAFR, Assets, Capital Assets section. No depreciation is recorded until the asset is placed in service.

The following guidelines must be used to determine if costs associated with capital projects are 1) capital expenditures versus current period expenses, 2) the amount of the expenditures, and; 3) whether the project should be recorded in the Construction in Progress accounting in IFAS at year end.

- If the cost incurred increases the future economic benefits, it is a capital expenditure. Future economic benefits are increased by:
    - Extending the life of the asset
    - Improving the productivity, and
    - Improving the quality of service.
- If the cost incurred was to maintain the asset, it is a current period expense. *Please refer to Chapter 3 and Chapter 4 of this manual for further information on identifying costs that are capitalizable or should be expensed.*
- Review all costs associated with capital projects appropriations to determine if the project should be capitalized through the CWIP Status Report process.
- Ensure project and related expenditures fall into appropriate phase in the life of the asset.
    - Planning
    - Acquisition

- Construction
- Improvement
- Renovation
- Repair
- Replacement
- Relocation,
- Demolition, and,
- Construction in progress may also apply to software and other intangible assets as discussed in Chapter 4 of this manual.

Responsibilities

The following are general management and processing responsibilities of the participants in the CWIP accounting processes:

Accounts Division, Department of Finance

The Accounts Division, under the Department of Finance shall provide the County's CWIP accounting management oversight. This division shall also provide the requisite performance reporting; develop and promulgate accounting policies and procedures; and coordinate CWIP procedural accounting requirements, to include the requisite technical training and assistance to all County departments having construction responsibilities.

The Accounts Division shall also carry out responsibilities for all County's capitalized and non-capitalized construction projects, to include coordination, assistance and the CWIP status reporting on processing elements performed by the departments (i.e., the project cost reconciliation reports and project completion requirements).

The Accounts Division shall also be responsible for recording the *completed* buildings and structures into the IFAS FA Subsidiary system, while maintaining the official property records and cost documentation for *completed* projects.

Departmental Program Manager

County departments having construction authority shall comply with all CWIP policies and procedures, and shall coordinate the CWIP requirements with the Accounts Division.

The Project Manager is responsible for day-to-day coordination of the CWIP accounting requirements with the Accounts Division, to include:

- Maintaining a record-keeping system

- Performing monthly or quarterly cost reconciliation reporting requirements
- Initiating form, Transfer Report, to include the sign-off by the Program Manager and forwarding the completed forms to Accounts Division.

Procedure for Quarterly CWIP Status Report

Documentation Requirements

Departments must ensure that sufficient internal documentation is maintained to support changes made to CWIP balances. The following information is necessary to meet this requirement:

- Each project should be assigned a project number to accurately track all project-related disbursements. **Each** invoice for **every** project should be reviewed and entered into a comprehensive spreadsheet (maintained by the department) which includes, at a minimum, the following information:
    - Project Number or Index Code
    - Project Title
    - Subproject Title
    - Date Paid
    - Fund Code
    - Cost Code
    - Vendor Name
    - A breakdown of the payment showing amounts expensed and capitalized (listed separately). If capitalized, the spreadsheet should also document the asset category (land, building, equipment, infrastructure or CWIP).
- For each reclassification from CWIP, the following information should be added to the spreadsheet:
    - Amount of decrease in CWIP
    - Date of decrease in CWIP
    - Asset category of offsetting increase (e.g. building, infrastructure)
    - Offsetting increase charged to expense, if any (this should be rare since expense items should not have been initially recorded as CWIP).

This spreadsheet will allow the departments to more easily track CWIP and should be reconciled with the CWIP Quarterly Status Report at least on a quarterly basis to ensure accuracy and completeness of reported amounts.

Refer to Appendix xx for a sample spreadsheet that may be used for CWIP documentation.

CWIP Status Report

Each department with capital improvement projects is required to provide status for each index code (starting with "3") reporting in the County's IFAS, on a quarterly basis[12].

The financial information of the CWIP Status report is updated by the Finance Department. The departments are responsible for updating the following sections of the report:

1. Status of the Project – the status of the project must be provided at the Contract or Purchase Order level and not at the index code level. At a minimum, the following information shall be provided:
   a. Notice to Proceed – actual or estimated date
   b. Bid Advertisement/Bid Opening – actual or estimated date
   c. Construction Project – if there is a delay in issuance of NTP or delay in start of construction activities once NTP is issued, a brief explanation of the reason for the delay and estimated date when the project is projected to start must be provided
   d. Completed Project[13] – if a project was completed during the quarterly period being reported, the project at the contract or purchase order level must indicate "Project Completed" and the completion date or date in service (DIS).
2. Project Phase – at the contract or purchase level, identify if the phase is in the planning, design, construction, construction services, surveying, land acquisition, etc.
3. Percent Completion – project's percent completion. When a project is 100% complete, this indicates that the project in service, the index code will be closed. No additional spending may be charged to the project and any remaining costs are expensed as incurred. If the project is not 100% complete (partial close) but meets one of the three criteria in Transferring to Capital Assets, the index activity will remain open and costs will continue to accrue to the index code until the project is 100% completed. Upon final completion of the project, the additional accrued costs are placed in service, and the activity is closed. The DIS for

[12] Reporting requirements effective Fiscal Year 2015, on a semi-annual basis at the minimum and effective Fiscal Year 2016, on a quarterly basis.
[13] Completed project which triggers the date in service may or may not have a 100% completion.

these additional costs will be the date the original costs were placed in service or the date on which the expense was incurred but reported as a sub-asset.

4. Contact Information – name and contact information of the project manager assigned to the contract or purchase order.

Procedure for Placing Constructed Assets in Service

Ongoing Review

As part of the CWIP Status Report, on an ongoing basis, regardless of project activity levels, departmental project managers will perform a review of all construction-in-progress report to determine the percentage of completion for each project.

Reporting Asset Placed in Service

Upon the earlier occurrence of 1) substantial completion[14] (execution of substantial completion contract documents), 2) occupancy, or 3) when the asset becomes use or useful, the project manager must send a completed Request to Place Asset in Service form within 5 business days via email to Dawn Winter and cc Mark Pigao. The subject of the email should read as "DIS – [Name of Project]" to ensure that the asset is recorded in the County's fixed asset system within the same month.

Upon receipt of the Request to Place Asset in Service, the Financial System Analyst, Mark Pigao will review and analyze the project ledger data to determine the costs to be capitalized for each asset resulting from the project, and prepare the Capital Fixed Asset form. The Capital Fixed Asset form must be signed by the project manager and department head, and must be returned to the Financial System Analyst within 10 business days.

Projects that have not reached the completion or occupied level will continue to be tracked in the CWIP status report. Annually, the Finance System Analyst will provide departments with a Schedule of CWIP detailing accumulated costs and percent completion information for each project that is open and has not yet been placed into service.

Other Procedures

In addition to the procedures outlined above, departments must also follow the following procedures required by the Real Property Manager and Risk Management.

[14] The construction work on a project is substantially complete if it is providing benefits or services for the intended purpose and/or is generating revenue, where applicable. If any of these criteria are not met, the asset should remain in the CIP.

Construction of a Building:

- **As soon as a Certificate of Occupancy** for the building has been acquired, please contact Risk Management[15]. When the Certification of Occupancy has been obtained, responsibility and liability for that building transfers to the County of Maui. Notifying Risk Management is the only way for departments to be assured that the building is covered by insurance for accidents or loss.

Acquisition of Real Property:

As soon as the department have closed on the purchase of the building:

- Department must submit the original conveyance document (i.e. warranty deed) to the Finance Director. The Finance Department will notify the following agencies: State of Hawaii's Department of Land and Natural Resources (DLNR), County's Real Property Assessment Division and Risk Management. The Finance Department's Real Property Manager will enter the information into the County Related Property Management System (CRPMS). The Risk Management notifies the County's insurance agent for the purchased asset to be included in the list of properties covered by the County's insurance policy.

[15] Prior to the construction of the building, the department is also responsible for notifying Risk Management for the building to be included in the insurance policy.

Chapter 7. Physical Inventory

Overview

Introduction

The purpose of this topic is to provide guidance in the administration of fixed asset physical inventory. The objectives of a physical inventory are to ensure that the assets recorded in the FA system physically exist, determine if unrecorded or improperly recorded transactions have occurred, and identify any excess, defective, or obsolete assets on hand. An effective inventory results in an accurate accounting of assets, and indicated the reliability of the systems of accountability for the acquisition, use, and disposal of those assets.

Inventory Policies and Procedures

Annual Inventory Policy

Chapter 103D-1208 of the Hawaii Revised Statutes requires that each department head or designated staff, having in their custody or under their control or using property belonging to the County, to complete and submit an annual inventory report to the Council. The inventory report includes all non-expendable properties in the possession, custody, control or use of the department.

Annual Inventory Procedures

At the end of each fiscal year, the Finance Department (A/P, Claims and Inventory Supervisor) transmits a memo to all the department heads to review the inventory listings report as of the end of fiscal year. A Certificate of Custodian must be signed by the department/agency head and notarized to comply with HRS 103D-1208. The certification must be returned along with a copy of the inventory listing report by the specified date on the memo. The Finance Department will then transmit the required documents to the County Council.

Guidelines

The following general guidelines have been established to ensure that the inventory will be effectively implemented and performed by the department:

- Individuals responsible for the property management function of the department should establish a timetable to coordinate the effort necessary to conduct the inventory.
- Responsible persons should assist in conducting physical inventories in their area.
- Discrepancies between recorded and actual inventories must be resolved in a timely manner through the submission of revised input forms and tagging, if necessary.

- Each item recorded is physically inspected for changes in condition and availability codes.
- Additions, deletions, and changes to FA inventory records must be transmitted to the individual responsible for departmental property management on a timely basis.
- Inventories may be conducted on a cyclical basis (i.e. all capital assets do not have to be inventoried at the same time as long as the entire inventory is done within the required annual process). Cyclical inventories enable property managers to schedule inventory activities over a long period of time, and thus, conserving staff resources.

The physical inventory must verify the asset's existence, and should provide a reference to lists and/or other documents evidencing the existence and cost of the asset examined. Procedures must include verification from the list to ensure the physical existence of listed assets and from the physical assets back to the list to ensure all assets physically in existence are recorded in the inventory records.

Although a physical inventory is only required once a year, it is recommended that equipment inventories be conducted quarterly, if practical. This is due to equipment assets being more subject to change, therefore, necessitating tighter control.

Guidelines - Equipment

The following detailed guidelines are provided for conducting the inventory and apply primarily to items in the machinery and equipment category:

- The individual performing the department's property management function will be permitted access to every room being inventoried.
- Either all the equipment (or the equipment sampled) located in the room will be checked for tag number and traced back to the inventory listing with the following physical attribute fields rechecked: location, responsible person, equipment condition, and equipment availability. Tagged items in the room which are reported on the department inventory report as located elsewhere will require a revision to record the change of location.
- If tagged items are missing from the inventory listing, or if untagged items are identified as meeting the FA definition of either a capitalized or controlled asset, inventory information must be completed at the time for subsequent entry into the FA system.

- A sampling of items with tags should be made and traced to the inventory listing to ensure it is recorded. Also, a sampling of items from the listing should be made to ensure the physical existence of the item.
- Any items found to be unrecorded or not physically existing should be listed as a discrepancy, subsequently researched, and then either entered or removed by disposal from the system, as appropriate.
- Once all the departmental locations have been checked for tagged, untagged, recorded or unrecorded items, the required changes will be processed by the Inventory Accountant.

To assist the departments in taking these physical inventories, xxx report, should be used. This is a detailed report that lists a department's assets by location in terms of xxx.

Equipment Additions and Transfers

System Generated (New Additions)

Any inventory item that is properly coded and paid via Purchase Order (PO) or Contract creates a fixed asset "shell" for entry in the Fixed Asset (FA) system. All PO information and Accounts Payable information will be recorded in the FA system without any departmental input. However, additional information is required from the departments to complete the fixed asset record.

Inventory Items Paid via Purchase Order:

For the inventory record to be system generated, the PO must be written and coded properly. The following is required for proper input of the Purchase Requisition (PR):

1. The cost of **each inventory item** must be at least $1,000 unless the item is exempt as stated in Chapter 4 of this manual.
2. The sub-object code must begin with "7".
3. The quantity and unit price should be indicated on each line (i.e. no lump sum or job lot amounts).

Additional detailed information is also required at the time the PO is paid for completion of the record. In order to accomplish this, a Fixed Asset stamp will be stamped by Purchasing on all pink receiving copies of the POs. The information on this stamp must be completed by the department prior to submitting the pink PO copy to Accounts Division for payment. Accounts will not pay any POs that do not have the Fixed Asset information completed.

Inventory Items Paid via Contract and Cash Advance:

Inventory items paid via contract and cash advance must be added to FA system manually. Departments should submit the Inventory Input Sheet form when requesting payment on a contract. *See Manual Input of Records section below.*

Manual (Additions and Transfers)

When requesting to add inventory items paid by contract or request for payment, the department must submit a Manual Inventory Input Sheet form. This form is also used to add any inventory items that weren't generated by the system such as donated property or property transferred from another governmental agency or items that were mis-coded on the PO.

The Manual Inventory Input Sheet form must also be submitted by the department when transferring inventory between County locations.

Tagging of Equipment

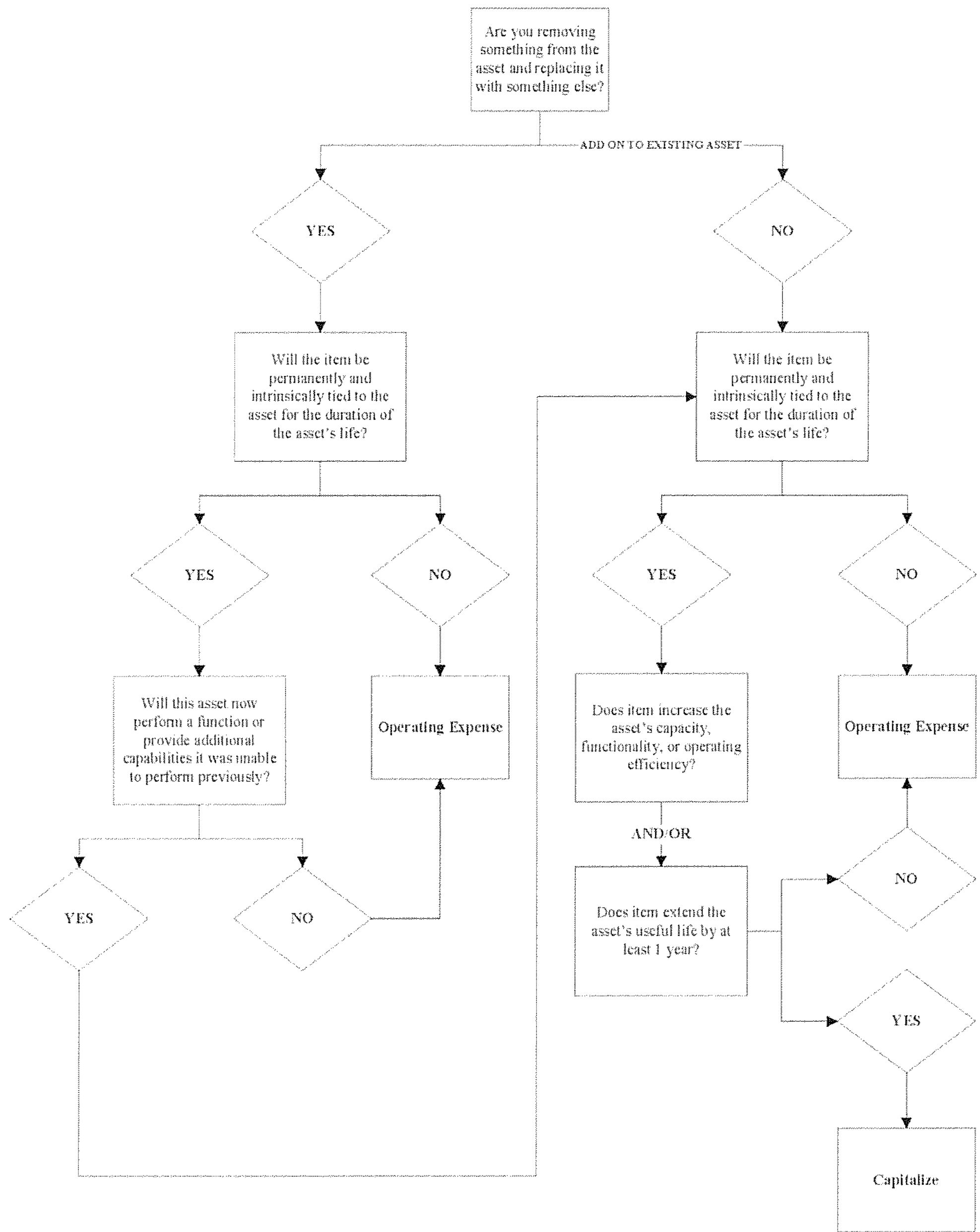
All equipment must be tagged. Tags must have an identification number and be pre-numbered. Consistency of placement is a primary consideration in the tagging process. The placement of the tag should facilitate its usefulness during the annual inventory process without hindering the operation of the asset. Generally, property tags are placed in one of the two locations, 1) near the serial number plate or 2) near the upper right-hand corner of the item which is fully visible without movement of the asset.

Departments/agencies are responsible for ensuring that the property tags are affixed and placed properly.

Chapter 8. Capital Asset Forms

Required Forms/Certifications

DECISION TREE FOR DETERMINING IF EXPENSE QUALIFIES AS REPAIRS/MAINTENANCE OR CAPITAL ASSET



COUNTY OF MAUI
REQUEST TO DISPOSE OF COUNTY PROPERTY
PURSUANT TO MAUI COUNTY CODE CHAPTER 2.72

APPLICATION TO: THE DIRECTOR OF FINANCE

APPLICANT:______________________________
NAME AND OFFICIAL POSITION

APPLICATION DATE:______________________

1. I hereby request that the property fully described on the attached Removal From Inventory Form be disposed of in the proposed method indicated in the last column.
2. The purpose(s) for which the property is (was) used is indicated on the attached Removal From Inventory Form.
3. The estimated value of the property is set forth on the attached Removal From Inventory Form.
4. The reason for disposal of the property is set forth on the attached Removal From Inventory Form.

I verify that the above and attached information is true and correct to the best of my knowledge.

____
Signature of Department Head

STATE OF HAWAII)
)SS.
COUNTY OF MAUI)

On this___day of ___________, 20__, before me appeared______________________
to me personally known, who, being by me duly sworn, did say that such person executed the foregoing instrument as the free act and deed of such person, and if applicable, in the capacity shown, having been duly authorized to executed such instrument in such capacity.

IN WITNESS WHEREOF, I have here unto set my hand and official seal.

____
Notary Public, State of Hawaii

My commission expires: __________

ACTION TAKEN:

______________________________ __________
APPROVED DIRECTOR OF FINANCE Date

[ ] DISAPPROVED - REMARKS______________________________

REPORT OF DISPOSAL:

I certify that I have participated in, or witnessed the disposal of all property in the manner indicated on the Removal From Inventory Form.

______________________________ __________
Signature of Participant or Witness Date

____
Title

INV DISPOSAL APPLICATION (EFF 04/2002)

COUNTY OF MAUI
REMOVAL FROM INVENTORY FORM
DATE: ________

TMENT ________] [DIVISION ________] [SECTION ________] [DISTRICT ________] [HEADER ________]

DECAL NUMBER	DESCRIPTION OF PROPERTY	PURPOSE FOR WHICH PROPERTY WAS USED	ORIGINAL COST	ESTIMATED VALUE	REASON FOR REMOVAL	PROPOSED METHOD OF REMOVAL CHECK APPLICABLE BOX
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT
						[ ]AUCT [ ]TRIN [ ]LDFL [ ]RECY [ ]NTLO [ ]GRNT

PROPOSED METHOD OF REMOVAL: SELLING [AUCTION], EXCHANGING [TRADE IN] OR OTHERWISE DISPOSING [LANDFILL(*), RECYCLE (*), NOT LOCATABLE i.e. MISSING, STOLEN, ETC] PER MCC 3.72, OR BY GRANT PER MCC 3.36

[ ] AUCT = AUCTION [ ] TRIN = TRADE-IN [ ] LDFL = LANDFILL [ ] RECY = RECYCLE [ ]NTLO = NOT LOCATABLE [ ] GRNT = GRANT (**)

(*) NOTE: To dispose by Landfill [LDFL] and Recycle [RECY], Estimated Value column [*] must be zero ($0).

(**) NOTE: For Grant please attach copy of fully executed grant agreement. In compliance with Maui County Code Chapter 3.36

COUNTY OF MAUI
INVENTORY INPUT SHEET - ITEMS GREATER THAN OR EQUAL TO $1,000 ($500*)
PROPERTY ADDITIONS,TRANSFERS OR CORRECTIONS
* Non- MIS computer equipment and all wheeled vehicles/trailers
DATE ________

GAINING/PURCHASING DEPT ________ DIVISION ________ SECTION ________ DISTRICT ________ SPECIFIC LOCATION ________

DISPOSING DEPARTMENT ________ DIVISION ________ SECTION ________ DISTRICT ________ SPECIFIC LOCATION ________

DECAL# LICENSE PLATE	COM VEH#	ASSET CLASS	PROPERTY DESCRIPTION	MAKE	MODEL	SERIAL#/VIN	YEAR	IN SERVICE DATE	ORIGINAL COST	PO,CONTRACT PAY REQUEST NO.	INDEX/SUBOBJ CODE	FINANCE USE PRIMARY/SEC CLASS
								TOTAL	$0.00			

CERTIFICATION OF DISPOSING/LOSING DEPARTMENT
I HEREBY CERTIFY THAT THE PERSONAL PROPERTY ITEMS DESCRIBED
HAVE BEEN TRANSFERRED TO ________

SIGNATURE OF CUSTODIAN ________ DATE ________

TITLE OF CUSTODIAN ________

CERTIFICATION OF GAINING/PURCHASING DEPARTMENT
____ I HEREBY CERTIFY THAT THE PERSONAL PROPERTY ITEMS HAVE BEEN TRANSFERRED TO MY CUSTODY
____ I HEREBY CERTIFY THAT THE PERSONAL PROPERTY ITEMS ARE TRUE AND CORRECT TO THE BEST OF MY KNOWLEDGE

SIGNATURE OF CUSTODIAN ________ DATE ________

TITLE OF CUSTODIAN ________

FIXED ASSET RECORD FOR EQUIPMENT, MACHINERY, VEHICLES & FURNITURE

ASSET IDENTIFICATION		ASSET LOCATION	
Decal/License Plate No.:	______	District:	______
Make:	______	Department:	______
Model:	______	Division:	______
Serial No./VIN:	______	Section:	______
Asset Year:	______	Specific Location:	______
In Service Date:	______		
Purchase Price:	______		
Classification:	______		