
STATE OF OHIO

**FINANCIAL REPORTING
AND ACCOUNTING POLICIES
FOR CAPITAL ASSETS
OTHER THAN HIGHWAY- AND BRIDGE-RELATED
INFRASTRUCTURE**

Effective October 02, 2014

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Overview

Introduction

The State of Ohio (the State) has a significant investment in capital assets such as land, buildings, land improvements, machinery and equipment (including furniture and fixtures, computer software, and works of art and historical treasures), vehicles, infrastructure, and construction-in-progress. In a major effort to improve financial reporting, accountability, and operational efficiencies in managing these assets, the State has established policies for the accounting and reporting of capital assets.

Complete and accurate capital asset records can help managers identify under-utilized buildings or surplus assets that can be reassigned for more productive use. Accurate records of capital assets and their associated accumulated depreciation can also help identify potentially needed replacement and renovation of existing assets. This type of management information is useful in making budgetary decisions for specific requests and long-term capital planning. Furthermore, detailed capital asset records for equipment and vehicles can assist in the development of a preventive maintenance program.

This document outlines in detail the information on capital assets (other than highway- and bridge-related infrastructure of the Department of Transportation) that state agencies must furnish to OBM each year for the State to meet its legal responsibilities with regard to external financial reporting. OBM addresses highway- and bridge-related infrastructure reporting requirements in a separate policy document that is solely applicable to the Department of Transportation.

Statements of Principle

These policies provide a basis for maintaining and reporting *auditable* information on the State's capital assets in conformity with generally accepted accounting principles (GAAP) for state and local governments. Section 1400, "Reporting Capital Assets," *Codification of Governmental Accounting and Financial Reporting Standards* (the Codification), as amended by Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments*, outlines the following three basic statements of accounting principle.

Reporting Capital Assets

A clear distinction should be made between general capital assets and capital assets of proprietary and fiduciary funds. Capital assets of proprietary funds should be reported in both the government-wide and fund financial statements. Capital assets of fiduciary funds should be reported only in the statement of fiduciary net position. All other capital assets of the governmental unit are general capital assets. They should not be reported as assets in governmental funds but should be reported in the governmental activities column in the government-wide statement of net position.

Valuation of Capital Assets

Capital assets should be reported at historical cost. The cost of a capital asset should include ancillary charges necessary to place the asset into its intended location and condition for use. Donated capital assets should be reported at their estimated fair value at the time of acquisition plus ancillary charges.

Depreciation of Capital Assets

Capital assets should be depreciated over their estimated useful lives unless they are either inexhaustible or are infrastructure assets using the modified approach as set forth in this section. Inexhaustible assets such as land, land improvements, and buildings that are considered to be historical treasures and are maintained in such a way as to be considered inexhaustible should not be depreciated. Depreciation expense should be reported in the government-wide statements of activities; the proprietary fund statement of revenues, expenses, and changes in fund net position; and the statement of changes in fiduciary net position.

Legal Requirements

Section 125.16, Ohio Revised Code, bestows the overall responsibility for coordinating and overseeing stewardship reporting of the capital assets owned by state agencies upon the Department of Administrative Services (DAS). Specifically, Section 125.16, Ohio Revised Code, states the following:

§ 125.16 Inventory records for state property.

- (A) In accordance with procedures prescribed by the director of administrative services, the officer in charge of each state agency, other than an institution of higher education, shall maintain current and accurate records of tangible personal property and real property, as defined by the department of administrative services that the state agency holds either directly or on behalf of the state. These records shall specify the value of the property, the number of acres of land, the number and kind of buildings, and other significant information about the property, as designated by the department.

On or before the first day of October immediately following the end of each fiscal year, the officer in charge of each state agency shall cause its inventory activity at the end of that fiscal year to be certified as correct and filed with the director, in accordance with procedures the director prescribes. In addition, the officer in charge of each state agency shall cause a full and accurate physical inventory to be taken and concluded prior to the close of each fiscal biennium. The officer in charge of each state agency holding such property shall report to the director, on forms or media the director prescribes, regarding all property acquired, updated, or disposed of by that agency, in the detail and format and at the times the director requires.

This division does not apply to any canal lands administered and managed and any canals and reservoirs operated and maintained by the director of natural resources under Chapter 1520 of the Revised Code.

- (B) The director of administrative services shall maintain current inventory records as certified and filed under division (A) of this section by a state agency, other than an institution of higher education. The director may establish uniform methods of identifying state property.

While the foregoing statute addresses stewardship reporting responsibilities with regard to the State's capital assets, it does not, however, specify accounting and financial reporting policies for these assets. The purpose of this document is to establish and document the State's ac-

counting and financial reporting policies that state agencies must follow when reporting their capital asset balances for consolidation in the State's comprehensive annual financial report, which the Office of Budget and Management (OBM) is required to publish under Section 126.21(A)(9), Ohio Revised Code.

Specifically, Section 126.21(A)(9), Ohio Revised Code, states the Director of OBM shall

Issue the official comprehensive annual financial report of the state. The report shall cover all funds of the state reporting entity and shall include basic financial statements and required supplementary information prepared in accordance with generally accepted accounting principles and other information as the director provides. All state agencies, authorities, institutions, offices, retirement systems, and other component units of the state reporting entity as determined by the director shall furnish the director whatever financial statements and other information the director requests for the report, in the form, at the times, covering the periods, and with the attestation the director prescribes. The information for state institutions of higher education, as defined in section 3345.011 of the Revised Code, shall be submitted to the director by the Ohio board of regents. The board shall establish a due date by which each such institution shall submit the information to the board, but no such date shall be later than one hundred twenty days after the end of the state fiscal year unless a later date is approved by the director.

Any questions about the financial reporting policies outlined in this document should be addressed to OBM's Financial Reporting Section.

Financial Reporting of Capital Assets

Because of the unique nature of governmental financial operations, a clear distinction must be made between the State's general capital assets and capital assets of proprietary and fiduciary funds. In keeping with the first basic statement of principle of reporting capital assets, as outlined in Section 1400 of the Codification, the State reports general capital assets and capital assets of proprietary and fiduciary funds separately.

General Capital Assets

General capital assets include assets the State acquires or constructs using resources accounted for in its governmental fund types.

In its fund financial statements for governmental funds, which are prepared on the modified accrual basis of accounting with a measurement focus on the flow of current financial resources, the State excludes general capital assets from the related governmental fund's balance sheet, and accordingly, the State does not report depreciation expense in the statement of revenues, expenditures, and changes in governmental fund balances.

However, in the State's government-wide financial statements, which are prepared on the accrual basis of accounting with a capital maintenance measurement focus, the State reports 1.) its general capital assets, net of accumulated depreciation, under the governmental activities column in the statement of net position and 2.) the related depreciation expense by program/function under the governmental activities section of the statement of activities.

Capital Assets of Proprietary and Fiduciary Funds

The State accounts for its proprietary and fiduciary fund capital assets in the proprietary (i.e., enterprise) and fiduciary (i.e., pension trust) fund types. Proprietary and fiduciary fund types operate on an accrual basis of accounting with a measurement focus on the flow of economic resources.

In its fund financial statements, the State reports capital assets associated with proprietary and fiduciary fund operations, net of accumulated depreciation, on the respective proprietary or fiduciary fund's balance sheet, and depreciation expense on the statement of revenues, expenses, and changes in proprietary fund net position and the statement of changes in fiduciary fund net position.

In its government-wide financial statements, the State reports 1.) its proprietary fund capital assets, net of accumulated depreciation, under the business-type activities column in the statement of net position and 2.) the related depreciation expense by program/function under the business-type activities section of the statement of activities. The State is not required to report fiduciary fund capital asset balances, net of accumulated depreciation, and related annual depreciation expense in its government-wide financial statements.

Capital Assets of Independently Audited Organizations

The financial statements of some organizations consolidated in the State's annual financial report are independently audited in conformity with generally accepted government auditing standards. Each independently audited organization establishes its own capital asset accounting policies and capitalization thresholds. For consolidation in the State's financial statements, OBM accepts the separately issued financial report of each organization and the capital asset-related disclosures therein on the provision that the respective report has received an unqualified opinion from the organization's independent auditor.

Fundamentals for Identifying Capital Assets

Definition

When cited in governmental accounting and financial reporting standards, the term, *capital assets*, includes land, improvements to land, easements, buildings, building improvements, vehicles, machinery, equipment, software, works of art and historical treasures, infrastructure, and all other tangible and intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period. *Infrastructure assets* are long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets. Examples of infrastructure assets include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems. Buildings, except those that are an ancillary part of a network of infrastructure assets, should not be considered infrastructure assets.

Cost Valuation

In keeping with the second basic statement of principle of reporting capital assets, as outlined in Section 1400 of the Codification, the State's capital assets should be reported at *historical cost*. Historical cost is the cash or cash equivalent price paid at the time of purchase or acquisition. The cost of a capital asset should include ancillary charges necessary to place the asset into its intended location and condition for use such as freight and transportation charges, site-preparation costs, and professional fees. If historical cost is not available, the asset should be reported at estimated historical cost. Donated capital assets should be reported at their estimated fair value at the time of donation plus ancillary charges, if any.

Significant Value and Useful Life Concepts

The identifying characteristics of a capital asset are *significant value* and *useful life*. In setting its capitalization policy, the State has established benchmarks to identify what the minimum cost of an asset should be (i.e., its significant value) to justify the time and expense of maintaining the information required for reporting it in the State's financial statements.

For a capital asset that does not fall under the asset classifications of land, infrastructure, software licenses/purchases, or building renovations and improvements, the State considers its costs to be of a significant value when they exceed \$15,000. For computer software and building renovations and improvements, the State considers costs to be of a significant value when they exceed \$100,000. For land and infrastructure assets, the State considers *all* costs associated with these asset classes to be of significant value.

Finally, if an asset meets the test of significant value and has an *estimated useful life of at least two years following the date of acquisition*, the State reports it as a capital asset.

The State's capitalization policy for capital assets, as summarized above and outlined more fully later in this document, applies to the State's GAAP financial reporting requirements only. It does not supersede the statutory requirements carried out by the Department of Administrative Services (DAS) for maintaining internal records on tangible personal property, as outlined in Section 125.16, Ohio Revised Code, and the guidelines issued by the DAS General Services Division.

Capital Asset Classes and Costing Methodologies

Major Classes of Capital Assets

The major classes of capital assets reported in the State's annual financial report and, as may be applicable, their respective capitalization thresholds for external financial reporting are as follows:

- *Land*, including easements on land that is not owned by the State, and also including any rights to access water, timber, gas, oil, minerals, etc. on land that is not owned by the State, regardless of cost;
- *Buildings* that cost more than \$15,000 each and any associated renovations and improvements thereon that cost more than \$100,000 per building component;
- *Land Improvements*, including renovations and improvements thereon, that cost more than \$15,000 each, and land improvements of any cost that comprise part of the cost of a capitalizable building, as described in Appendix 1;
- *Machinery and Equipment* (e.g., computer software, trademarks, furniture and fixtures, and individual works of art and historical treasures, etc.), including renovations and improvements thereon, that cost more than \$15,000 each, with the exception of computer software, which is capitalized when one of the following is true: 1.) it is integral to the functionality of a related system and the vendor does not separately itemize the cost of the software, when purchased, 2.) its cost exceeds \$100,000 a license, when purchased, (this would also apply to trademarks) or 3.) its development, renovation or improvement costs exceed \$100,000, when internally produced or modified (this would also apply to trademarks);
- *Vehicles*, including renovations and improvements thereon and trailers that are not self-propelled, that cost more than \$15,000 each and are capable of being licensed through the Department of Public Safety's Bureau of Motor Vehicles for intended over-the-road transportation use;
- *Infrastructure Assets* of the Department of Natural Resources acquired or constructed since June 30, 2001, regardless of cost; and
- *Construction-in-Progress* (which includes internally developed or modified software) that is expected to meet the criteria for inclusion in the State's government-wide financial statements when completed.

For the Department of Transportation, the State capitalizes all highway- and bridge-related infrastructure assets acquired or constructed prior to July 1, 2001, regardless of cost, and all highway- and bridge-related infrastructure assets acquired or constructed since June 30, 2001 that cost \$500,000 or more.

The following discussion briefly describes each asset class.

Land

Land is *real* property. Land costs include the land's initial cost, surveying fees, appraisal and negotiation fees, legal and title fees, damage payments, and assumption of any liens, mortgages, or encumbrances on the property. The demolition of unwanted structures at the time of acquisition of the land, including associated clearing, filling, and leveling, with the intention of using *cleared* land for the construction of a new building, is considered a part of land costs. Each

parcel of land the State owns should be recorded as a separate asset. Land should be reported as an acquisition when the State receives title to the land. Easements that the State acquires that permanently restrict the zoning of land, or which allow the State access to land it does not own, or are necessary for the construction of Department of Transportation infrastructure such as roads and bridges, are also considered to be Land assets.

Land upon which infrastructure is constructed is also part of the *Land* capital asset account, as are any easements or right-of-way costs associated with infrastructure assets.

Buildings

Buildings are permanent structures designed with a foundation and roof and may or may not be enclosed, with walls. The cost of a building includes its construction or purchase costs and the costs of all fixtures permanently attached and made a part of the building. *Permanently attached* means removal of the fixtures alters the intended use of the building. Buildings should be reported as acquisitions when they are ready for occupancy.

The cost of a constructed building includes contractor payments, in-house labor costs, professional fees for architects, appraisers, and financial advisors, site-preparation costs that are directly related to the building site (e.g., clearing, filling, leveling, and excavating), and damage claims and insurance. Other costs incurred during the period of construction, including any other expenditures required to prepare the asset for its use, should also be included in a building's cost.

Pre-fabricated structures that can be emplaced or displaced by a crane and do not require a foundation should be classified as land improvements rather than buildings.

Normally, works of art are considered to be part of a building when they are permanently affixed to a building. Therefore, fixed works of art are included in the inventory of buildings. The term, *fixed works of art*, includes, but is not limited to, items such as murals, bronze plaque reliefs, acropediums, statues attached thereto, ornate finishes, millwork, marble and stonework, plaster work, bronze grilles, and gates and doors.

A building may be recorded as a number of "component" assets. Component assets have significant and separately identifiable costs associated with them. The separate recording of building components helps facilitate the partial retirement of buildings due to renovations. Retiring components, as renovations are performed, results in a more accurate and useful capital asset value. Examples of building components are provided in Appendix 1.

Buildings that are connected by means of a covered walk are considered to be separate buildings for the purpose of recording them in the State's inventory.

The State Architect's Office has provided a breakdown of the costs of a *standard* building by component asset category on a percentage basis. If a state agency is constructing a new building or purchasing an existing building, it may apply the total cost to the standard percentages for each building component listed in Appendix 1. These percentages should be adjusted when the building is not considered to be *standard*. Typical features that would cause a building to be considered non-standard are large land sites, long distances from normally available utilities, specialized building use groups (such as hospitals, auditoriums, natatoriums, etc.), high-rise buildings, and storage buildings lacking some utilities. The standard percentages are as follows:

- 60 percent of the cost of a *standard* building may be applied to the *All Other Construction* component asset category

- 30 percent of the cost of a *standard* building may be applied to the *General Construction* component asset category
- 10 percent of the cost of a *standard* building may be applied to the *Land Improvements* component asset category

When a state agency builds or purchases multiple buildings and no breakdown of costs by individual building is available, it may allocate the total costs among buildings based on a pro-ration of the square footage of each building constructed or acquired.

EXAMPLE

A state agency spends \$3 million for the construction of three *standard* buildings. Building A has 20,000 square feet, Building B has 30,000 square feet, and Building C has 50,000 square feet, for a total of 100,000 square feet. The total cost of the \$3 million acquisition may be allocated as follows:

Allocation of Multiple Building Costs					
Building A:	\$3,000,000	X	20,000/100,000	=	\$ 600,000
Building B:	\$3,000,000	X	30,000/100,000	=	900,000
Building C:	\$3,000,000	X	50,000/100,000	=	<u>1,500,000</u>
			Total Cost Allocated.....		<u>\$3,000,000</u>

For Building A, total costs should be further allocated among the building components as follows:

Building A					
All Other Construction:	\$600,000	X	60 cent	Per- =	\$360,000
General Construction:	\$600,000	X	30 cent	Per- =	180,000
Land Improvements:	\$600,000	X	10 cent	Per- =	<u>60,000</u>
			Total Costs Allocated for Building A.....		<u>\$600,000</u>

Building component costs of Buildings B and C should also be allocated accordingly so the total \$3 million acquisition cost of all three buildings can be properly reported in the capital asset inventory records.

The allocation of building component costs for renovation projects often fall into the same building component. For example, the replacement of a roof, electrical system, and HVAC should all

be classified as *All Other Construction*. The allocation of costs to building components when renovations cover more than one building component, however, is not easily subject to estimates, since the scope of such renovation projects is almost infinitely variable. Nevertheless, some estimates may be possible for large renovation projects that involve renovating virtually all of a building's systems.

A major exception to the general policy for reporting buildings applies to roadside rest stops associated with the highway network that the Department of Transportation owns and operates. The State considers these structures to be an ancillary part of the highway system, and accordingly, the State classifies them as infrastructure assets.

Land Improvements

The costs of improvements, which are not attached to, mounted on, or in a building, should not be classified as land or buildings. Assets falling under this classification include sidewalks, retaining walls, underground and aboveground storage tanks, yard lighting, fencing, alleys, landscaping, storm sewers, various kinds of towers (e.g., communication towers), shoreline-erosion prevention and restoration costs, marinas, golf courses, and parking lots (including curbs and gutters) that are related to State buildings and facilities. Site preparation costs (clearing, filling, leveling, and excavating), which are related to the site of the land improvement, should be included in the costs of the land improvement. The State capitalizes costs of improvements in the same manner as buildings.

State parks have various pathways, jogging paths, bridle paths, access roads, etc. Paths or roads such as these that are not paved and are not intended to **regularly** carry vehicles, which are capable of being licensed for over-the-road use, are considered to be land improvements, not infrastructure.

Freestanding historical monuments, plaques, and markers are not considered to be land improvements, and are not capitalized.

Unlike buildings, land improvements should be separately reported as a single asset with no components. For example, a parking lot should be reported as an asset separately from the land upon which it is built. Curbs and gutters associated with parking lots should be included as land improvements.

Another major exception to the general policy for reporting land improvements applies to land improvements associated with the highway network that the Department of Transportation owns and operates. The State considers these assets to be part of the highway system, and accordingly, the State classifies them as infrastructure assets.

Machinery and Equipment

Machinery and equipment are tangible assets, which

- are not attached permanently to land, buildings, or land improvements,
- have unique serial numbers,
- are capable of being moved (although some disassembly may be required), and
- can be acquired under a capital lease.

For example, machinery bolted to a floor should be classified as equipment. However, fixtures, which are attached to land, buildings, or land improvements in such a way that *removal alters*

the intended use of the facility or site, should not be reported as machinery and equipment. Rather, state agencies should report such assets as an ancillary part of the land, building, or land improvement to which they are attached.

Costs of machinery and equipment include the total purchase price, net of purchase discounts, plus any trade-in allowances, transportation charges, installation costs, taxes, and any other costs required to prepare the asset for its intended use. (For a full discussion of the valuation policies regarding trade-ins, see page 18, “Exchanges or Trade-ins with Outside Parties.”) Machinery and equipment assets should be reported as acquisitions when the state agency physically receives the asset, **not** at the time when it pays the vendor for the acquisition.

Examples of machinery and equipment include, but are not limited to:

- computers, telecommunications, and electronics, including any integrated software for which the vendor has not separately identified its cost,
- printing presses and reproduction equipment, and
- construction-related machinery.

Each piece of machinery and equipment acquired that is determined to be a capital asset should be recorded as a separate asset. Computer software, furniture and fixtures, and individual works of art and historical treasures should also be included in the asset class of machinery and equipment. Spare or replacement parts should not be capitalized.

Vehicles and trailers that can be licensed for over-the-road use should not be classified as machinery and equipment, but should be reported under the *vehicles* asset classification.

Computer Software

Computer software is an intangible asset that is subject to capitalization. Computer software can be an integral part of a system, it can be purchased or licensed from external vendors, it can be purchased or licensed from external vendors and subsequently modified, or it can be developed and created in-house. Web sites created by governments are also considered to be intangible capital assets, similar to software, and their development costs should be capitalized.

When software is an integral part of and is essential to the functionality of a larger system, and the vendor has not separately identified its cost, the software’s costs should be capitalized as part of the system. When software is separately purchased or licensed, it should be capitalized as an asset if its cost is greater than \$100,000. A group license (i.e., installed on a local area network server or a wide area network server) would be reported as one capital asset. When software is developed and created in-house, it should be capitalized when total related costs such as direct costs of services and materials externally purchased and internal payroll costs directly associated with acquiring or designing the software, including coding, installation, and testing, exceeds \$100,000. If a license agreement covers more than one year, as in the case that the agreement requires annual installment payments to the vendor for the right to use the software over the life of the agreement, and if it is the State’s intention at the time of entering into the license agreement to keep the software for the life of the agreement, then the cost of the software should include the cost of the annual license fees for all years.

Governmental Accounting Standards Board Statement No. 51 (GASB 51), *Accounting and Financial Reporting for Intangible Assets*, addresses the issue of capitalization of software projects that are internally generated. Software projects are considered to be internally generated when they are either created entirely by the government, or when they are purchased/licensed

and then subjected to more than minimal modifications. GASB 51 requires that costs incurred during the preliminary project stage and the post-implementation operation stage be expensed, while costs incurred during the application development stage should be capitalized. The chart below explains the activities involved in these stages.

Preliminary Project Stage <i>(to be expensed)</i>	Application Development Stage <i>(to be capitalized)</i>	Post-Implementation/ Operation Stage <i>(to be expensed)</i>
<ul style="list-style-type: none"> • Conceptual formulation of alternatives • Evaluation of alternatives • Determination of existence of needed technology • Final selection of alternatives 	<ul style="list-style-type: none"> • Design of chosen path, including software configuration and software interfaces • Coding • Installation to hardware • Testing, including parallel processing phase 	<ul style="list-style-type: none"> • Training • Application maintenance

Preliminary Project Stage

Below are examples of costs associated with the following activities that occur during the Preliminary Project Stage:

- strategic decision-making about allocation of resources between alternative projects at a given point in time,
- determinations of performance requirements and system requirements,
- invitations to vendors to perform demonstrations,
- exploration of alternative means of achieving specified performance requirements,
- determinations of the existence of technology needed to meet performance requirements, and
- selection of software vendors and consultants that will assist in the software’s development or installation.

Application Development Stage

Below are examples of costs associated with the following activities that occur during the Application Development Stage:

- external direct costs of materials and services consumed in developing or obtaining internal-use software,
- payroll and payroll-related costs (e.g., costs of employee benefits) for State employees who are directly associated with and who devote time to the computer software project, to the extent of time spent directly on the project. General and administrative costs, as well as overhead costs will not be capitalized by the State.
- data conversion costs may be capitalized only when considered necessary to make the software operational. An example of a capitalizable data conversion cost would be a human resources system that is dependent on the transfer of information such

as pay rates, payroll withholding data, and employee direct deposit information from the legacy system.

Post-Implementation/Operation Stage

Below are examples of costs associated with the following activities that occur during the Post Implementation/Operation Stage:

- the costs of maintenance, or costs that combine maintenance with minor upgrades whose costs cannot be easily distinguished from the costs of the maintenance.
- all training costs incurred during and after the system implementation.

Capitalization of the project's costs should begin when the Preliminary Project stage is complete and management authorizes and commits to funding the project. Capitalization should cease when a computer software project is substantially complete and ready for its intended use. A project is deemed to be ready for its intended use "after all substantial testing is completed. At this point depreciation should begin.

Note that when software projects involve multiple stages that are completed and become active at different times, each stage should be capitalized as an individual asset as it enters service.

The costs associated with modifying existing computer software should be capitalized if the modification results in increased functionality, efficiency, or estimated useful life for the software, and the costs are greater than \$100,000. The costs of routine maintenance, that does not result in increased functionality, efficiency, or estimated useful life, should be expensed.

Trademarks

Trademarks that are owned and registered by the State are also considered to be internally generated intangible assets. Trademarks are capitalized when their costs exceed \$100,000. Capitalizable costs relating to the creation of trademarks would include payments to vendors, the cost of registering the trademark, and any other direct costs incurred by the State, such as the salaries and fringe benefits of State employees directly involved in the creation of the trademark. Non-capitalizable costs relating to the creation of trademarks would include any costs incurred prior to determining the specific objective of the trademark, demonstration of the technical feasibility of creating the trademark, and demonstration of the State's ability and intention of obtaining the trademark.

Group Purchases and Unit Cost

Capital assets purchased in quantities of two or more should be capitalized only after determining the unit cost of each individual asset. State agencies should report only individual capital assets (quantities of one) under the machinery and equipment classification; *group purchases of assets should not be reported in the aggregate*. Individual assets should be reported as capital assets if the aggregate cost of the group purchase when divided by the number of units purchased results in a unit cost of more than \$15,000, and the assets have an expected useful life of at least two years following the date of acquisition. For example, the cost of each workstation acquired in a group purchase should be compared with the \$15,000 capitalization threshold requirement for machinery and equipment.

Capital Assets Composed of Multiple Units

A key consideration in defining a capital asset is the definition of an asset in cases when property is composed of a group of distinguishable sub-units such as in the following cases:

- Asset systems (should be reported as individual assets)

- Assets with associated component parts (should be reported as a single asset)
- Assets with associated attachments (should be reported as a single asset)

The State defines *asset systems* as a group of interdependent assets acquired to be used together for normal state operations. Asset systems consist of assets that can be used separately when not integrated into a system. Examples of asset systems include mainframe computer systems and telephone systems. Each asset within such a system is subject to the \$15,000 capitalization threshold. For example, two computer terminals tied into a mainframe constitute three separate assets, each subject to the \$15,000 capitalization threshold for machinery and equipment. As another example, in a telephone system composed of many individual telephone sets, each telephone set is subject to the \$15,000 capitalization threshold established for machinery and equipment.

In contrast to asset systems, an *asset with associated component parts* necessary to the functioning of the asset is considered to be all one asset when the utility of the component parts is mainly dependent on that of the asset. Associated component parts include internal parts that upgrade the performance of the primary asset, since the internal parts cannot be easily removed from the main asset for use elsewhere, and since the component parts cannot function unless they are attached to a main asset. The cost of the asset and its component parts are together subject to the \$15,000 capitalization threshold for machinery and equipment. For example, a mainframe central processing unit with a cost of \$14,000 and its associated cables with a cost of \$1,500 would qualify for capitalization since their combined cost exceeds the \$15,000 capitalization threshold for machinery and equipment. However, in the case of a security system, the wiring and backbone should be reported as part of the building, but the cameras, unless permanently attached to the building, should be reported separately as equipment. Assets with associated component parts that qualify for capitalization should be reported as one asset, and the component parts should be included in the description of the asset, when purchased and installed at the same time. Associated component parts acquired subsequent to the installation of the primary asset are considered to be separate assets, and should be capitalized if they meet the \$15,000 threshold for machinery and equipment.

For *assets with associated attachments*, attachments (i.e., assets that cannot function independently) that are purchased and put into service at the same time as the primary asset, with the intention of using the primary asset and the attachments together as a system, should be reported as part of the primary asset since their life and utility coincide with that of the primary asset's (e.g., a collator installed in a copy machine). Attachments acquired after the purchase of the primary asset, however, should not be associated with the primary asset, and therefore, should be capitalized as separate assets, if individually they meet the \$15,000 capitalization threshold for machinery and equipment.

For example, if a state agency purchases a copier with a cost of \$26,000 and a collator with a cost of \$12,000 at the same time, the assets are associated. Since their combined cost exceeds the \$15,000 threshold, the state agency should report the copier at a cost of \$38,000 with the collator included in the description of the asset.

By way of contrast, the same assets purchased at different times would not be associated, and therefore, the state agency should report the copier at a cost of \$26,000. The state agency would not report the collator, since its cost does not meet the \$15,000 capitalization threshold for machinery and equipment. Furthermore, when a state agency retires the primary asset or one of its attachments, the entire cost of the asset and its associated attachments should be retired from the inventory system. If individually, the original costs of the remaining assets meet

the \$15,000 capitalization threshold, the cost of these assets should be added back into the OAKS asset management system separately at their original cost and with the original acquisition date.

Vehicles

Vehicles that are capable of being licensed through the Department of Public Safety's Bureau of Motor Vehicles and are intended for over-the-road transportation use and costing more than \$15,000 should be capitalized. This includes trailers that are not self-propelled.

Vehicle costs include the total purchase price after any purchase discounts, plus any trade-in allowances, transportation charges, taxes, and any other costs required to prepare the vehicle for its intended use. (For a full discussion of the valuation policies regarding trade-ins, see page 18, "Exchanges or Trade-ins with Outside Parties.") Vehicles should be reported as acquisitions when the State legally takes title to the asset.

Infrastructure

Infrastructure assets are long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets. Infrastructure assets exist primarily for public use even though the State owns and manages the assets. Infrastructure assets include bridges, dams, drainage systems, lighting systems, roads, sewer tunnels, water systems, and canals.

Reporting Issues at Transition — GASB 34

In conformity with Governmental Accounting Standards Board Statement No. 34 (GASB 34), *Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments*, which first became effective for fiscal year 2002, the State reports all infrastructure assets that the Department of Transportation owns and manages, and all infrastructure assets that the Department of Natural Resources (DNR) had built or acquired after June 30, 2001. DOT and DNR are the only state agencies that qualify as having material amounts of infrastructure assets to report in the State's financial statements.

The State classifies and reports all major infrastructure assets that DOT builds and maintains in two networks, highways and bridges. OBM addresses highway- and bridge-related infrastructure reporting requirements for DOT in a separate policy document.

For retrospective reporting at transition, when GASB 34 first took effect for fiscal year 2002, the State did not report infrastructure assets that DNR acquired on or before June 30, 2001. The estimated costs of this state agency's parks and recreation network of infrastructure assets did not meet the required threshold of 10 percent of all general capital assets the State reported for the fiscal year ended June 30, 1999, in conformity with the provisions outlined in GASB 34.

Construction-in-Progress

Labor, material, equipment, and overhead costs of a project under construction (e.g., buildings and building improvements, land improvements, large software implementation projects, and infrastructure) should be temporarily reported in the account, *Construction-in-Progress*. When a project is completed, costs in this account should be transferred and allocated to one or more of the other major asset classes. A project is generally considered complete when it is ready for its intended use. Costs should be capitalized as construction work is completed. Construction for a project is complete when the building is substantially finished and occupied. This would include a building that, although technically not completely finished, is occupied under a temporary occupancy permit.

Capitalization of Interest Incurred During Construction

Financial Accounting Standards Board Statement No. 34 (FASB 34), *Capitalization of Interest Cost*, establishes standards for capitalizing interest cost as part of the original cost of acquiring certain capital assets such as buildings and sophisticated items of equipment. FASB 34 also requires disclosure of the total interest incurred and the portion capitalized. This FASB statement primarily applies to capital assets of proprietary funds. Please refer to Appendix 2 for the State's policy on "Capitalization of Interest"

Collections of Works of Art, Historical Treasures, and Similar Assets

The State owns various collections of works of art, historical treasures, and similar assets. Collections can be found at the Governor's residence, Malabar Farm (Louis Bromfield estate), which the Department of Natural Resources operates, the Ohio Arts Council, the State Library of Ohio, and the Capitol Square Review and Advisory Board. Collections at the Ohio Historical Society, which is not part of the State's financial reporting entity, belong to the society, and therefore, do not constitute state assets.

The State does not capitalize the foregoing collections of works of art or historical treasures because, in each case, the collections meet the following three criteria under GAAP, which qualify the collections for exclusion from financial reporting:

- the collection is held for public exhibition, education, or research in furtherance of public service rather than for financial gain.
- the collection is protected, kept unencumbered, cared for, and preserved.
- the collection is subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections, **or** the sales of collection items is prohibited by law.

The State does, however, report individual works of art, historic treasures, and similar assets as capital assets.

The State capitalizes real estate holdings such as land, buildings, land improvements, and related construction-in-progress that it owns but which the Ohio Historical Society uses in its operations. Such assets represent museums that house the Society's collections of works of art and historical treasures or are themselves historical treasures.

Capital Asset Costs

Purchased capital assets should be capitalized based on historical cost or estimated historical cost, if the historical cost is unknown.

Capitalized costs *include*, but are not limited to, the following:

- the purchase price of the capital asset, net of purchase discounts, plus any trade-in allowances. For a full discussion of the valuation policies regarding trade-ins, see page 18, "Exchanges or Trade-ins with Outside Parties."
- freight and handling, including shipping insurance.
- internal labor directly chargeable to a capital project that would not have been incurred during the period in the absence of activity associated with the project.

- allocation of fringe benefit expenses, calculated as a percentage of direct labor based on actual approved fringe benefit cost rates.
- installation and inspection costs.
- various fees incurred in the acquisition of land, such as title, legal commission, appraisal, closing costs and survey fees.
- external and internal architectural, engineering, and design costs directly related to the asset, including fees paid to the State Architect's Office.
- temporary relocation and rearrangement of existing machinery and equipment, and any other movable fixtures while pending completion of an improvement, renovation, or new construction.
- demolition, removal, and disposition of existing equipment or structures in preparation for a new project. The cost to remove or demolish a building or other structure existing at the time of acquisition of land, including associated clearing, filling, and leveling, with the intention of using the cleared land, is considered a part of the land's cost.
- site-preparation costs related to buildings and land improvements, such as clearing, filling, leveling, and excavating.
- insurance premiums charged during the construction phase.

Costs *excluded* from capitalization include, but are not limited to, the following:

- a permanent relocation and rearrangement of existing machinery and equipment.
- start-up time, including the cost of "debugging" problems associated with the completion of a project.
- licensing and registration fees for vehicles and operational equipment.
- costs incurred for assets not acquired, such as surveying, title searches, legal fees, and other expert services incurred for a prospective land purchase that did not transpire.
- extraordinary costs incidental to the construction of capital assets such as those due to strike, flood, fire, or other casualties, and any costs needed to fix substandard work for which the State received reimbursement.
- asbestos removal, soil remediation, and other environmental clean-ups, unless the result increases the useful economic life of the asset.
- costs related to the conceptual process involved in the selection of software, as well as training and data-conversion costs, unless the data conversion is necessary for the functioning of the new system.
- costs related to the training of personnel in the use of capital assets.
- interest costs related to assets acquired through capital leases.

- costs arising from judgments and out-of-court settlements.
- acquisition fees charged by DAS for reviewing and approving the purchase of computer software and hardware.
- maintenance costs that are identified as such.

Acquisition Methods and Valuation

Direct Purchase

Acquisition costs and costs to place the asset in use should be capitalized.

Construction

The amount capitalized for a constructed asset should include all costs incurred in constructing the asset and placing it in service. Refer to the “Capital Asset Costs” section on pages 15 and 16.

Exchanges or Trade-ins with Outside Parties

This section covers direct exchanges of assets, whether similar (e.g., assets within the same major class, such as one parcel of land for another similar parcel) or non-similar, between a state agency and a party external to the State’s primary government (i.e., vendors, non-profit organizations, general public, Ohio’s public colleges and universities, etc., which are legally separate from the State).

When no consideration is involved in the exchange of **similar** assets, the asset received should be reported at the net book value (i.e., historical cost net of accumulated depreciation) of the asset traded or exchanged. When the exchange is for **dissimilar** assets, however, the fair value of the newly acquired asset should be used for reporting the cost of the asset.

When consideration is either given or received in the exchange of **similar** assets, then the asset received should be recorded at its fair value. Fair value in this case is defined as the sum of the cash paid plus the *lesser* of either the trade-in value given for the relinquished asset or the net book value of the relinquished asset at the time of the trade. When the exchange is for **dissimilar** assets, however, fair value is defined as the sum of the cash paid plus the trade-in value of the relinquished asset at the time of the trade.

Exchanges with Other State Agencies

When a state agency transfers capital assets to another state agency, regardless of whether consideration was or was not exchanged between the two agencies, the buying/receiving agency should record the capital asset at the same net book value that the selling/donating agency recorded in its records at the time of the transfer. This is true regardless of whether the transfer involves only governmental funds, proprietary funds, or both.

Donations

Capital assets may be acquired by gift from individuals or organizations that are external to the State. In such cases, donated assets should be valued at their estimated fair value at the time of acquisition plus ancillary charges.

Capital Assets Acquired through Grants, Contributions, or Other Nonexchange Transactions

Capital assets acquired through grants, contributions, or other nonexchange transactions should be reported at historical cost or fair value and depreciated, as appropriate. Related revenues should be reported as either program revenues or general revenues in the government-wide statement of activities. When the State reports related revenues in the proprietary funds, the capital contributions should be reported after nonoperating revenues and expenses in the proprietary fund statement of revenues, expenses, and changes in fund net position.

Leased Capital Assets

All capital leases must be recorded in OAKS asset management.

- Agencies that maintain their inventory of capital assets on the OAKS asset management system are expected to enter their capital assets and the related capital leases in OAKS asset management at the time of inception of the lease.
- Agencies that do not maintain their capital assets in OAKS asset management are expected to complete an “OAKS Capital Lease Form” and send the form to DAS.AMS@DAS.OHIO.GOV at the time of the inception of the lease. The DAS Asset Management Services staff will enter the capital leases into OAKS asset management for agencies not using OAKS asset management.

The State classifies lease agreements as either capital (those which **do** meet the criteria for inclusion as capital assets) or operating (those which **do not** meet the criteria for inclusion as capital assets). A lease is an agreement between two parties in which a lessee makes periodic payments to a lessor, generally the owner, for the right to use property for a stated period of time. Installment purchases can qualify as lease agreements. Note that multi-year licensing agreements for software are not considered to be either capital or operating leases, and the software held under such agreements is considered to be a capital asset of the State.

Application of FASB 13 Criteria

The State classifies a lease as *capital* if it meets at least one of the four criteria prescribed under Financial Accounting Standards Board Statement No. 13, *Accounting for Leases*. When a lease does not meet any of the criteria, the State classifies it as an operating lease.

1. The lease transfers ownership of the property to the lessee (i.e., the state agency or the State of Ohio) during or at the end of the lease term.
2. The lease contains a bargain-purchase option. A bargain-purchase option is a provision allowing the lessee to buy the property at a very favorable price.
3. The lease term is equal to or greater than 75 percent of the estimated economic life of the leased property.
4. The present value of the minimum lease payments equals or exceeds 90 percent of the fair value of the leased property. Minimum lease payments generally equal the property rental payments excluding executory costs such as maintenance and insurance.

Criteria 3 and 4 are not applicable if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, or if the asset being leased is land.

Capital Lease Accounting

Capital assets should be capitalized at a lease’s inception.

For capital lease acquisitions involving trade-ins of capital assets, see the discussion under “Exchanges or Trade-ins with Outside Parties” on page 18.

Assignment of Historical Cost for Multiple Assets Under Lease

When a lease involves numerous assets, it is necessary to allocate the aggregate cost associated with the contract to the individual assets on a reasonable basis, if the costs of the individu-

al assets are not evident from the lease agreement. The recommended basis of allocation is to treat the individual rental costs of the assets as a component of the aggregate rental associated with the contract in a fashion similar to the approach outlined for group purchases/unit cost, as explained on page 12.

An example of how historical cost can be assigned to individual pieces of equipment covered under the same lease agreement follows.

EXAMPLE

Assume monthly rentals of the following — all are part of one contract:

Tape Drive.....	\$ 200
Central Processing Unit.....	400
Printer	300
Total monthly rental.....	<u>\$ 900</u>

The aggregate historical cost of contract at the inception of the lease as stated in the lease agreement is \$59,000.

Calculation of Individual Asset Cost = monthly rental fee for individual asset divided by the total monthly rental fee under the lease multiplied by the aggregate historical cost of the contract

Tape drive:

$$\$200/\$900 \times \$59,000 = \underline{\underline{\$13,111}}$$

Central Processing Unit:

$$\$400/\$900 \times \$59,000 = \underline{\underline{\$26,222}}$$

Printer:

$$\$300/\$900 \times \$59,000 = \underline{\underline{\$19,667}}$$

Renovations and Improvements

Renovations and Improvements

Renovations made to buildings, land improvements, machinery and equipment, and vehicles should be reported if they meet established capitalization criteria. A renovation enhances an already existing asset to a condition beyond that which results from normal maintenance or repair, and/or increases the useful life of the asset. Renovations should be reported as capital asset additions. Examples of renovations include a roof replacement or the installation of a better electrical system in a building.

Improvements are additions to buildings, land improvements, machinery and equipment, or vehicles that did not previously exist while, as defined above, renovations add to, update, or repair an existing asset. Improvements should be reported as capital asset additions separately from renovations, and although associated with an existing asset, improvements should be reported as separate capital assets. Examples of improvements include the installation of an air conditioning system in a building that did not have one previously and the placement of a color synthesizer in a black-and-white printing press to enable it to print in color.

Cost thresholds for renovations and improvements apply to each building component for a given building, or to a project for a land improvement or piece of equipment, although the project may stretch over multiple years. In these cases, the amount of the unfinished renovation or improvement should be reported as construction-in-progress until completed.

For example, a building renovation such as a new roof installation that costs \$110,000 for a building would constitute a new capital asset even if the associated project costs were to be allocated over several years. If, however, roofing costs covered two distinct buildings, with a cost of \$55,000 for each building, the roofing would not constitute a new capital asset because it would not meet the \$100,000 threshold established for the capitalization of components per individual building.

Leasehold Improvements

Renovations and improvements made to assets under non-cancellable operating leases with a term of greater than two years (i.e., leases for capital assets that do not meet the State's capitalization criteria), commonly referred to as *leasehold improvements*, should be reported when they meet the capitalization criteria established for renovations and improvements. However, the estimated useful life of a leasehold improvement cannot exceed the remaining period that the lease covers. In the case of energy efficiency projects that are managed through DAS, the leased asset should be linked to the building being renovated.

EXAMPLE

A state agency leases a floor in a 20-floor building. None of the provisions in the lease meet any one of the four capitalization criteria described in the "Leased Capital Assets" section on page 19. Accordingly, the lease falls under the category of an *operating lease*, and the state agency capitalizes no asset.

In the confines of the leased floor space of the building, the state agency installs a raised floor and secured walls to accommodate a computer. If the cost of the improvement exceeds the capitalization threshold established for such assets (i.e., greater than \$100,000 for individual classes of building components), and the improvement has an estimated useful life of two years or more that does not exceed the remaining time period covered under the lease, then the state agency should report the *leasehold improvement* as a capital asset.

Leasehold improvements should only be recorded as capital assets when the State pays for the cost of the improvement. If the lessor pays the cost of the improvement under the terms of the lease agreement, then the lessor, not the State, should report the leasehold improvement as a capital asset, even though the cost of the improvement may be passed onto the State through lease payments.

Capitalized Costs for Renovations

A renovation to a building, land improvement, piece of machinery or equipment, or vehicle should equal or exceed the capitalization thresholds for the respective asset class (i.e., greater than \$100,000 for individual classes of building components and \$15,000 for land improvements, machinery and equipment, and vehicles) before a state agency capitalizes the renovation for financial reporting purposes. If multiple renovation projects are occurring within the same building, professional judgment must be used to determine if any of the projects need to be combined when considering whether the costs meet the capitalization thresholds established for the building components that are being renovated. The timing of the start of the projects and the intent of management can help in determining whether the projects should be capitalized individually or in groups.

Generally, the capitalization threshold the State establishes for building renovations is higher because additional costs equal to or less than \$100,000 should normally be accounted for as maintenance costs.

In addition to reporting renovations that meet the required criteria for capitalization, in some instances, a state agency should also *retire* buildings or building components, land improvements, machinery or equipment, or vehicles that have undergone renovation. For example, when a state agency maintains detailed construction records from which it can identify the book value (i.e., historical cost less accumulated depreciation) of a specific section of a building under renovation, the agency should report a retirement and reduce the historical cost and the associated accumulated depreciation balance recorded for the asset.

The following steps assist state agencies in the identification of renovations that qualify for capitalization. This guidance also assists agencies in the identification of any assets that should be retired in conjunction with the renovation when detailed construction documentation supporting the cost of the specific section of a building that is being replaced is not available.

- STEP 1:* The agency should determine which components are being renovated when the renovated asset is a building that has been reported by separate building components in the capital asset records.

- STEP 2:* The agency should obtain existing data on the building component, including the original cost and any subsequent renovation costs, as currently reported in the OAKS Asset Management System at the Department of Administrative Services or the respective state agency's in-house capital asset system, for the building component or asset. When the renovation is for a building that is not reported by building component, the agency should obtain information about the original cost and any subsequent renovation costs, as currently recorded, for the entire building.

- STEP 3:* When the renovation exceeds the dollar threshold for capitalization, it should be reported as a capital asset renovation.

After determining that a renovation qualifies for capitalization, the following steps should be performed to determine whether the original building or building components under renovation should be retired.

STEP 4: The agency should apply the *dollar-approach test*, as outlined below.

The agency should locate the building's or building component's original cost and determine if the actual cost of the renovation activity is 150 percent or more of the building component's original cost plus any subsequent renovation costs. When a building is not reported by building component, the state agency should determine if the actual cost of the renovation activity is 150 percent or more of the building's original cost and any subsequent renovation costs.

EXAMPLE

A roof renovation is completed at a cost of \$240,000. The original cost of the building component that includes roofing was \$150,000. The *dollar-approach test* can be applied as follows:

$$\begin{array}{r} \text{Cost of Renovation} \\ \text{Original Cost of Component} \end{array} \quad \frac{\$240,000}{\$150,000} = \underline{\underline{160\%}}$$

STEP 5: If the actual cost of the renovation at completion is 150 percent or more of a building's or building component's original cost plus any subsequent renovation costs, the building or component should be retired at the original cost plus any subsequent renovation costs. This treatment is in line with the policies discussed in the "Retirements" section on pages 32 and 33.

The following examples illustrate how to apply the *dollar-approach test*.

EXAMPLE 1

<i>Type of Renovation</i>	Replace and Upgrade HVAC
<i>Renovation Cost</i>	\$1,232,500
<i>Original Cost of Building Component that Includes HVAC</i>	\$725,000

- a) This renovation should be capitalized, since its cost is greater than \$100,000 capitalization threshold for a building component.
- b) The original building component should be retired because the cost of the renovation is more than 150 percent of the original cost of the building component.

$$\begin{array}{r} \text{Cost of Renovation} \\ \text{Original Cost of Component} \end{array} \quad \frac{\$1,232,500}{\$725,000} = \underline{\underline{170\%}}$$

EXAMPLE 2

<i>Type of Renovation</i>	Replace and upgrade HVAC
<i>Renovation Cost</i>	\$725,000
<i>Original Cost of Building Component that Includes HVAC</i>	\$725,000

- a) This renovation should be capitalized, since its cost is greater than \$100,000 capitalization threshold for a building component.
- b) The original building component should not be retired because the cost of the renovation is less than 150 percent of the original cost of the building component.

$$\frac{\text{Cost of Renovation}}{\text{Original Cost of Component}} = \frac{\$725,000}{\$725,000} = \underline{\underline{100\%}}$$

Capitalized Costs for Improvements

An improvement is defined as an addition of a new component. An improvement should exceed the capitalization thresholds for capital assets (i.e., \$100,000 for buildings and \$15,000 for land improvements, machinery and equipment, and vehicles), and it should have an estimated useful life of at least two years following the date of acquisition.

EXAMPLE 1

Type of Improvement: A new central air conditioning system is added to a building.

Cost: \$750,000

The improvement should be capitalized since

- its cost exceeds \$100,000;
- it has an estimated useful life of at least two years following the date of acquisition; and
- it is a new component.

If similar improvements are being made to several buildings, and the cost breakdown by building is not evident, then the square footage of each building can be used to allocate the cost of the improvement.

The following example illustrates the allocation of the cost of putting a new floor into two different buildings.

EXAMPLE 2

<i>Square footage of building A</i>	100,000
<i>Square footage of building B</i>	50,000
<i>Cost of new flooring</i>	\$200,000

Improvement Cost Allocated to Building A $[(\$100,000 / \$150,000) \times \$200,000] = \underline{\underline{\$133,333}}$

Improvement Cost Allocated to Building B $[(\$50,000 / \$150,000) \times \$200,000] = \underline{\underline{\$66,666}}$

Maintenance and Repair Costs

Maintenance and repair costs should be reported as operating costs in the period incurred. These ordinary costs are either required throughout the life of an asset to keep it in efficient operating condition or for necessary repair. A discussion of some types of maintenance and repair costs follows.

- Maintenance activities (e.g., painting, minor repairs, etc.) restore an asset to its former condition or make it possible for the asset to be utilized for its estimated useful life. In other words, maintenance activities keep an asset in good working condition throughout its estimated useful life. Maintenance may be distinguished from renovations and improvements by the fact that maintenance does not extend the useful life of the asset. For example, service contracts for elevators are considered maintenance. Therefore, these kinds of costs should not be recorded separately or in conjunction with capital asset information.
- Custodial services should not be included under the category of asset maintenance. Custodial services (e.g., cleaning) or activities such as lawn mowing do not generally maintain an asset in efficient operating condition or extend an asset's useful life. Therefore, these types of costs should not be recorded separately or in conjunction with capital asset information. Appendix 3 contains additional examples to distinguish renovations and improvements from maintenance activities and custodial services.
- Rearranging and moving costs normally should be reported as operating costs in the period incurred, unless they are in conjunction with expansion or betterment of the asset, in which case they should be capitalized. For example, a building, which currently houses individuals and equipment, undergoes a major renovation. In this case, all costs of rearranging, moving, and providing temporary housing should be included in the renovation project's total cost.
- Neither the cost of permanently relocating a facility, including the cost of relocating personnel, nor the transfer of individual assets between locations should be capitalized. This is also true for a permanent rearrangement of equipment within a facility, which is not done in conjunction with an expansion or betterment.
- Administrative and executive salaries should not be capitalized even though a portion of such salary cost may be related to capital asset acquisition.
- Costs incurred for assets not acquired should not be capitalized. For example, surveying costs, title searches, legal fees, and the costs of other expert services incurred for a prospective land purchase that did not close should not be capitalized.
- Extraordinary costs incidental to the construction of capital assets such as those due to strike, flood, fire, or other casualties should not be capitalized.
- Costs of abandoned construction should not be capitalized.
- Asbestos removal costs, soil remediation, and other environmental clean-up costs should not be capitalized, except in the case when the outcome extends the useful life of the asset.

Cost Adjustments

Change in Historical Cost

When an asset's recorded cost differs from the asset's true cost, an adjustment should be reported. A difference can occur when a state agency records a cost in error or when an asset's final cost is not known with certainty or available at the time the asset is placed in service (e.g., additional preparation, project cost overruns, etc.). Cost adjustments should only be recorded when they exceed five percent of a project's total cost. When a cost adjustment is necessary, it should be reported as an adjustment when it was not made in the same fiscal year as when the capital asset was added to the inventory.

Reporting of Assets Previously Acquired But Not Previously Reported

When a state agency does not report an asset in the year of acquisition due to error or oversight, the asset should be reported as an adjustment in the fiscal year when the asset is added to the capital asset inventory.

Timing of Adjustments

Cost adjustments due to erroneous cost information should be made when identified.

Cost adjustments for additional preparation costs should be recorded

- at the time when final cost information is known, or
- in conjunction with fiscal year-end procedures for each fiscal year in which overruns or additional costs result in a change to the asset's cost basis or funding mix.

Cost Adjustments Involving Multi-Asset Projects

In applying cost adjustments to individual assets when additional costs are incurred for a multi-asset project, adjustments should be assigned to the asset(s) to which the additional cost can be directly attributed.

When a cost/object relationship is not readily apparent, the following guidelines should be observed:

- For projects, which include equipment directly purchased and placed into service with constructed assets, cost overruns should generally be allocated to the constructed assets, or
- If an asset's cost accounts for no less than 75 percent of all capitalizable costs of a project, the overrun should generally be allocated to that asset.

Allocations of Additional Cost for Two or More Assets

For allocations of additional cost or overruns to two or more assets, the existing cost of each asset should be applied as the allocation base.

The following example illustrates allocation of additional cost when the cost adjustment affects two assets.

EXAMPLE

<i>Cost of Asset A</i>	\$100,000
<i>Cost of Asset B</i>	\$50,000
<i>Cost Adjustment</i>	\$12,000
<i>Final Adjusted Cost for Asset A</i>	$\$100,000 + [(\$100,000 / \$150,000) \times \$12,000] = \underline{\$108,000}$
<i>Final Adjusted Cost for Asset B</i>	$\$50,000 + [(\$50,000 / \$150,000) \times \$12,000] = \underline{\$54,000}$

The same example could be applied to the allocation of costs by square footage of the assets involved, rather than by their costs.

Depreciation

General Policy

In keeping with the third basic statement of principle of reporting capital assets, as outlined in Section 1400 of the Codification, capital assets should be depreciated over their estimated useful lives unless they are either inexhaustible or are infrastructure assets using the modified approach. Inexhaustible assets such as land, certain land improvements, and certain buildings which represent historic treasures that are maintained in such a way that they are considered to be inexhaustible should not be depreciated. Depreciation expense should be reported in the government-wide statements of activities; the proprietary fund statement of revenues, expenses, and changes in fund net position; and the statement of changes in fiduciary net position. Corrections to errors in the reporting of accumulated depreciation should be accounted for retrospectively if considered to be material to the State's financial statements; otherwise, the errors should be corrected prospectively. Changes to depreciation resulting from changes in accounting estimates (such as the estimated useful life of an asset), or changes in accounting principle (e.g., adopting a change in the method of calculating depreciation) should be accounted for prospectively.

Accordingly, the State should depreciate capital assets reported in the following classes:

- Buildings, including improvements thereon, that are not considered to be historic treasures,
- Land improvements that are not considered to be historic treasures (i.e., exhaustible ones such as parking lots, towers, storage tanks, etc.)
- Machinery and equipment, including software, furniture and fixtures, and individual works of art and historical treasures. As discussed earlier, not all works of art and historical treasures are depreciated,
- Vehicles
- Infrastructure assets associated with state parks and other facilities that the Department of Natural Resources operates

Furthermore, the State should not depreciate capital assets reported in the following classes:

- Land
- Land improvements (i.e., inexhaustible ones such as grading, filling, grubbing, etc.)
- Construction-in-progress
- Certain state-owned buildings and land improvements that the Ohio Historical Society uses
- Highway- and bridge-related infrastructure assets that the Department of Transportation owns and manages

The State does not depreciate

- construction-in-progress because the capital asset is not complete and ready for its intended use as long as it remains under construction.

- certain state-owned buildings and land improvements that the Ohio Historical Society uses because these capital assets are considered to be historic treasures and are inexhaustible, since they are maintained in a manner that is greater than that applied to similar assets that do not have equal cultural, aesthetic, or historical value.
- highway- and bridge-related infrastructure assets that DOT owns and maintains because the State has elected to adopt the *modified approach* for reporting these assets, as more fully explained in a separate policy document that is solely applicable to these two infrastructure networks.

Depreciation reported for all governmental, proprietary, and fiduciary funds should be calculated in conformity with the methodology, conventions, and estimated useful lives and salvage values that the DAS has adopted for OAKS Assets Management System and the FleetOhio System. Depreciation should begin on the date that capital assets are placed into service, and should stop when the assets are removed from service, which may differ from the time of disposal. The only exceptions to this policy are as follows:

- The Department of Mental Health and Addiction Services (MHA) and the Department of Developmental Disabilities (DDD) should continue to calculate depreciation in conformity with the methodologies, conventions, useful lives, and salvage values prescribed for hospital assets under the federal Medicaid Program.
- Independently audited organizations can set their own depreciation policies.

State agencies must use the *straight-line method* for the calculation of depreciation. Estimated useful lives and salvage values for capital assets, as DAS has established for the OAKS Asset Management System can be found in the latest edition of “Profile I.D.s with Useful Lives”. State agencies should follow the convention of calculating annual depreciation expense using the number of months that the asset was owned during the fiscal year, including the month of acquisition and the month of retirement. See Appendix 4 for guidance on how to calculate depreciation expense and the accumulated depreciation balance.

Reporting Issues at Transition — GASB 34

In conformity with Governmental Accounting Standards Board Statement No. 34 (GASB 34), *Basic Financial Statements — and Management’s Discussion and Analysis — for State and Local Governments*, which became effective for fiscal year 2002, the State reported depreciation expense for its general capital assets for the first time.

Therefore, state agencies reported accumulated depreciation balances for their depreciable capital assets, as of July 1, 2001, so opening balances could be established for fiscal year 2002, the year of transition.

In preparation for the transition, the Office of Budget and Management (OBM) had conducted an analysis to identify active capital assets that had surpassed their estimated useful lives, as of June 30, 2000. Through this analysis, OBM found that certain vehicles reported in the FleetOhio System and the in-house capital asset system at DOT and certain buildings that DMH and DMR owned had surpassed their estimated useful lives reported in the capital asset systems just mentioned at this point in time. This finding had resulted in the establishment of revised useful life estimates for all vehicles and the extension of useful life estimates for selected building assets that DMH and DMR own. These revisions more accurately reflect the State’s experience with respect to the actual service lives of these assets than did previous useful life estimates.

Additions

Accounting Treatment for Additions

All payments a state agency makes during the fiscal year for the acquisition of capital assets on a budgetary basis (i.e., cash basis) should not be reported as expenses on the

- government-wide statement of activities
- statement of revenues, expenses, and changes in proprietary fund net position, and
- statement of changes in fiduciary fund net position

Such outlays should only be reported as changes to the capital asset account balances that are reported on the

- statement of net position at the government-wide level
- statement of net position for the proprietary funds at the fund level, and
- statement of net position for the fiduciary funds at the fund level

For a successful conversion in the Ohio Administrative Knowledge System (OAKS) from a budgetary reporting basis to a GAAP reporting basis at year-end, the Office of Budget and Management (OBM) determines the costs by program/function that should be recorded for the fiscal year as additions to the capital asset accounts on an accrual basis. Through special journal entries posted in the OAKS after year-end, OBM eliminates costs of capital asset additions normally reported in the nominal accounts on a budgetary basis, since such costs should only be recorded as changes in the real accounts established for each capital asset class.

To assist OBM with its year-end GAAP adjustments posted in the OAKS, state agencies should follow these guidelines when reporting their capital additions for the fiscal year.

- Costs of land, easements, and construction-in-progress (C-I-P) for buildings, land improvements, infrastructure, and large equipment systems being assembled over a period of time (e.g., MARCS and OAKS) should be reported as additions on a cash basis; that is, additions for these asset classes should be reported only to the extent that related disbursements had been posted in the OAKS through the June 30 cut-off date.
- Costs of machinery and equipment, vehicles, and acquisitions of existing buildings, infrastructure, and land improvements should be reported as additions on an accrual basis; that is, additions for these asset classes should be reported to the extent that a state agency has received and taken possession of these assets on or before the June 30 year-end cutoff, not necessarily when the state agency paid the vendor. If the asset is being purchased over a period of time with a number of payments (e.g., installment basis), the full cost of the asset should be reported as an addition for the same period as when the state agency takes possession of the capital asset.
- State agencies should follow OBM's guidelines on the coding of the last receipt date field on vouchers processed in OAKS. These guidelines can be found at OBM's Web site at the following address:
<http://obm.ohio.gov/StateAccounting/financialreporting/gaap.aspx>.

For C-I-P, OBM determines the necessary adjustments to correctly report additions to this asset class on an accrual basis. OBM identifies accounts payables for C-I-P by analyzing vouchers processed in the OAKS for material dollar amounts after June 30, during the subsequent months of July and August. Specifically, OBM reviews payments coded against expenditure accounts with last receipt dates indicating that C-I-P had been completed through June 30. OBM limits its review of year-end payables for adjustment purposes to C-I-P additions, since this is the only asset class likely to report material accounts payables, as of June 30, for which the corresponding costs are not included in a state agency's reported additions for the year.

In the subsequent reporting year, OBM reverses the adjustments it had identified as the previous year's costs of additions captured on the OAKS for accounts payable related to C-I-P.

In summary, OBM adjusts the cash-basis amount reported by the agencies as C-I-P additions for the fiscal year by increasing it for the accounts payable balance reported for C-I-P, as of June 30. Conversely, OBM also adjusts the cash-basis, C-I-P additions reported for the fiscal year by decreasing it for the accounts payable balance reported for C-I-P, as of the previous year-end. After OBM makes these adjustments, OBM derives the C-I-P additions on an accrual basis.

Retirements

Reasons for Retirement

A capital asset should be reported as *retired* when it is:

- scrapped or razed
- sold or traded in
- donated
- lost, stolen, or destroyed
- demolished as part of a renovation project

An asset should be retired or disposed of when it no longer serves its intended purpose. This can result from technological advances, normal wear-and-tear, destruction through natural causes, or theft. For more detailed asset retirement policies, refer to DAS guidelines and rules.

In cases where a capital asset has been damaged, such as a building damaged by flood or fire, and management intends to restore the functionality of the asset, the net book value of the portion of the asset that is being replaced should be removed from the total net book value of the asset. This amount, net of any insurance proceeds, should be reflected as a loss. Refer to the “Accounting Treatment for Retirements” section on page 33 for more details on accounting for losses on capital asset retirements. The cost to restore the asset to functionality should then be capitalized and depreciated over the remaining life of the asset.

In some cases, capital assets no longer used in one state agency may be transferred to another. Refer to the “Exchanges with Other State Agencies” section on page 18 for guidelines on such transfers.

A complete listing of retirement codes defined for the Fixed Assets Management System can be obtained from DAS.

Declaring a Capital Asset Excess or Surplus

When an agency no longer has use for a capital asset, it should be declared as excess or surplus. After such a declaration, the state agency should either transfer the capital asset to another state agency or retire it. (Refer to DAS guidelines for transferring or retiring capital assets.)

Retention of Documentation

A letter of surplus declaration or some other form of documentation on the declaration of surplus should be placed in the capital asset’s permanent file.

Expeditious Retirement

Capital assets that are no longer needed for state operations should be expeditiously identified and retired.

Authorization for Retirement

The appropriate releasing authorization, and if necessary, receiving authorization, should be obtained when a state agency retires a capital asset.

Disposition Records

Disposition records should include:

- disposition method and date
- date of sale, if sold
- sale price, if sold
- method of determining fair value, if sold

Record Retention

Records on disposed or retired assets should be maintained to comply with record retention schedules established for accounting records. If litigation involving capital assets has been initiated, the related records should be retained until the litigation is resolved.

Accounting Treatment for Retirements

A capital asset retirement should be recorded by crediting the appropriate capital asset account for the estimated historical cost of the asset, and by debiting the related accumulated depreciation account. Any net book value (i.e., historical cost less accumulated depreciation) remaining at the time of disposal should be offset against any proceeds received from the disposition of the asset to determine a gain or loss on the disposition. A gain results when proceeds received exceed the asset's book value; a loss results when the asset's book value exceeds the proceeds received.

The State does not consider proceeds from normal dispositions of personal property (i.e., machinery and equipment and vehicles) to be material enough to warrant the calculation and reporting of a gain or loss on a separate line item in the State's financial statements.

However, OBM centrally tracks the proceeds from the disposition of real estate assets, as reported on the OAKS, to judge whether such transactions do result in material gains or losses for the State. In cases when OBM judges the gains on dispositions of real property to be material for financial reporting purposes, it reclassifies the revenues associated with the proceeds from the *program revenue* category reported for the program/function assigned to the state agency receiving the sale proceeds to the *general revenues* classification reported in the government-wide statement of activities.

When no material gains or losses result from the disposition of capital assets, depreciation expense should be credited or debited for the net gain or loss, respectively.

Replacement

For an asset replacement, the original asset replaced should be reported as a retirement, and the replacement should be reported as a capital asset addition.

Impairments

Definition of Impairment

According to Governmental Accounting Standards Board Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries* (GASB 42), an asset impairment is a *significant, unexpected decline in the service utility* of an asset. The term, *significant*, refers to the magnitude of the impairment when compared to the service utility of the asset. An *unexpected decline* refers to a decline in the net book value of an asset that exceeds that expected through accumulated depreciation. *Service utility*, in turn, is defined as the usable capacity that an asset was expected to provide at acquisition.

Determination of Impairment

The determination of whether a capital asset has been impaired is a two-step process. First, capital assets that have experienced events or changes in circumstances that could potentially indicate impairment are identified. Then, assets so identified are tested to determine if actual impairment has occurred. In GASB 42, the GASB emphasizes that the events or changes in circumstances that indicate potential impairment should be self-evident, and consequently, known as a matter of course. In other words, **state agencies are not expected to go to any special or extraordinary effort to identify capital assets that are potentially impaired.**

On the basis of materiality and the expected insignificant impact on the State's government-wide financial statements, OBM only applies GASB 42's provisions to land, land improvements, buildings, construction-in-progress, and infrastructure holdings at the major state agencies listed below, and OBM will not attempt to apply GASB 42 to machinery and equipment or vehicles.

- Office of the Adjutant General
- Department of Administrative Services
- Department of Mental Health and Addiction Services
- Department of Developmental Disabilities
- Department of Natural Resources
- Department of Public Safety
- Department of Rehabilitation and Correction
- Department of Transportation
- Department of Youth Services
- Ohio School for the Blind
- Ohio School for the Deaf

The five most common indicators of potential impairment, as defined by GASB 42 and which are not mutually exclusive or exhaustive, are as follows:

- Physical damage to the capital asset, such as by fire or flood, that requires restoration efforts to restore the asset's service utility;
- Enactment of laws or legislation, or other changes in environmental factors, that limit or curtail the use of the capital asset because the asset does not meet and cannot be modified to meet the requirements of the new laws or situation, such as underground storage tanks that do not meet new EPA requirements;
- Technological or other developments that render the capital asset obsolescent or obsolete, causing the asset to be used much less frequently, or not at all, such as a piece of medical equipment that has become less useful because new equipment is more efficient or effective;
- A change in the manner of use of a capital asset or a change in the estimated useful life of the asset, such as closing a school prior to the end of its estimated useful life because of a decline in enrollment; and
- Halting construction-in-progress prior to the completion of the asset perhaps due to budgetary problems, or a change in circumstances that eliminates the need for the asset that is being constructed.

A decrease in the use of a capital asset is **not**, in and of itself, considered a potential sign of asset impairment if it is not associated with one of the five indicators listed above.

Agencies need to assess capital assets in inventory, which have been identified as being potentially impaired by association with one of the five indicators of impairment, to determine whether the assets in question meet **both** of the following criteria, which identify *actual*, as opposed to *potential*, impairment.

- The magnitude of the decline in service utility is significant, meaning the expense, (including depreciation) associated with continued operation of the asset, or the cost of restoration of the asset, is significant in relation to the current service utility of the asset, and
- The decline in service utility of the capital asset is unexpected, meaning the decline in useful life or the cost of restoration is outside of the reasonable range of expectations usually associated with the asset.

If both of these criteria are met, the capital asset should be considered to be impaired. Impairments are considered to be permanent in nature, unless evidence demonstrates that the impairment is only temporary. An example of a temporary impairment would be the closure of a school due to a decline in enrollment, if it can be demonstrated that the decline is only temporary, and that the school will be reopened at a future date. Temporary impairments do not result in a change in the carrying value of the asset (i.e., historical cost, or fair value at the date of donation, less accumulated depreciation).

Calculating the Amount of Impairment

Under GASB 42, the amount of the impairment for capital assets that are permanently impaired and remain in service must be calculated, net of any insurance recoveries, and recognized as an expense in the State's government-wide statement of activities. The carrying value of the asset must also be decreased by the calculated amount of the asset's impairment.

GASB 42 also requires that capital assets that are impaired and are taken out of service permanently should be carried at the lower of carrying value or fair value, with no further recogni-

tion of annual depreciation expense. Capital assets that are taken out of service temporarily, however, continue to be listed at carrying value, and the recognition of annual depreciation expense should be suspended until the assets are placed back into service.

GASB 42 discusses several different methodologies for calculating the amount of a capital asset's impairment. The methodology employed depends largely on which of the five indicators of potential impairment, as discussed above, apply to the asset.

- The **restoration cost approach**, under which the amount of the impairment is derived from the estimated cost to restore the utility of the capital asset to its original state, exclusive of any costs attributable to improvements or additions. The estimated restoration cost can be converted to historical cost either by deflating the restoration cost by using a historical cost index, or by taking the ratio of the estimated restoration cost to the current replacement cost of the asset. The result can be applied to the carrying value of the asset to calculate the amount of the impairment.
- The **service units approach** identifies the historical cost of the service utility of the capital asset that cannot be used due to the impairment. The amount of the impairment is calculated by comparing the value of the service unit potential of the asset before and after the impairment occurred.
- The **deflated depreciated replacement cost approach** calculates the estimated replacement cost for an asset which is no longer being used for the purpose for which it was originally intended. This replacement cost can be depreciated and deflated to match the age of the original asset. The difference between the resulting depreciated, deflated replacement cost, and the carrying value of the original asset represents the impairment loss.

The relationship between the types of impairment and the methodology used to calculate the impairment is examined below.

Type of Impairment	Method used to Calculate The Amount of the Impairment
Physical Damage	Restoration cost approach
Changes in legal or environmental factors	Service units approach
Technological change or obsolescence	Service units approach
Change in manner or duration of use	Service units approach or Deflated depreciated replacement cost approach

Note that when the impairment involves a permanent cessation of construction-in-progress, asset should be carried at the lower of carrying value or market value.

Reporting Issues at Transition – GASB 42 Implementation

GASB 42 became effective for the fiscal year ended June 30, 2006. For the implementation of this standard's provisions for fiscal year 2006, OBM requested information on impairments and assets that have been removed from service through June 30, 2005. This was done so that

OBM could identify any necessary beginning balance adjustments to net position reported in the government-wide financial statements, for the fiscal year ended June 30, 2006.

Annually, OBM will continue to request information on impairments and assets that have been removed from service from these state agencies. On the basis of information provided, OBM will determine the appropriate method for calculating the amount of the impairment, and perform the actual calculation.

- report the changes in the net book values of impaired capital assets resulting from these calculations and the identities of such assets to either the OAKS asset management group at DAS or to the capital asset coordinators at the respective state agencies that do maintain their own capital asset inventory reporting systems, as appropriate, so that the net book value of the impaired assets can be properly adjusted and reported.
- provide the identities of capital assets removed from service to either the OAKS asset management group at DAS or to the capital asset coordinators at the respective state agencies that do maintain their own capital asset inventory reporting systems, as appropriate, so that the annual depreciation expense will no longer be calculated for the assets.

OBM will limit its calculations to apply only to assets with a net book value at the time of impairment of at least \$5 million.

Capitalization of Pollution Remediation Outlays

Definition of Pollution Remediation

In November 2006, the GASB issued Governmental Accounting Standards Board (GASB) Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations (GASB 49)*. The Office of Budget and Management (OBM) implemented the accounting and financial reporting provisions of this new accounting standard for fiscal year 2009.

As defined in GASB 49, a pollution remediation obligation is “an obligation to address current or potential effects of existing pollution by the means of various pollution remediation activities.” The Statement assumes that the State will be aware of an incident whereby a site has become polluted. GASB 49 does not apply to potential pollution remediation activities that could be required upon the retirement of an asset in the future, nor does it apply to current pollution prevention or control activities. It also does not apply to fines, penalties, or civil torts.

The State will determine whether it has incurred a pollution remediation obligation by way of an **obligating event** and will recognize a liability for pollution remediation only when an obligating event has occurred.

GASB 49 defines an obligating event as one of the following:

- The State is compelled to take action due to an imminent danger to public health or the environment.
- The State has violated a pollution prevention-related permit or license.
- The State has been named, or is likely to be named, by a regulatory agency as a responsible party or as a potentially responsible party to conduct or pay for pollution remediation activities.
- The State has been named, or is likely to be named, in a lawsuit that seeks to compel it to undertake or pay for pollution remediation activities.
- The State voluntarily obligates itself to conduct or pay for pollution remediation activities.

Once the State has recognized the existence of an obligating event, the State must report a pollution remediation liability to the extent that the liability is measurable. This liability includes the anticipated direct costs of all activities related to the pollution remediation effort, whether short-term or long-term, for any or all of the following:

- Pre-cleanup activities including site assessment, site investigation, corrective measures feasibility study, and remediation plan;
- Cleanup activities and site restoration;
- External oversight and enforcement-related activities that are chargeable to the State; and
- Operation and maintenance of the remedy, including postremediation monitoring.

For purposes of this liability calculation, direct costs consist of salaries and benefits, materials, equipment, capital assets, legal services (excluding legal costs related to seeking recovery of pollution remediation costs from other parties), and any other professional services. However, the liability does not include indirect costs (i.e., overhead) or payments for fines, penalties, and civil torts arising from exposure to toxic substances.

As the liability becomes measurable, the State will recognize the total amount of the estimated pollution remediation liability and related expense, net of any cost recoveries, in the government-wide financial statements and in the enterprise fund financial statements. In the governmental fund financial statements, the State will recognize expenditures for pollution remediation activities, net of any cost recoveries that are measurable and available, only to the extent that the costs are incurred during the current fiscal year and are expected to be paid with expendable, available financial resources.

Acquisition of Capital Assets Relating to Pollution Remediation

In certain circumstances, pollution remediation costs are reported as capital assets, as described below:

- Pollution remediation costs are incurred to prepare a property for sale. Costs may be capitalized only for the portion necessary to increase the carrying value of the property to the estimated fair value of the property after removal of the pollution.
- Pollution remediation costs are incurred to prepare property for use when the property was known or suspected to be polluted when acquired. Costs may be capitalized only for the portion necessary to prepare the property for its intended use.
- Pollution remediation costs are incurred to repair and restore a pollution-caused decline in service utility that was previously recognized as a capital asset impairment. Costs may be capitalized up to the amount necessary to place the asset in its intended location and condition, i.e., the fair market value of similar assets.
- Costs are incurred to acquire property, plant, and equipment for pollution remediation that have an alternate future use. In this case, costs may be capitalized only for the amount of estimated service utility remaining after pollution remediation activities are complete.

In these cases, a capital asset will be recognized by the State in the government-wide financial statements and in the enterprise fund financial statements, rather than a liability and expense.

On the basis of materiality and the expected insignificant impact on the State's government-wide financial statements, OBM only applies GASB 49's provisions to the major state agencies listed below.

- Office of the Adjutant General
- Department of Agriculture
- Department of Administrative Services

- Department of Mental Health and Addiction Services
- Department of Developmental Disabilities
- Department of Natural Resources
- Department of Public Safety
- Department of Rehabilitation and Correction
- Department of Transportation
- Department of Youth Services
- Environmental Protection Agency

Reporting Issues at Transition – GASB 49 Implementation

GASB 49 became effective for the fiscal year ended June 30, 2009. For the implementation of this standard's provisions for fiscal year 2009, OBM requested information from the agencies listed above on pollution remediation liabilities that existed as of June 30 of 2007, 2008, and 2009. This was done so that OBM could identify any necessary beginning balance adjustments to net position reported in the government-wide financial statements, for the fiscal year ended June 30, 2009, as well as make any changes needed to the comparisons reported in the Management's Discussion and Analysis section of the CAFR.

OBM will limit its requests for information to only those instances that report estimated pollution remediation liabilities of at least \$5 million.

Internal Controls for Capital Assets

Control Objectives

In conformity with the guidelines established under the State's Internal Accounting Control Program (IACP), state agencies should meet the following general internal control objectives for capital assets.

- Only authorized and needed property should be procured.
- Property acquisitions should be recorded timely and accurately in source documents and accounting records.
- Detailed subsidiary records should be maintained for individual capital assets and should be periodically reconciled with control accounts.
- Periodic physical verification should be made of the existence and condition of property.
- Physical security measures should be commensurate with the size, type, and value of property.
- Issues, transfers, retirements, and losses should be reported and accounted for timely.
- Assets should be properly requisitioned and used exclusively for state government activities.
- Capital asset records should be accurately maintained.
- Adequate segregation of duties should exist among functions affecting the control and reporting of capital assets.

State agencies should institute internal accounting controls to provide a means of meeting control objectives for capital assets. Internal control is designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes 1.) the cost of a control should not exceed the benefits likely to be derived, and 2.) the valuation of costs and benefits requires estimates and judgments by management.

The following discussion focuses on some recommended internal control procedures over capital assets.

Acquisitions and Dispositions

State agencies should establish policies and procedures that are clearly defined to govern the acquisition and disposals of capital assets.

Capital asset acquisitions and dispositions should be recorded in the state agency's property control records as events occur. Employees responsible for maintaining property control records should be promptly notified when capital asset acquisitions, dispositions, or other activities have occurred.

For construction, renovation, and large repair projects, state agencies should utilize the services of the Division of General Services at DAS. State agencies should also have procedures in place to ensure that all capital assets are fully utilized and obsolete ones are disposed of

through the DAS Office of State and Federal Surplus Property. Excess real property should be reported to the DAS Office of Real Estate Services and the DAS Office of State Inventory and OAKS Asset Management.

Identification Numbers and Tagging Procedures

Each capital asset a state agency acquires should be assigned a number to uniquely identify it among all other assets. Identification numbers allow state agencies to access all information related to specific assets.

Except as listed below, all capital assets, including equipment that may be “built into” or installed in a building (e.g., heavy maintenance machinery), should be appropriately identified with tags visibly affixed.

State agencies should issue sequential asset identification tags and account for the sequence of tags issued (i.e., no duplicates or breaks in the number sequence used). To improve accountability, assets should be tagged on the date that they are received or placed into service with the tag number cross-referenced on supporting documentation. Additionally, asset tags should be replaced when damaged or lost; previously tagged equipment with missing tags may be retagged with the originally assigned identification number.

Tagging procedures should be in conformity with procedures outlined in the DAS General Services Division’s “State of Ohio Property Inventory Policies and Procedures” document. Bar code inventory labels or comparable electronic medium should meet standards of the DAS Division of Computer Information System’s.

The following classes of capital assets do not require tags: land, buildings, land improvements, vehicles, construction-in-progress, and infrastructure.

Employees responsible for the agency’s capital asset accounting records should control the tagging of assets.

Condition and Location

Data gathered on each asset during a physical inventory should include an asset’s condition and location. Location need not be verified for buildings. A condition assessment should be based on the physical appearance of the asset. Ideally, all changes in an asset’s condition should be reported as they happen.

Safeguarding of Assets

The following techniques are specifically deigned to physically safeguard capital assets.

- Controlled access to all buildings
- Employee identification card and visitor login requirements for secured areas
- Established procedures to protect all assets, including files and records, from potential fire and water damage
- Checkout procedures for capital assets most susceptible to theft (e.g., audio-visual equipment, laptop computers, etc.)
- Proper segregation of duties to ensure employees responsible for
 - property control do not engage in the purchasing, receiving, or expenditure processing functions
 - custody of capital assets do not have access to property control records

- maintaining property control records do not take the physical inventory of capital assets
- Accurate tracking of capital assets in the property records and regular, periodic physical inventories

Required Physical Inventory

Section 125.16, Ohio Revised Code, requires state agencies to complete a physical inventory of all tangible personal property each biennium. Physical inventory-taking procedures should be thorough and well documented.

State agencies should compare and reconcile the results of their physical inventory with their property records to permit a timely investigation and resolution of significant differences and to further enhance control and accountability. Discrepancies noted during the physical inventory should be reported to the employee responsible for inventory control and to upper management.

Physical Inventory Reports

The following represents information that should appear on a physical inventory report.

- Date of last physical inventory for each asset
- A list of all equipment items missing since the previous inventory, including tag number, description, original location from where the item is missing, historical cost, and cause, if known
- A certification statement, which the individual prepares and signs each time there is a physical inventory and/or review of an inventory for a group of capital assets. The statement should be completed at the end of each inventory and should identify the inventory taker or reviewer, the date, and a reference to any exceptions identified. The physical inventory results, whether recorded on a master inventory listing or separate reports, should be attached to a copy of the certification statement to the Department of Administrative Services as supporting documentation.

Special Physical Inventory

In addition to the regularly scheduled biennial physical inventory, a special physical inventory may be taken of all capital assets when

- a different person assumes responsibility for the location or department.
- an organizational change occurs affecting the distribution of the equipment assigned to a particular location.
- a special request is made for a physical inventory.

Missing Assets

Assets may be missing for several reasons, including theft, unrecorded transfers, and loans of equipment. State agencies should pursue explanations for missing equipment when possible, and they should undertake efforts to locate missing assets. If theft is suspected, state agencies should notify the State of Ohio Highway Patrol.

Data-Collection Process for State's Capital Assets

OAKS and FleetOhio

OAKS asset management at DAS maintains capital asset information for most state agencies. Section 125.16, Ohio Revised Code, assigns DAS the stewardship responsibility for the State's capital assets. OAKS manages inventory records for the State's capital assets other than licensed vehicles and highway- and bridge-related infrastructure assets. The FleetOhio System manages inventory records for the State's vehicles.

Independent Property Management Systems Operated by State Agencies

Annually, state agencies that maintain their own property management systems and have been exempted from maintaining inventory records on OAKS should submit accurate property information to OBM, including detailed activity reports at the asset record level. These reports should list the following types of asset activity during the fiscal year:

- Additions
- Retirements/Deletions
- Transfers Between State Agencies
- Cost Adjustments
- Ending Balance of Active Assets

Beginning with state fiscal year 2002, OBM requests that agencies, which operate their own property management systems, also include the annual depreciation expense and the accumulated depreciation balance through June 30, as part of the asset record detail on the activity reports. This information assists the State in complying with the reporting requirements under GASB 34.

In addition to the activity reports requested by OBM as discussed above, DAS requires state agencies that operate their own property management systems to submit a summary of inventory activity on the DAS Annual Certification of State Property Inventory Form. The base cost totals for this report must reconcile with base cost figures reported on the detailed activity reports. The following summary of information should be included on the DAS certification:

- Active Beginning Balance (should agree with the ending balance reported for the previous fiscal year)
- Additions
- Retirements/Deletions
- Transfers Between State Agencies
- Adjustments (e.g., changes in base cost, retirement reversals, changes to retirement dates, reclassifications, etc.)
- Ending Balance of Active Assets

Assignment of Funding Source Codes

State agencies should report the respective OAKS fund(s) from which capital asset acquisitions had been financed. Funding source code 999, was used for all capital assets (other than high-

way- and bridge-related infrastructure at the Department of Transportation) that state agencies acquired prior to the July 1, 1987. With the advent of OAKS asset management, funding source codes such as 999 that do not exist as legitimate funds in OAKS can no longer be used; therefore, GRF will be used in place of 999. Similarly, donated assets cannot be coded with a funding source code of DON, but instead should also be coded as GRF. In order to identify those capital assets that have been donated to the State, DAS will prepare a report for OBM specifically to identify donated capital assets.

In cases when a state agency has capital assets acquired since July 1, 1987 and the funding source is not known, the default funding source code assigned to the assets should be GRF.

Recommended Data Elements for Capital Asset Records

The following data should be maintained for each capital asset record, as may be applicable.

- Agency*
- Funding source (OAKS fund)
- Major asset class
- Asset class
- Description of asset
- Square feet or acreage
- Voucher number
- Method of acquisition
- Purchase order or requisition number
- Acquisition date (should be flagged when estimated)
- Valuation method (e.g., actual or estimated historical cost, fair value)
- Vendor name and address
- Set-up date
- Change date
- Assigned tag number
- Manufacturer name
- Model number/identifier
- Serial number
- Location(s)

- Estimated useful life
- Estimated salvage value
- Date of disposition
- Method of disposition
- Authorization of disposition

*This data element permits OBM to report fixed assets by function.

Financial Reporting Requirements

Basic Financial Statements

In the government-wide statement of net position, capital assets that are

- being depreciated or have been depreciated should be reported, net of accumulated depreciation, and
- not being depreciated, such as land or infrastructure assets using the modified approach, should be reported separately from assets being depreciated, since the State has a significant amount of such assets.

This requirement applies to governmental activities, business-type activities, and component units, which consist of the Air Quality Development Authority, Ohio Facilities Construction Commission, Broadcast Education Media Commission, the Ohio Capital Fund, and the state-assisted universities and state community colleges. The same information for capital assets should also be reported in the proprietary funds' statement of net position in the fund financial statements.

For governmental activities, business-type activities, and component units, total capital assets, net of accumulated depreciation and any outstanding balances of bonds, mortgages, notes, or other borrowings attributable to their acquisition, construction, or improvement, should be reported as net investment in capital assets on the statement of net position at the government-wide level. The same information for capital assets should also be reported in the proprietary funds' statement of net position in the fund financial statements.

Notes Disclosures

Accounting standards require governments to provide detail in the notes to the financial statements about capital assets of the primary government reported in the statement of net position. The information disclosed should be divided into major classes of capital assets as well as between those associated with governmental activities and those associated with business-type activities. Capital assets that are not being depreciated should be disclosed separately from those that are being depreciated.

Information presented about major classes of capital assets should include:

- Beginning- and end-of-year balances (regardless of whether the government presents beginning-of-year balances on the face of the government-wide financial statements), with accumulated depreciation presented separately from historical cost.
- Capital acquisitions
- Sales or other dispositions
- Current-period depreciation expense, with disclosure of the amounts charged to each of the functions in the statement of activities

For collections not capitalized, disclosures should provide a description of the collections and the reasons these capital assets are not capitalized.

For capital assets that have been permanently or temporarily impaired and as a result have been removed from service at June 30, the net book value of such assets should be disclosed. For capital assets that have become permanently impaired and remain in service, as of June

30, the calculated amount of the impairment, the expenditure function to which the impairment is charged, a general description of the impairment, and the amount of any related insurance recoveries must be disclosed.

Determining whether to provide similar disclosures about capital assets of discretely presented component units is a matter of professional judgment. The decision to disclose should be based on the individual component unit's significance to the total of all discretely presented component units and that component unit's relationship with the primary government. At a minimum, the State should present similar disclosures on capital assets for its major component units.

In the notes to the financial statements, the State should disclose the following information on capital assets, collections of works of art and historical treasures for the primary government.

Changes in Capital Assets

Capital asset activity, for the year ended June 30, 20XX, was as follows (dollars in thousands):

Governmental Activities:	Balance July 1, 20xx	Increases	Decreases	Balance June 30, 20xx
Capital Assets, not being depreciated:				
Land	\$ xxx,xxx	\$ x,xxx	\$ x,xxx	\$ xxx,xxx
Land Improvements (Historical Treasures)	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Buildings (Historical Treasures)	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Construction-in-Progress	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Infrastructure:				
Highway Network:				
General Subsystem	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Priority Subsystem	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Bridge Network	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Total Capital Assets not being depreciated	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Other Capital Assets:				
Buildings	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Land Improvements	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Machinery & Equipment	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Vehicles	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Infrastructure:				
Parks Recreation, and Natural Resources- Network	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Total Other Capital Assets, at historical cost	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Less: Accumulated Depreciation for:				
Buildings	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Land Improvements	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Machinery & Equipment	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Vehicles	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Infrastructure:				
Parks Recreation, and Natural Resources Network	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Total Accumulated Depre- ciation	xxx,xxx	x,xxx	x,xxx	xxx,xxx

Other Capital Assets, net	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Governmental Activities Capital Assets, net.....	\$ xxx,xxx	\$ x,xxx	\$ x,xxx	\$ xxx,xxx

Depreciation Expense

Depreciation expense was charged to program/function of the primary government as follows (dollars in thousands):

Governmental Activities:

Primary, Secondary, and Other Education	\$x,xxx
Higher Education Support	x,xxx
Public Assistance and Medicaid.....	x,xxx
Health and Human Services.....	x,xxx
Justice and Public Protection	x,xxx
Environmental Protection and Natural Resources	x,xxx
Transportation	x,xxx
General Government.....	x,xxx
Community and Economic Development	x,xxx
Total Depreciation Expense — Governmental Activities	x,xxx
Gains/(Losses) on Capital Asset Disposals Included in Depreciation.....	x,xxx
Fiscal Year 20XX Increases to Accumulated Depreciation	\$x,xxx

At June 30, 20XX, the State considered the following governmental capital asset balances as being temporarily or permanently impaired and removed from service.

Governmental Activities:

Temporarily Impaired Assets Removed from Service:	
Buildings.....	\$x,xxx
Land Improvements.....	x,xxx
Total	\$x,xxx
Permanently Impaired Assets Removed From Service:	
Buildings.....	\$ x,xxx
Land Improvements.....	x,xxx
Total	\$x,xxx

Business-Type Activities:	Balance July 1, 20xx	Increases	Decreases	Balance June 30, 20xx
Capital Assets, not being depreciated:				
Land	\$ xxx,xxx	\$ x,xxx	\$ x,xxx	\$ xxx,xxx
Construction-in-Progress.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Total Capital Assets, not being depreciated.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Other Capital Assets:				
Buildings.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Land Improvements.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Machinery & Equipment	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Vehicles.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Total Other Capital Assets at Historical Cost.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx

Less: Accumulated Depreciation for:				
Buildings.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Land Improvements.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Machinery & Equipment	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Vehicles.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Total Accumulated Depreciation.....	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Other Capital Assets, net	xxx,xxx	x,xxx	x,xxx	xxx,xxx
Business-Type Activities Capital Assets, net.....	\$ xxx,xxx	\$ x,xxx	\$ x,xxx	\$ xxx,xxx

Depreciation expense was charged to the following business-type functions as follows (dollars in thousands):

Business-Type Activities:	
Workers' Compensation.....	\$x,xxx
Lottery Commission.....	x,xxx
Tuition Trust Authority	x,xxx
Liquor Control.....	x,xxx
Office of Auditor of State	x,xxx
Total Depreciation Expense for Business-Type Activities	x,xxx
Gains/(Losses) on Capital Asset Disposals Included in Depreciation.....	x,xxx
Fiscal Year 20XX Increases to Accumulated Depreciation.....	\$x,xxx

Similar disclosures will be made for the discretely presented component units that OBM considers to be significant to its financial statements.

Collections of Works of Art and Historical Treasures

The State owns various collections of works of art and historical treasures. Collections can be found at the Governor's residence, Malabar Farm (Louis Bromfield estate), which the Department of Natural Resources operates, the Ohio Arts Council, the State Library of Ohio, and the Capitol Square Review and Advisory Board. Collections at the Ohio Historical Society, which is not part of the State's financial reporting entity, belong to the society, and therefore, do not constitute state assets.

The State does not capitalize the foregoing collections of works of art or historical treasures because, in each case, the collections meet the following three criteria under GAAP, which qualify the collections for exclusion from financial reporting:

- the collection is held for public exhibition, education, or research in furtherance of public service rather than for financial gain.
- the collection is protected, kept unencumbered, cared for, and preserved.
- the collection is subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections, or the sales of collection items is prohibited by law.

Appendix 1 — Building Components and Allocation of Construction Costs

Effective for the fiscal year ended June 30, 2002, the State has elected to simplify its classification schematic for building components upon the advice and assistance of the State Architect's Office. Instead of allocating the costs of a new building into the 10 separate component categories, as outlined in the State's previous accounting and financial reporting policies for fixed assets, dated June 30, 1994, state agencies should distribute these costs into the two new building component categories, *General Construction* and *Other Construction*, and the land improvement component category, *Site Utilities*, as appropriate.

The Department of Mental Health and Addiction Services (MHA), the Department of Developmental Disabilities (DDD), and the independently audited state agencies are exempted from this requirement for the following reasons:

- MHA and DDD follow the accounting and financial reporting standards required for hospital assets under the federal Medicaid Program.
- Independently audited organizations can set their own accounting and financial reporting policies for capital assets.

State agencies should not reclassify building components reported in OAKS or in-house capital asset systems through June 30, 2001. This means, building component costs assigned to the 10 original categories or, under the *General Construction* category in cases when a categorization by building component was not possible, should continue to be reported in these categories. The 10 original building component categories and their features are listed below.

Building Component	Features
1. General Construction	basic construction components, such as foundation wall, interior foundations, slab on ground, framing, exterior wall, and structural floor
2. Site Preparation	cleaning, grading, installing public utilities, etc.
3. Roof and Drainage	roof covering materials and roof drainage
4. Interior Construction	interior finish of the building, such as floor finish, ceiling finish, wall partition materials and finishes
5. Plumbing	general plumbing; fixtures and installation of such items as sinks, lavatories, drinking fountains, bathtubs, showers, urinals, water heaters, etc.

Building Component	Features
6. Heating, Ventilation, and Air Conditioning (HVAC)	system for heating, ventilating, and cooling a building (e.g., furnace, boiler, and rooftop packaged units)
7. Electrical	electrical services including wiring and lighting
8. Fire Protection, Life Safety	sprinkler systems, manual fire alarm systems, and automatic fire detection systems
9. Elevators	elevators and elevator landings
10. Miscellaneous	features such as emergency generators, intrusion alarm systems, electric doors, fire escapes, public address systems, etc.

With a few adjustments, the two new building component categories retain the character of the *General Construction* component and aggregate all remaining components into the *All Other Construction* component. Site preparation costs associated with the construction of a building should now be reported as a land improvement, *Site Utilities*, rather than being included as part of the cost of the building.

The State Architect's Office has also provided the following percentage breakdown for allocating the cost of constructing or buying a *standard* building, and agencies may use this breakdown when reporting their building costs.

Building Component	Features
General Construction— accounts for <i>30 percent of a standard building's cost</i>	The basic construction components, such as foundation, slabs, framing, basement, exterior walls and windows, basement walls, structural floor, and asbestos removal.
All Other Construction— accounts for <i>60 percent of a standard building's cost</i>	Roof covering materials and roof drainage. Interior finish of the building, such as floor finish, ceiling finish, wall partition materials and finishes, and interior and exterior doors. General plumbing such as fixtures and installation of such items as sinks, lavatories, drinking fountains, bathtubs, showers, urinals, water heaters, etc. Systems for heating, ventilating, and cooling a building, such as furnaces, boilers, and rooftop-packaged units. Electrical services including wiring and lighting. Sprinkler systems, security systems, manual fire alarm systems, automatic fire detection systems, and emergency generators. Elevators and elevator landings, and escalators.
Land Improvements— accounts for <i>10 percent of a standard building's cost</i>	Site utilities, such as water lines, natural gas lines, and electrical lines that are buried in the ground.

General costs associated with the entire contract, such as insurance, bid and performance bonds, scheduling, supervision, close-out, punch list work, general conditions, architect, engineer, and construction manager fees, etc., should be allocated among the various building components in the percentages described above.

State agencies that have questions about how to categorize industry-regulated formatting for specification-writing and construction-costing of Divisions 1 through 16 into the State's building components may call the Financial Reporting Section of the Office of Budget and Management for guidance.

Appendix 2 — Capitalization of Interest

Capitalization of Interest Costs During Construction

Financial Accounting Standards Board Statement No. 34, *Capitalization of Interest Cost*, requires the capitalization of material interest charges incurred when constructing a capital asset or preparing it for its intended use. It also requires disclosure of the total interest incurred and the portion capitalized. FASB 34 provisions only apply to the State's capital assets reported in the *proprietary and fiduciary funds*.

Reasons for Capitalizing Interest

The primary reasons for capitalizing interest costs are to obtain a measure of acquisition costs that reflects the State's total investment in an asset and to charge costs that relate to a resource that will benefit future periods.

Qualifying Assets

Capital assets that qualify for interest capitalization require a period of time to be prepared for their intended use and provide a benefit in future periods.

Amount Capitalized

The *net* amount of interest should be capitalized for qualifying assets. Specifically, FASB Statement 62, *Capitalization of Interest Cost in Situations Involving Certain Tax-Exempt Borrowings and Certain Gifts and Grants*, stipulates that the amount of interest incurred on indebtedness directly associated with acquiring, constructing, and/or otherwise readying a qualifying asset for use, should be reduced by the amount of interest revenue earned.

Interest revenue can be earned through the investment of the proceeds of the related indebtedness and any other available construction funds before the funds are spent for construction. Any excess of interest revenue earned over interest costs should reduce the capitalized value of qualifying assets.

Proprietary and fiduciary fund types should report an adjustment for capitalized interest costs as a debit to the construction-in-progress account and a credit to the interest expense account.

Appendix 3 — Comparison of Costs for Renovations and Improvements, Maintenance, and Custodial Activities

Renovation or Improvement	Maintenance	Custodial
See the “Fundamentals for Identifying Capital Assets” section. Renovations and improvements are capital assets, if they meet the criteria.	Allows the asset to provide service to the State for its estimated useful life. Does not extend the useful life. Maintenance costs should not be capitalized.	Does not affect the usefulness or estimated useful life of the asset. Custodial costs should not be capitalized.
Examples:	Examples:	Examples:
Replace a worn-out roof on a building by tearing off the old roof and installing a new one	Annually, tar a roof to prevent leakage and premature deterioration	Periodically sweep the roof to remove rubbish
Add a color synthesizer to a printing press to enhance its capabilities	Replace small parts or perform general servicing to make the press work properly	Purchase 10 reams of paper and boxes of ink for the press
Remove old insulation and add new insulation to the walls of a building to enhance heating capabilities and efficiency	Place weather stripping around windows before winter to stop heat leakage	Wash windows and walls periodically
Resurface a parking lot due to deterioration	Patch holes in the surface to maintain a flat surface	Periodically clean, collect litter, sweep, etc.
Carpet an entire floor of a building not previously carpeted	Shampoo the carpet of an entire floor to maintain appearance	Clean a spot on a carpet caused by spills and periodically vacuum
Replace regular windows in a building with passive solar windows for greater energy efficiency	Replace a broken window with a new one	Wash windows to maintain visibility

Appendix 4 — Calculation of Annual Depreciation Expense and Accumulated Depreciation

In line with the State's accounting and financial reporting policies described under the "Depreciation" section of this document, the following five examples illustrate how the State calculates annual depreciation expense and accumulated depreciation.

These examples do not necessarily illustrate the depreciation methods applied to capital assets at the Department of Mental Health and Addiction Services (MHA), Department of Developmental Disabilities (DDD), and independently audited organizations. MHA and DDD calculate depreciation in conformity with the methodologies, conventions, useful lives, and salvage values prescribed for hospital assets under the federal Medicaid Program while the independently audited organizations follow their own prescribed policies on depreciation.

General Assumptions: The fiscal year is 2010, the straight-line method of depreciation is used, salvage value is zero, and the depreciation convention is based on the number of months the asset has actually been held, including the month of acquisition and the month of disposal.

EXAMPLE 1

FACTS:

<u>Acquisition Date</u>	<u>Estimated Useful Life in Months</u>	<u>Original Cost</u>	<u>Accumulated Depreciation, as of 6/30/09</u>
April 2007	60	\$60,000	\$27,000

The capital asset has a depreciation expense of \$1,000 a month.

$$\$60,000 \text{ cost} \div 60\text{-month estimated useful life} = \$1,000 \text{ a month}$$

The capital asset did not reach the end of its estimated useful life by 6/30/10; the depreciation expense for fiscal year 2010 is \$12,000.

$$\$1,000 \text{ a month} \times 12 \text{ months} = \$12,000 \text{ depreciation expense for FY 10}$$

The accumulated depreciation balance, as of 6/30/10, increases to \$39,000.

$$\begin{array}{r}
 \$27,000 \text{ accumulated depreciation, beginning @ 6/30/09} \\
 + \underline{12,000 \text{ depreciation expense for FY 10}} \\
 \hline
 \underline{\underline{\$39,000 \text{ accumulated depreciation, ending @ 6/30/10}}}
 \end{array}$$

The net book value of the capital asset, as of 6/30/10, is \$21,000.

$$\begin{array}{r}
 \$60,000 \text{ original cost of capital asset} \\
 - \underline{39,000 \text{ accumulated depreciation, ending @ 6/30/10}} \\
 \hline
 \underline{\underline{\$21,000 \text{ net book value of capital asset @ 6/30/10}}}
 \end{array}$$

EXAMPLE 2

FACTS:

<u>Acquisition Date</u>	<u>Estimated Useful Life in Months</u>	<u>Original Cost</u>	<u>Accumulated Depreciation, as of 6/30/09</u>
January 2010	60	\$30,000	\$0, since capital asset was acquired in FY 10

The capital asset has a depreciation expense of \$500 a month.

$$\text{\$30,000 cost} \div \text{60-month estimated useful life} = \text{\$500 a month}$$

The state agency owned the capital asset for six months in fiscal year 2010, including the month of acquisition; the depreciation expense for fiscal year 2010 is \$3,000.

$$\text{\$500 a month} \times \text{6 months} = \text{\$3,000 depreciation expense for FY 2010}$$

The accumulated depreciation balance, as of 6/30/10, increases to \$3,000.

$$\begin{array}{r} \$ \quad 0 \text{ accumulated depreciation, beginning @ 6/30/09} \\ + \quad 3,000 \text{ depreciation expense for FY 10} \\ \hline \end{array}$$

$$\underline{\underline{\$ \quad 3,000 \text{ accumulated depreciation, ending @ 6/30/10}}}$$

The net book value of the capital asset, as of 6/30/10, is \$27,000.

$$\begin{array}{r} \$30,000 \text{ original cost of capital asset} \\ - \quad 3,000 \text{ accumulated depreciation, ending @ 6/30/10} \\ \hline \end{array}$$

$$\underline{\underline{\$27,000 \text{ net book value of capital asset @ 6/30/10}}}$$

EXAMPLE 3

FACTS:

<u>Acquisition Date</u>	<u>Estimated Useful Life in Months</u>	<u>Original Cost</u>	<u>Accumulated Depreciation, as of 6/30/09</u>
October 2005	36	\$72,000	\$72,000

The capital asset has a depreciation expense of \$2,000 a month.

$$\text{\$72,000 cost} \div \text{36-month estimated useful life} = \text{\$2,000 a month}$$

The capital asset, which is still in service, as of 6/30/10, had reached the end of its estimated useful life by the end of the previous fiscal year; the depreciation expense for fiscal year 2010 is \$0.

(Continued)

EXAMPLE 3 (Continued)

The accumulated depreciation balance, as of 6/30/10, remains at \$72,000.

$$\begin{array}{r} \$72,000 \text{ accumulated depreciation, beginning @ 6/30/09} \\ + \quad \underline{\quad 0 \text{ depreciation expense for FY 10}} \\ \hline \underline{\underline{\$72,000 \text{ accumulated depreciation, ending @ 6/30/10}}} \end{array}$$

The net book value of the capital asset, as of 6/30/10, is \$0.

$$\begin{array}{r} \$72,000 \text{ original cost of capital asset} \\ - \quad \underline{\underline{72,000 \text{ accumulated depreciation, ending @ 6/30/10}}} \\ \hline \underline{\underline{\$ \quad 0 \text{ net book value of capital asset @ 6/30/10}}} \end{array}$$

EXAMPLE 4

FACTS:

<u>Acquisition Date</u>	<u>Estimated Useful Life in Months</u>	<u>Original Cost</u>	<u>Accumulated Depreciation, as of 6/30/09</u>	<u>Disposition Date for Capital Asset</u>
October 2006	48	\$36,000	\$24,750	September 2009

The capital asset has a depreciation expense of \$750 a month.

$$\$36,000 \text{ cost} \div 48\text{-month estimated useful life} = \$750 \text{ a month}$$

The state agency owned the capital asset for three months in fiscal year 2010, including the month of disposal, before it was disposed of; the depreciation expense for fiscal year 2010 is \$2,250.

$$\$750 \text{ a month} \times 3 \text{ months} = \$2,250 \text{ depreciation expense for FY 10}$$

The accumulated depreciation balance at 6/30/10 is \$0, since the capital asset had been disposed of and was not held in inventory, as of 6/30/10.

At the point of disposal in September 2009, the net book value of the capital asset was \$9,000.

$$\begin{array}{r} \$36,000 \text{ original cost of capital asset} \\ - \quad 24,750 \text{ accumulated depreciation, beginning @ 6/30/09} \\ - \quad \underline{\underline{2,250 \text{ depreciation expense for FY 10}}} \\ \hline \underline{\underline{\$ \quad 9,000 \text{ net book value of capital asset at disposition}}} \end{array}$$

EXAMPLE 5

FACTS:

<u>Acquisition Date</u>	<u>Estimated Useful Life in Months</u>	<u>Original Cost</u>	<u>Accumulated Depreciation, as of 6/30/09</u>	<u>Ending Date of Estimated Useful Life</u>
April 2007	36	\$54,000	\$40,500	March 2010

The capital asset has a depreciation expense of \$1,500 a month.

$$\$54,000 \text{ cost} \div 36\text{-month estimated useful life} = \$1,500 \text{ a month}$$

The state agency owned the capital asset through its entire estimated useful life, which expired in March 2010; depreciation expense for fiscal year 2010 is \$13,500.

$$\$1,500 \text{ a month} \times 9 \text{ months} = \$13,500 \text{ depreciation expense for FY 10}$$

During March 2010, the accumulated depreciation balance increases to \$54,000. At this point, the asset is fully depreciated, since it had reached the end of its estimated useful life.

$$\begin{array}{r} \$40,500 \text{ accumulated depreciation, beginning @ 6/30/09} \\ + \underline{13,500 \text{ depreciation expense for FY 10}} \end{array}$$

\$54,000 accumulated depreciation through March 2010

The net book value of the capital asset at the end of its estimated useful life in March 2010 is \$0. This balance would be reported, as of 6/30/10, if the state agency continues to use the capital asset in its operations and reports it in its inventory, as of 6/30/10.

$$\begin{array}{r} \$54,000 \text{ original cost of capital asset} \\ - \underline{54,000 \text{ accumulated depreciation through March 2010}} \\ \hline \underline{\underline{\$ \quad 0 \text{ net book value of capital asset}}} \end{array}$$

GLOSSARY

ABANDONMENT — The disposal or retirement of an asset due to complete deterioration or lack of usefulness. This occurs when an asset ages and the wear-and-tear either renders it useless or maintenance costs become excessive. An example of abandonment would be a large dump truck after 20 years needing repair every 10 days; the truck eventually becomes inoperative.

ACCUMULATED DEPRECIATION — The accumulation of systematic and rational allocation of the estimated cost of using capital assets (i.e., depreciation), on a historical cost basis, over their estimated useful lives.

ADDITION — The acquisition of a capital asset through purchase, construction, donation, or capital lease. The asset is acquired for use in the course of a state agency's normal operations, not with the intent to resell or consume the asset (e.g., supplies).

ADJUSTMENTS — Any change to the cost of a capital asset. Adjustments can result when cost errors are corrected or additional costs are incurred after the initial purchase of the asset to place it in working order (e.g., constructing a slab to support the weight of a large machine).

ASSET NUMBER — The number (alpha-numeric code) assigned to a capital asset to uniquely identify the asset among all other assets. The number should consist of a series of letters and/or numbers that may vary slightly depending on the class of asset and the method used to identify it. The asset number can be used to access and report data specific related to the asset.

ASSET SYSTEM — A group of interdependent assets acquired to be used together in the normal operations of the State. Asset systems consist of assets that could be used separately if they were not integrated into a system. Examples of asset systems are mainframe computer systems and telephone systems. For financial reporting, each asset within the system is subject to a \$15,000 capitalization threshold.

AUDITABLE — Records and documentation should be maintained in an orderly and accessible manner (i.e., transactions filed by fiscal year) to enable internal and independent auditors to conduct an examination and render an opinion on the financial statements. All records should be maintained in this manner.

BETTERMENT — See **IMPROVEMENTS**.

BUILDING — Buildings are permanent structures designed with a foundation and roof and may or may not be enclosed with walls. Buildings may be broken down into components, which can be recorded as individual assets. All buildings costing more than \$15,000 are capitalized. Prefabricated structures that can be easily emplaced and displaced (e.g., with a crane) and that do not require a foundation should be reported as land improvements. Buildings are subject to depreciation, with the exception of certain buildings the Ohio Historical Society operates, and buildings owned by DOT that are considered to be part of the highway infrastructure.

CAPITAL ASSETS — Land, land improvements, easements, buildings, building improvements, vehicles, machinery, equipment, works of art and historical treasures, infrastructure, and all other tangible and intangible assets that are used in operations and

that have initial lives extending beyond a single reporting period (i.e., at least two years following the date of acquisition).

CAPITALIZATION THRESHOLD — The dollar value at which the State elects to capitalize tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period (i.e., at least two years following the date of acquisition).

CAPITAL LEASE — An agreement between an agency and lessor whereby the agency makes periodic payments for the use of an asset in its normal operations. The terms of the lease are such that the agency in effect “owns” the asset. If a lease has **any one** of the following four characteristics, as outlined in Financial Accounting Standards Board Statement No. 13, *Accounting for Leases*, then it is considered a capital lease:

1. The lease transfers ownership of the property to the lessee (the agency or the State) during or at the end of the lease term.
2. The lease contains a bargain purchase option. A bargain purchase option is a provision allowing the lessee to buy the property at a very favorable price.
3. The lease term is equal to or greater than 75 percent of the estimated economic life of the leased property (does not apply to land).
4. The present value of the minimum lease payments equals or exceeds 90 percent of the fair value of the leased property (does not apply to land). Minimum lease payments generally equal the property rental payments excluding executory costs such as maintenance and insurance.

Criteria 3 and 4 are not applicable if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, or if the asset being leased is land.

Assets acquired under a capital lease arrangement are subject to the capital asset capitalization criteria for determining whether they should be reported as capital assets.

COMPONENT — One part of a group of separate parts that make up a capital asset. A component can be a single piece of equipment that is part of an asset system, or one of the building components as described in Appendix 1.

CONSTRUCTION — Building a structure by contracting an outside contractor or using one of the three construction agencies in the State, as opposed to buying or leasing a structure that is already completed. When a building is constructed, the total cost should be broken down into building components. Construction costs include all incidental costs necessary to place the asset into working order (i.e., materials, labor, licenses, fees, legal costs, etc.) and are accounted for as *construction-in-progress* until the structure is accepted for its intended use. Construction-in-progress is not subject to depreciation. Construction-in-progress can also apply to large software installation and modification projects.

DEPRECIATION EXPENSE — The method of systematically allocating the cost of a tangible capital asset over its estimated useful life. When capital assets are depreciated, the expense is charged against fund operations.

DISPOSAL — The abandonment or retirement of a capital asset. A state agency that sells, donates, or disposes of a capital asset must report the disposal as a retirement.

DONATION — Acquisition of a capital asset for nothing in return. This pertains to assets given to an agency at no cost or at a nominal amount to fulfill legal requirements. The asset is valued at the fair value of similar assets at the time of donation.

EASEMENT — The legal right to have access to or through a parcel of land without having ownership of the land. Such rights may include the right to erect or affix an asset to the land or buy an asset below the surface of the land. In cases where the State has granted an easement to an outside party on land that the State owns, if the easement is of such a character that it prevents the State from using the land for the State's purposes, then the land should be removed from the State's capital asset inventory.

ESTIMATED HISTORICAL COST — An estimate of a capital asset's price. An estimate may be derived from vendor price lists or catalogs, similar assets, staff estimates, vendor invoices, purchase orders, canceled checks, or appraisals. Estimated historical cost is used only when actual historical cost is unavailable.

ESTIMATED USEFUL LIFE — The period of time an asset is expected to operate efficiently for its designed purpose.

EXCESS — A capital asset that a state agency no longer needs. Excess assets may be transferred to another agency or retired.

FAIR VALUE — Value of an item in accordance with its relative sales value at the time of acquisition. Fair value can be derived from vendor catalogs, invoices for similar assets, or appraisals. Fair value should be used to value *donated* capital assets.

FIDUCIARY FUNDS — Funds used to report assets held in a trustee or agency capacity for others and which therefore cannot be used to support the government's own program. The fiduciary fund category includes pension trust funds, investment trust funds, private-purpose trust funds, and agency funds.

FISCAL FUNDING CLAUSE — Term used in connection with capital leases. A clause in a lease agreement that generally provides that the lease is cancelable if the legislature or other funding authority does not appropriate the funds necessary for a governmental unit to fulfill its obligations under the lease agreement.

FUNCTION — A group of related activities aimed at accomplishing a major service or regulatory program for which a government is responsible (e.g., general government, transportation, etc.).

FUND — A fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, that are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.

FUND FINANCIAL STATEMENTS — Basic financial statements presented on the basis of funds. Term used in contrast with *government-wide financial statements*.

FLEETOHIO — The fleet management information system that maintains property information on vehicles. The system provides accountability and allows for the efficient management, acquisition, and disposal of vehicles.

GAIN OR LOSS ON THE DISPOSAL OF CAPITAL ASSETS — The difference between the net book value of a capital asset at the time of disposal of the asset and the proceeds, if any, from the disposal of the asset. If the proceeds from the disposal of a capital asset are greater than the net book value of the asset, a gain occurs. If the proceeds from the disposal of a capital asset are less than the net book value of the asset, a loss occurs. As used in this definition, the term, proceeds, includes not only cash received from the sale of a capital asset, but also any trade - in value given for a capital asset.

GENERAL REVENUES — All revenues that are not required to be reported as program revenues. All taxes, even those that are levied for a specific purpose, are general revenues and should be reported by type of tax. All other nontax revenues (including interest, grants, and contributions) that do not meet the criteria to be reported as program revenues should also be reported as general revenues.

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP) — The conventions, rules, and procedures that serve as the norm for the fair presentation of financial statements.

GENERALLY ACCEPTED GOVERNMENT AUDITING STANDARDS (GAGAS) — Standards for the conduct and reporting of both financial and performance audits in the public sector. The General Accounting Office promulgates GAGAS through its publication, *Government Auditing Standards*, commonly known as the *Yellow Book*.

GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB) — The ultimate authoritative accounting and financial reporting standard-setting body for state and local governments.

GOVERNMENTAL ACTIVITIES — Activities generally financed through taxes, intergovernmental revenues, and other nonexchange revenues. These activities are usually reported in governmental funds and internal service funds.

GOVERNMENTAL FUNDS — Funds generally used to account for tax-supported activities. There are five different types of governmental funds: the general fund, special revenue funds, debt service funds, capital projects funds, and permanent funds.

GOVERNMENT-WIDE FINANCIAL STATEMENTS — Financial statements that incorporate all of a government's governmental and business-type activities, as well as its nonfiduciary component units. There are two basic government-wide financial statements: the statement of net position and the statement of activities. Both basic government-wide financial statements are presented using the economic resources measurement focus and the accrual basis of accounting.

HISTORICAL COST — The original cost incurred to acquire a capital asset and place it in service in the normal operations of the agency. Cost includes amounts paid or value assigned (in the case of a donated asset) and any incidental costs incurred to place

the asset into service, such as freight, installation charges, preparation of the area in which the asset is operated, demolition costs, etc.

IMPAIRMENT OF CAPITAL ASSETS — Asset impairment is a *significant, unexpected decline in the service utility* of an asset. The term, *significant*, refers to the magnitude of the impairment when compared to the service utility of the asset. An *unexpected decline* refers to a decline in the net book value of an asset that exceeds that expected through accumulated depreciation. *Service utility*, in turn, is defined as the usable capacity that an asset was expected to provide at acquisition.

IMPROVEMENT — An addition made to, or change made in, a capital asset, other than maintenance, to prolong its life or to increase its efficiency or capacity. The cost of the addition or change is added to the book value of the asset. Improvements can be separated into two categories: 1.) additions to a previously existing asset, and 2.) replacement of a component of a building or item of equipment with a new part having significantly improved and superior performance. In each case, the result tends to enhance the overall efficiency of the asset and increase the useful life. Improvements must be separately identified from normal maintenance and upkeep. Improvements are subject to depreciation. Any costs made to keep an asset operating at its normal capacity or preventing it from prematurely deteriorating, are considered maintenance and are not to be added to the value of the asset. An example of an improvement would be taking out an old engine from a truck and replacing it with a newer, bigger one. An example of maintenance costs would be the replacement of the oil, spark plugs, and antifreeze in either the old or the new engine.

INFRASTRUCTURE — Long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets. Examples of infrastructure assets include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, tunnels, canals, and lighting systems. Buildings, except those that are an ancillary part of a network of infrastructure assets, should not be considered infrastructure assets.

INSTALLMENT PURCHASE — A purchase method calling for payment to be made in periodic installments. Transfer of ownership occurs at the time of the purchase, although this method delays the recognition of expense until payments are made. Some capital leases are in effect installment purchases.

INTANGIBLE ASSETS — A capital asset that possess all of the following characteristics:

- The asset lacks physical substance
- The asset is nonfinancial in nature, i.e., is not cash, investments, receivables or prepayments
- The asset has an estimated useful life of more than one year.

Examples of intangible assets include software, easements, rights to access assets related to land that the State does not own, such as water rights, timber rights, gas rights, mineral rights, oil rights, patents, trademarks, etc.

NET INVESTMENT IN CAPITAL ASSETS — One of three components of net position that must be reported in both government-wide and proprietary fund financial statements. Net, for this purpose, includes the outstanding balances of any bonds, mortgages, notes, or other borrowings, including capital leases, that are attributable to the acqui-

tion, construction, or improvement of capital assets of a government. Note that the amount of related debt used in this calculation does not include any unspent debt proceeds.

LAND — Real property recorded individually by “parcel.” All land, regardless of cost, is capitalized. This account includes costs incurred in preparing land for use (e.g., razing of structures). The land is recorded as a capital asset separate from any improvements made to it. Land is not subject to depreciation.

LAND IMPROVEMENTS — Improvements made to land such as parking lots, sidewalks, retaining walls, yard lighting, fencing, etc. Land improvements are often associated with land on which State buildings are located. Land improvements differ from infrastructure in that the general public primarily use infrastructure assets, while the State primarily uses land improvements in the operations of the State. Only improvements costing more than \$15,000 and having an estimated useful life of at least two years following the date of acquisition should be reported as land improvements in the State’s financial statements. Land improvements may or may not be subject to depreciation, depending on the nature of the land improvement. Inexhaustible land improvements such as grading, filling, or grubbing would be examples of land improvements that are not subject to depreciation. Prefabricated structures that can be easily emplaced and displaced (e.g., with a crane) and that do not require a foundation should be reported as land improvements. Land improvements are subject to depreciation, with the exception of certain land improvements the Ohio Historical Society operates.

LEASE — An agreement entered into by a state agency whereby periodic payments are made for the right to use an asset, such as computers, copiers, and vehicles. (See the “Leased Capital Assets” section, beginning on page 19.)

LEASE/PURCHASE — A lease agreement entered into whereby the ownership of the asset being leased transfers to a state agency at some time during or at the end of the lease.

LEASEHOLD IMPROVEMENT — A capitalizable improvement or renovation to an asset covered under an operating lease if the lease is noncancellable and has a term of greater than two years. The improvement becomes the property of the lessor at the end of the lease term. The improvement should be considered an asset of the State while the lease is in effect, even though the original asset being leased is not considered to be an asset of the State. The useful life of the leasehold improvement must not exceed the remaining period that the lease covers. Leasehold improvements are capitalized by the State when the State pays directly for the cost of the leasehold improvement.

LESSEE — The party who leases property from the lessor.

LESSOR — The owner of property that is leased to the lessee.

LOSS — The involuntary disposal of a capital asset due to fire, flood, theft, vandalism, etc.

MACHINERY AND EQUIPMENT — Tangible property of a more-or-less permanent nature, other than land or buildings and improvements thereon (e.g., machinery, tools, trucks, and furnishings). Machinery and equipment assets with a cost of more than \$15,000 and an estimated useful life of at least two years following the date of acquisition

should be capitalized in the State's financial statements. Examples of equipment include printing presses and computers. Equipment is subject to depreciation. This account includes costs incurred in the acquisition of machinery and equipment (e.g., transportation cots).

MAINTENANCE — The normal repairs and upkeep performed on an asset to keep it operating in good working condition. Such repairs do not prolong the life of the asset, but merely keep it operating properly. Consequently, maintenance costs should not be capitalized.

MATERIALITY — The magnitude of an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement.

MODIFIED APPROACH — The election not to depreciate infrastructure assets that are part of a network or subsystem of a network that meet two specific requirements. First, the government manages the eligible infrastructure assets using an asset management system that has certain specified characteristics; second, the government documents that the eligible infrastructure assets are being preserved approximately at (or above) a condition level established and disclosed by the government.

NET BOOK VALUE — The difference between the historical cost of an asset and its accumulated depreciation at a given point in time.

OAKS ASSET MANAGEMENT — The property management system, which maintains property information for the State. As part of its primary function, OAKS maintains information on the State's capital assets in accordance with generally accepted accounting principles. The system improves control, financial reporting, accountability, and operational efficiency in managing capital assets. Complete and accurate records aid management in budget planning and help management to identify under-utilized assets, that is, assets that should be replaced or modified.

OPERATING LEASE — Any lease agreement that gives a state agency the right to use a specific asset or group of assets for a period of time. At the end of the term, the asset is returned to the vendor from whom it was leased. Operating leases do not meet any of the four criteria for capital leases discussed on page 19. Consequently, assets held under operating leases should not be capitalized.

PARCEL OF LAND — Any measurement of land acquired with a single deed. If a deed is not accessible, then a parcel of land may consist of the total number of acres associated with a facility. This can be an acre, a square mile, 200 acres, etc. A parcel represents a single asset.

PRIMARY GOVERNMENT — Term used in connection with defining the financial reporting entity. The primary government (e.g., the State of Ohio) is the focus of the financial reporting entity.

PROGRAM — Group activities, operations, or organizational units directed to attaining specific purposes or objectives.

PROGRAM REVENUE— Term used in connection with the government-wide statement of activities. Revenues that derive directly from the program itself or from parties outside

the reporting government's taxpayers or citizenry, as a whole; they reduce the net cost of the function to be financed from the government's general revenues.

PROPRIETARY FUNDS — Funds that focus on the determination of operating income, changes in net position (or cost recovery), financial position, and cash flows. There are two different types of proprietary funds: enterprise funds and internal service funds.

PURCHASE — Acquiring an asset by paying for it, exchanging another asset for it, or a combination of the two. Writing a check, paying cash, assuming a mortgage, entering into a capital lease arrangement, and trading-in an old asset are all examples of methods for purchasing an asset. Purchases are limited to acquisition of assets delivered and placed into service in the condition they were received (i.e., already complete, not requiring construction). Minor assembly in the case of equipment does not constitute construction.

RENOVATION — Construction performed on an already existing building, land improvement, or item of equipment to enhance its usefulness. Renovation also includes replacement of destroyed portions (e.g., fire damaged rooms). Renovations should be capitalized when they have an estimated useful life of at least two years following the date of acquisition, and cost \$15,000 or more for equipment and land improvements or \$100,000 or more for building components.

RETIREMENT — The disposal, abandonment, or disappearance of a capital asset.

SALE — Disposal of a capital asset in exchange for some consideration. Examples of consideration are cash or another asset.

SPARE PARTS — Small parts of a larger capital asset that are used to replace broken parts and maintain the asset in working order. The use of a spare part to replace a broken part does not increase the useful life of the main asset. Spare parts may be obtained by purchase or by removal from capital assets that are no longer functional. The replacement of a broken part with a spare part does not change the net book value of the capital asset. Spare parts should not be capitalized, and are not to be confused with associated component parts or associated attachments.

SUPPORTING DOCUMENTATION — Documents or materials to substantiate the purchase and/or disposal of a capital asset. The documentation should provide evidence in support of the cost used to value an asset. Included as supporting documentation are vouchers, purchase orders, receiving slips, contracts, mortgages, leases, titles of ownership, etc.

SURPLUS — An asset no longer of any use to the State. Surplus assets should be expeditiously retired.

TAG — An identifier attached to certain assets. A tag contains an asset number used to uniquely identify this asset among all other assets similar and dissimilar.

TRANSFER — The physical movement of an asset or change of responsibility for an asset from one state agency to another.

VEHICLE — Vehicles, including renovations and improvements thereon and trailers that are not self-propelled, that cost more than \$15,000 and are capable of being licensed

through the Department of Public Safety's Bureau of Motor Vehicles for intended over-the-road transportation use are considered to be capital assets. Vehicles are subject to depreciation.

WORKS OF ART AND HISTORICAL TREASURES — Assets such as paintings, sculptures, historical manuscripts and books, and antiques that are held individually, and that are maintained or preserved. The State does not capitalize collections of works of art or historical treasures. Historical buildings and museums and associated land improvements operated by the Ohio Historical Society are also considered to be historical treasures, and are capitalized by the State, but are not depreciated. Works of art that are permanently attached to a building are considered to be part of the building and are depreciated with the building.