June 17, 2021

ACTION: **First and Final Round Approval of Revisions to Board Policy 7002; Capitalization; Definitions and Classifications**

Board Policy 7002 is being revised to update and incorporate the new GASB 87 requirements for the financial reporting of leases. As the update for the GASB was being reviewed, additional areas were updated to clarify capitalization requirements of certain projects and dollar thresholds were revised for inflation and increased construction costs.

The policy has been reviewed by the college comptrollers, the Council of Business Officers, and the Council of Presidents. The proposed changes are recommended for approval.

The System Office recommends approval of the Revisions to Board Policy 7002; Capitalization; Definitions and Classifications.

ATTACHMENTS:

- Revisions to Board Policy 7002 (PDF)

BOARD POLICY

Asset -- Type and Classification

			Expected Life *
1.	Land		N/A~~--~~
2.	Buildings		
	a.	~~Major~~ Buildings and Structures	50 years
	~~b.~~	~~Minor Buildings and Structures~~	~~25 years~~
	~~c~~b.	Building Improvements/Renovations	35 years
3.	Improvements Other Than Buildings		
	a.	Utility Generation and Distribution Systems	30 years
	b.	Fences	10 years
	c.	Landscaping ~~Improvements~~	20 years
	~~d.~~	~~Digital or lighted signs~~	~~10 years~~
4.	Equipment		
	a.	Heavy Equipment	10 years
	b.	Autos, Vans, and Other Passenger Vehicles Used in Motor Pool	3 years
	c.	Trucks, Busses, and Cargo Vehicles	8 years
	d.	Mowers, Skid Steer, Toolcat, and Other Grounds Equipment	5 years
	e.	Computer Equipment	3 years
	f.	Miscellaneous Educational Materials Stored on Computer-Related Equipment/Devices	3 years
	g.	Specimens, Collections, and Library Holdings	**~~--~~
	h.	Leases	**~~--~~
	i.	Office Furnishings	7 years
	j.	Used Equipment	3 years
	k.	All Equipment Not Specifically Defined in Other Classifications	10 years
5.	Intangible Assets		10 years
6.	Construction Work in Progress		N/A~~--~~

~~(~~*"Expected Life" is a reference to the depreciable life of an asset. A fixed asset, which has been capitalized, shall remain in the College's capital asset accounts net of accumulated depreciation until disposed of.~~)~~
**"Expected Life" varies depending on the criteria as noted in the Equipment section.

Depreciation Method

The depreciation method used will be straight-line beginning with the month of purchase, donation, or substantial completion.

1. **Land**

Land will be capitalized at acquisition cost including assessments, commissions, legal and recording fees; draining, filling, other site preparation costs; judgments levied from damage suits; and demolition cost of structures on land acquired as building sites. Land acquired by gift will be measured and capitalized at acquisition value. Acquisition cost of property, which includes structures not to be razed, will be allocated between land and buildings based on appraised values.

2. **Buildings**

a. ~~Major~~ Buildings and Structures

1) Acquisition by Construction

Initial capitalization includes initial construction costs of the building structure, including all internal piping, wiring, and permanent fixtures associated with the distribution of utilities within the building. Cost should also include architect fees, inspection fees and permits, bid advertising, any bond issuance costs and insurance costs incurred during the construction period. Exclude costs of landscaping, sidewalks, utility tunnels, or furnishings which are to be capitalized in other fixed asset accounts. The cost of constructing a building of less than five hundred thousand dollars ($500,000) should be charged to expense unless capitalization/reporting is required by bond or lease purchase agreement covenants.

2) Acquisition by Purchase

Buildings acquired by outright purchase will be capitalized at acquisition cost with proportionate allocation of the purchase price and associated closing costs allocated to land on the basis of current fair market values.

3) Building Additions

Additions are extensions, enlargements, or expansions made to an existing asset. Additions are capitalized and depreciated over 50 years because they are considered extraordinary or major alterations. If an addition project exceeds five hundred thousand dollars ($500,000), then the project costs should be added to the capitalized value of a building. Any addition project of less than five hundred thousand dollars ($500,000) should be charged to expense as long as the cost does not exceed twenty-five percent (25%) of the building cost before the addition is built. Also, work done on the existing asset to accommodate the addition should be regarded as part of the cost of the addition and capitalized. Examples of additions are extra floor space added to a building, the addition of an air conditioning system to an office, the addition of pollution control devices, the addition of attached ramps, the addition of truck docks, the addition of fire escapes, and other appurtenances.

~~b. Minor Buildings and Structures~~

~~Capitalization and renovation policy would be the same as (a) above, except this classification would consist of any building whose value exceeds one hundred thousand dollars ($100,000) and is less than five hundred thousand dollars ($500,000) and may include the following: garages, sheds, greenhouses, and shops. Buildings whose value is less than one hundred thousand dollars ($100,000) should be expensed.~~

b. Building Improvement/Renovation

Capital improvements should be distinguished from ordinary repairs that are expenses that maintain the existing asset in normal operating condition and should be expensed immediately.

Ordinary repairs are recurring in nature and are normally small relative to the value of the asset; they do not materially add to the use of the asset, and do not substantially extend its operational life. Examples of ordinary repairs include replacing minor parts, janitorial and utility services, and care of grounds.

Improvements and replacements are substitutions of a part of an asset for another. While replacement is the substitution of an asset of basically the same type and performance capabilities, improvement is the substitution of a better asset with superior performance capabilities. Replacements are considered as ordinary repairs and maintenance and are expensed as opposed to capitalized. The example of a replacement expense is replacing an old carpet with a new one. The replacement will not increase the service life of the building to which the original cost of the old carpet was added.

Major renovation and remodeling that involves updating a building interior for the purpose of enhancing functionality, and extending the useful life (i.e. sprinklers and fire alarms, data (telephone)/electrical wiring systems within the building, heating, ventilation and air conditioning (HVAC) systems) will be capitalized if the renovation ~~when~~ is viewed as a single project:

1) ~~e~~Exceeds five hundred thousand dollars ($500,000). ~~and t~~
2) The project objective and scope includes modernization of the structure as a whole, and not merely a rearrangement of selective office/classroom areas.
3) In the event a renovation project involves significant razing of the existing structure, an estimate of the cost of initial construction, which was razed, should be removed from the existing building asset valuation.
4) Office furnishings of renovations should be capitalized separately from any structural renovation costs.

A ~~S~~special maintenance project, undertaken primarily to preserve or enhance the general appearance should be charged to expense (i.e. ~~C~~costs of repairs ~~and updates of~~ or replacement of roofs, ~~;~~ painting, caulking, tuck pointing, etc.). ~~sprinklers and fire alarms; data (telephone)/electrical wiring systems within the building; and heating, ventilation and air conditioning (HVAC) systems should be considered building improvement/renovation costs.~~

3. **Improvements Other Than Buildings**

The following classifications of improvements will be capitalized:

a. Utility Generation and Distribution System

Includes cost of utility generation systems within power plant structures, as well as equipment for transmission of utilities from one location to another but does not include equipment and transmission lines for utilities contained within a building for its own use. (Utility Distribution Systems within a building structure, i.e., internal piping and wiring, are capitalized as part of the building cost.) This account includes the installed cost of equipment used in the generation of heat, power, steam, electricity, and cooling; the cost of constructing utility tunnels; as well as any equipment, switchgear, piping, and wiring housed in the tunnels. Includes costs on sanitary and storm sewers, electrical transmission lines and similar type equipment.

Cost includes actual equipment, related transportation costs and installation costs, as well as any legal or other fees, licenses, surveying, equipment rental, or other such costs incurred in connection with the installation of the facilities. Additions or extensions to existing utility generators and distribution capacity will be capitalized in the year such addition was completed.
Utility Generation and Distribution System projects will be capitalized if the project exceeds two hundred ~~and~~ fifty thousand dollars ($2~~0~~50,000). Repairs and related maintenance of current systems should be charged to expenses.

b. Fences

Includes cost of material, installation, surveying and other related items incurred for the construction of permanent security and traffic control fences. Cost of replacing wire, sections of posts and/or rails and wire should be charged to expense. Additions to fences or complete replacement of fences should be capitalized in the year completed. Costs under ~~fifty~~ one hundred thousand dollars ($10~~5~~0,000) should be charged to expense.

c. Landscaping ~~Improvements~~

Includes initial construction cost of sidewalks, drives, parking lots, athletic fields, trails, plazas, outdoor lighting, digital or lighted signs, shrubs and trees, lawns, ground watering systems for lawns, and roads. Also includes surveying, filling, and draining costs if such costs are incurred solely for the installation of the improvement and are not part of an overall land acquisition and construction project. These examples are to be used as a guide and are not intended to be all-inclusive.

Additions to existing landscaping ~~improvements~~ should be capitalized in the year completed. Maintenance, partial replacement, and resurfacing projects are to be charged to expense.

Landscaping ~~improvement~~ projects with a cost under ~~fifty~~ one hundred thousand dollars ($10~~5~~0,000) should be charged to expense.

~~d. Digital or Lighted Signs~~

~~Digital or lighted signs are a stand-alone signs which displays information and other messages. Digital or lighted signs shall include the costs of installation and wiring. Costs under twenty thousand dollars ($20,000) should be expensed.~~

4. **Equipment**

Equipment items acquired by the Colleges with a cost exceeding five thousand dollars ($5,000), and having an economic useful life of two (2) years, will be capitalized at net invoice price plus freight, installation charges, and trade-in allowance, if any. Items purchased in bulk quantity will be classified according to the smallest useable unit, (e.g., ten (10) computers purchased for one thousand five hundred dollars ~~(~~[$1,500]~~)~~. Although the invoice will be for fifteen thousand dollars ~~(~~[$15,000]~~)~~, these items will not be capitalized.) Component parts, which individually cost less than the capitalization level but when combined exceed the capitalization level, shall be capitalized when purchased as a functional unit. Items of lesser value may be capitalized when required by a regulatory agency.

a. Heavy Equipment

Includes tractors, front-end loaders, and telehandlers.

b. Autos, Vans, and Other Passenger Vehicles Used in Motor Pool

Includes all vehicles which are used primarily for the transportation of individuals.

c. Trucks, Busses, and Cargo Vehicles

Includes all busses used to transport individuals as well as vehicles used to transport cargo.

d. Mowers, Skid Steer, Toolcat, and Other Grounds Equipment

Includes all equipment which is used for the upkeep of ~~groups~~grounds.

e. Computer Equipment

This equipment should be classified separately due to the rapid obsolescence. Cost includes net invoice price plus inbound transportation and installation costs. Warranties and built-in software included as part of the original purchase price (and not a separate line item on the invoice) shall be included in the capitalization amount. The cost of software purchased subsequently should not be capitalized for financial reporting purposes since such software is generally licensed and not owned, even if the license agreement allows perpetual use of the software without additional license payments. Subsequent purchases of warranties shall not be capitalized but entered as operating expenses.

f. Miscellaneous Education Materials Stored on Computer-Related Equipment/Devices

Miscellaneous educational materials that are stored on computerized hardware or software devices shall be capitalized at acquisition cost. If donated, these items should be measured and capitalized at acquisition value at the date of donation.

The miscellaneous education materials will be capitalized as a single unit entry each year (not as the smallest useable unit) if in excess of five thousand dollars ($5,000) per year.

g. Specimens, Collections, and Library Holdings

Art objects, specimens, and artifacts shall be capitalized only when they are installed as an integral part of a building structure and cannot be easily moved from the building. In that case, they are capitalized as part of the building project. All other art objects, specimens, artifacts, and collections, including library materials, shall be expensed, so long as the items meet the following three (3) conditions:

1) Items are held for public exhibition, education, or research in furtherance of public service, rather than financial gain;
2) Items are protected, kept unencumbered, cared for, and preserved; and
3) The proceeds from sales of any collection items must be used to acquire other items for collections.

h. Leases

The Colleges enter into various leasing agreements for the use of equipment, facility space, etc. In governmental accounting a lease is defined as a contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction. ~~there are two classifications of leases, capital or operating~~.

Lease agreements will be sorted into three categories: short-term leases, contracts that transfer ownership, and all other leases.

~~If the lease meets one or more of the following criteria, it is a capital lease and should be capitalized:~~

~~1) The lease transfers ownership of the property to the lessee by the end of the lease term.~~

1) Short-term leases

Short-term leases are defined as leases that have a maximum possible term of twelve (12) months or less, including any options to extend, regardless of their probability of being exercised. Leases that are month-to-month are considered short-term. Short-term leases will be accounted for similarly to operating leases, with lease payments being recorded as expense or revenue by the lessee or lessor.

2) Contracts that transfer ownership

If the underlying asset transfers ownership to the lessee by the end of the contract, the transaction should be reported as a financed purchase of the underlying asset by the lessee, or sale of the asset by the lessor.

3) All other leases

Any agreement that doesn't qualify as a short-term lease or ownership transfer contract will fall into this category, with implications for both lessees and lessors. This includes leases that previously were considered operating leases and, therefore, were not reported as liabilities.

At the commencement of the lease term, the lessee should recognize a lease liability and an intangible right-to-use lease asset (lease asset). The lease liability will be measured at the present value of payments expected to be made during the lease term. Lease payments will result in reduction of the lease liability and recognition of interest expense. The lease asset will be measured as the sum of the initial measurement of the lease liability, initial direct costs, and lease payments made at or prior to commencement, less any lease incentives received from the lessor at or before the commencement of the lease term. The lease asset will be amortized over the shorter of the lease terms or the useful life of the underlying asset.

~~2) The lease contains a bargain purchase option.~~

~~3) The lease term is equal to 75 percent (75%) or more of the estimated economic life of the leased property. However, if the beginning of the lease term falls within the last 25 percent (25%) of the total estimated economic life of the lease property, including earlier years of use, this criterion should not be used for the purposes of classifying the lease.~~

~~4) The present value at the beginning of the lease term of the minimum lease payments, excluding that portion of the payments representing executory costs such as insurance and maintenance to be paid by the lessor, including any profit thereon, equals or exceeds 90 percent (90%) of the excess of the fair value of the leased property to the lessor at the inception of the lease over any related investment tax credit retained by and expected to be realized by the lessor. However, if the beginning of the lease term falls within the last 25 percent (25%) of the total estimated economic life of the leased property, including earlier years of use, this criterion should not be used for purposes of classifying the leases. A lessor should compute the present value of the minimum lease payments using the interest rate implicit in the lease. A lessee should compute the present value of the minimum lease payments using the lessee's incremental borrowing rate unless it is practicable to obtain the implicit rate computed by the lessor and the implicit rate computed by the lessor is less than the lessee's incremental borrowing rate. If both of those conditions are met, the lessee shall use the implicit rate.~~

~~A capital lease is recorded at the full value of the contract, including the ultimate purchase if applicable, in an appropriate fixed asset account at the time the contract is made. At the same time, a total lease contract liability should be established. All subsequent payments under the contract should be recorded in the appropriate operating expense account and later transferred by accounting as a reduction of the lease payable account.~~

~~Occasionally, equipment will be purchased under a lease contract, even though it was not the intent to purchase the equipment at the time the lease was negotiated. Under these circumstances, the equipment should be capitalized at the time the decision is made to purchase and only for the amount of the negotiated purchase price. Prior year lease payments should not be capitalized.~~

~~If the lease agreement does not meet one or more of the four criteria listed above, it is classified as an operating lease. The payments made on an operating lease are charged to expense over the lease term as it becomes due. Normally operating leases are not capitalized.~~

i. Office Furnishings

Includes furniture such as desks, chairs, cabinets, and appliances in a building.

j. Used Equipment

Includes all heavy equipment, autos, vans, passenger vehicles, trucks, busses, cargo vehicles, mowers, skid steers, toolcats, computers, office furnishings, and all other equipment which is purchased in a used condition by the Colleges.

k. All Equipment Not Specifically Defined in Other Classifications

This classification includes apparatus, machinery, implements, and tools used on campus grounds or in classrooms, laboratories, offices, shops, production operations, storerooms, and auxiliary enterprises which do not fall into one of the categories noted above.

---

5. **Intangible Assets**

Intangible assets are those that lack physical substance, are nonfinancial in nature, and ~~has~~ have an initial useful life that extends beyond a single reporting period. To be recorded as an asset the intangible must be owned by the Colleges and be separately identifiable. Examples of intangible assets are computer software and website, easements, various rights (e.g. land use, water, timber, and mineral), licenses and permits, patents, copyrights and trademarks. Intangible assets must have an acquisition cost of five hundred thousand dollars ($500,000) and a life greater than two (2) years to be capitalized. Purchased intangible assets shall be capitalized using the asset's purchase price. Donated intangible assets shall be measured and capitalized at the asset's acquisition value. Intangible assets with indefinite useful lives should not be amortized. ~~For~~ ~~i~~Intangible assets that are the result of contractual or legal rights, including patents, license, trademarks, etc., ~~these assets~~ should be amortized over the contractual or legal life.

Internally developed software for capitalization purposes includes software that is developed in-house by the Colleges' own personnel or by a contractor on the Colleges' behalf and commercially available software that is purchased or licensed by the Colleges that requires more than minimal incremental effort before being put into operation. Such software shall be amortized over ten~~d~~ (10) years.

Software development generally involves three (3) phases as follows:

a) Preliminary project stage

Activities in this stage will generally include the conceptual formulation and evaluation of alternatives for the software project, the determination of the existence of needed technology, and the final selection of alternatives for the development of the software.

b) Application development stage

Activities in this stage will generally include the design of the chosen path, including software configuration and software interfaces, coding, installation of hardware, and testing, including the parallel processing phase.

c) Post-implementation/operation stage

Activities in this stage include user application training and system maintenance.

Costs associated with activities of the preliminary project stage and post-implementation/operation stage should be expensed as incurred. Once preliminary project stage activities are completed and management has authorized and committed to funding the software project, costs associated with activities of the application development stage should be capitalized until the software is in place and operational.

6. **Construction Work in Progress**

Construction Work in Progress account is designed to accumulate all costs incurred in connection with projects undertaken for the construction or renovation of capital assets. Costs should remain in the Construction Work in Progress account until the project is complete and the building or other constructed asset is placed in service.

~~-~~Upon completion of the project, all costs will be removed from the Construction Work in Progress account and charged to appropriate building, improvements other than buildings, equipment, and intangible asset accounts in accordance with the capitalization policy.

~~Effective beginning with fiscal year 2017-18 i~~Interest cost incurred before the end of a construction period is to be expensed.

Policy Adopted:	3/11/94	
Policy Revised:	11/11/95	
Policy Revised:	5/21/01	
Policy Revised:	4/13/07	
Policy Revised:	4/17/09	
Policy Effective:	7/1/10	Approved: 6/3/10
Policy Revised:	3/25/11	
Policy Revised:	1/14/14	
Policy Revised:	6/10/14	
Policy Revised:	5/3/16	
Policy Revised:	5/10/19	
Policy Revised:	7/3/19	
Policy Effective:	7/1/21	Approved:_________