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GFOA Recommended Practice

Establishing Appropriate Capitalization Thresholds for Fixed Assets (1997)

Background. In the public sector, the term "fixed assets" typically is used to refer to land, buildings, equipment, and improvements other than buildings acquired by a government for use in the provision of goods or services to citizens. It is incumbent upon public-sector managers to maintain adequate control over all of a government's assets, including its fixed assets, to minimize the risk of loss or misuse.

Not all fixed assets are required to be reported on a government's balance sheet. Specifically, fixed assets with extremely short useful lives and fixed assets of small monetary value are properly reported as an "expenditure" or "expense" in the period in which they are acquired. Fixed assets that are reported on the balance sheet are said to be "capitalized." The monetary criterion used to determine whether a given fixed asset should be reported on the balance sheet is known as the "capitalization threshold." A government may establish a single capitalization threshold for all of its fixed assets or it may establish different capitalization thresholds for different classes of fixed assets.

Capitalization is, of its nature, primarily a financial reporting issue. That is to say, a government's principal concern in establishing specific capitalization thresholds ought to be the anticipated information needs of the users of the government's external financial reports. While it is essential to maintain control over all of a government's fixed assets, there exist much more efficient means than capitalization for accomplishing this objective in the case of a government's smaller fixed assets. Furthermore, practice has demonstrated that fixed asset systems that attempt to incorporate data on numerous smaller fixed assets are often costly and difficult to maintain and operate.

Recommendation. The Government Finance Officers Association (GFOA) recommends that state and local governments consider the following guidelines in establishing capitalization thresholds for their fixed assets:

1. Fixed assets should be capitalized only if they have an estimated useful life of at least two years following the date of acquisition.
2. Fixed assets' capitalization thresholds should be applied to individual fixed assets rather than to groups of fixed assets (e.g., desks, tables).
3. As a general rule, capitalization thresholds should be designed to encompass approximately 80 percent of a government's total noninfrastructure assets. (Infrastructure assets are assets that are immovable and of value only to the government).

4. In no case should a government establish a capitalization threshold of less than \$1,000 for any individual item.
5. In establishing capitalization thresholds, governments that are recipients of federal awards should be aware of federal requirements that prevent the use of capitalization thresholds in excess of certain specified maximum amounts (i.e., currently \$5,000) for purposes of federal reimbursement.
6. Governments should exercise control over their noncapitalized fixed assets by establishing and maintaining adequate control procedures at the departmental level.

Reference

- *Government Fixed Asset Inventory Systems: Establishing, Maintaining and Accounting*, Paul Glick, GFOA, 1987.