CITY OF STOUGHTON
FINANCE DEPARTMENT
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To: Capital Improvement Plan (CIP) Committee members
Finance Committee members
Mayor Swadley
Other interested parties
From: Dave Ehlinger
Re: City policy regarding capital asset threshold
Date: September 2, 2022

The draft Capital Improvement Plan (CIP) dated 09-02-2022 is scheduled to be discussed at the next CIP Committee meeting. This draft was prepared using the same methodology as in prior years.

However, it should be pointed out that our past practice is not following the prior approved policies. In addition, these policies are inconsistent.

Supporting documentation for the comments below are either attached to this cover letter and/or hyperlinked below.

A. The audited financial statements in the Notes to the Financial Statements section have consistently indicated that capital assets have an initial cost of more than **$5,000** for general capital assets.
   - *It should be noted that no capitalization threshold policy as adopted by the Common Council has been located.*
   - *The $5,000 threshold is consistent with the Government Finance Officers Association (GFOA) Best Practice for capitalization threshold.*

B. The CIP policy as adopted by the Common Council in 2006 indicates that CIP items are either (a) large expenditures exceeding **$15,000** or (b) not budgeted every year. *It should be noted that just because something is not budgeted every year it does not automatically become a capital asset.*

C. Wisconsin Statute 67.04 indicates that debt shall only be issued for capital expenses (i.e., not operating expenses).

D. Wisconsin Statute 66.0602 limits local government levy amounts with the exception of levy used to pay debt related expenses that are the result of prior capital purchases paid for by debt.

E. Baker Tilly US, LLP prepares the audited financial statements on our behalf using the $5,000 capitalization threshold.

F. The current CIP policy indicates grouping of similar items together can constitute a capital asset.
    - *General Accepted Accounting Principles (GAAP), whether governmental or not, indicates that a group of items should only be capitalized as a single asset if all the components are needed to operate together.*
    - *The GFOA best practice for capitalization threshold is for individual items rather than to groups of similar items.*

Given all of the above, some direction is needed from elected officials in relation to the Capital Improvement Plan for the 2023 budget.

1. What dollar amount for capitalization threshold should be used?

    - Higher dollar value
        - More expenses restricted by the current levy limit statutes, thus reducing the effectiveness of the departments involved.
        - Lower audit fees by Baker Tilly US, LLP in relation to capital assets.
    - Lower dollar value
        - Fewer restrictions under the current levy limits, thus increasing the effectiveness of the departments involved.
        - Increased interest expenses in subsequent years, which is exempt from the current levy limits.
        - Higher audit fees by Baker Tilly US, LLP in relation to capital assets.

2. Should groups of similar assets purchased be combined together as a single capital asset?

    - Allowing for grouping of assets together has the same effect as "lower dollar value" as per the above.
    - Not allowing for grouping of assets together has the same effect as "higher dollar value" as per the above.

Respectfully requested,

David P. Ehlinger, CPA
Director of Finance/Comptroller
City of Stoughton

Capital Assets

Government-Wide Statements

Capital assets, which include property, plant and equipment, are reported in the government-wide financial statements. Capital assets are defined by the City government as assets with an initial cost of more than $5,000 general capital assets and $15,000 for infrastructure assetsand an estimated useful life in excess of one year. All capital assets are valued at historical cost or estimated historical cost if actual amounts are unavailable. Donated capital assets are recorded at their estimated acquisition value at the date of donation.

Additions to and replacements of capital assets of business-type activities are recorded at original cost, which includes material, labor, overhead and an allowance for the cost of funds used during construction when significant. The cost of renewals and betterments relating to retirement units is added to plant accounts. The cost of property replaced, retired or otherwise disposed of, is deducted from plant accounts and, generally, together with removal costs less salvage, is charged to accumulated depreciation.

Depreciation of all exhaustible capital assets is recorded as an allocated expense in the statement of activities, with accumulated depreciation reflected in the statement of net position. Depreciation is provided over the assets' estimated useful lives using the straight-line method. The range of estimated useful lives by type of asset is as follows:

Buildings	15-75	Years
Land Improvements	15-30	Years
Machinery and Equipment	3-15	Years
Utility System	5-100	Years
Infrastructure	30-75	Years

Fund Financial Statements

In the fund financial statements, capital assets used in governmental fund operations are accounted for as capital outlay expenditures of the governmental fund upon acquisition. Capital assets used in proprietary fund operations are accounted for the same way as in the government-wide statements.

Land Held for Resale

Land held for resale consists of land and improvements and is valued at cost of acquisition, demolition, and site improvement.

CITY OF STOUGHTON CIP POLICY

PURPOSE

The CIP (Capital Improvement Plan) is to be used as a guide for future capital improvements and will incorporate the following elements:

1. A CIP is for large non-reoccurring expenditures.
    a. *Large*: $15,000 or more for a single item or group of similar items.
    b. *Non-reoccurring*: Not budgeted every year.
2. The CIP will cover the next six years.
3. CIP projects will be coordinated between departments of the City.
4. Because a CIP is referenced when putting together the City's Debt Plan, a high degree of confidence in the accuracy of the CIP is required (i.e., the first year's items should remain pretty much unchanged from the most recent CIP approval, the second year could have minor changes with an expectation of total amounts not varying more than 15% from the prior approval, third year changes in total should not vary more than 25% from the prior approval, and the fourth through sixth years allowed a little more flexibility.)
5. The CIP is a tool to help eliminate property tax "spikes," and an effort is made to "level out" debt service resulting from the implementation of Capital Budget items.

CALENDAR

April – May: Department Heads prepare CIP updates and review with Oversight Committees

By the end of June: CIP Team meets and reviews the prepared updates

July – August: CIP Team passes on their recommendations to the Finance Committee. (CC to the Oversight Committees and Department Heads) **(**Department Heads include subsequent year CIP items in their initial Budget requests.)

September: Finance Committee reviews CIP

Early October: COW on CIP

End of October: Council approves final CIP.

RESPONSIBILITIES

Finance Director: Overall coordination of the CIP process is vested with the Finance Director. Each year the Finance Director will identify funding sources for CIP items, i.e., Debt, Levy, or Fund Balance, and include these in the Departmental Summary Report.

The Finance Director will also update an estimate of what percentage of the annual budget is represented by debt service for each of the next three years.

Department Heads: Will prepare a CIP Summary detailing any requested changes to the previously approved CIP. This summary will accompany the CIP as it moves through the Update approval process.

Oversight Committees: Will meet to review departmental updates assigned to them.

ADOPTED BY THE COMMON COUNCIL: January 24, 2006

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Recommendation:

GFOA recommends that state and local governments adhere to the following guidelines for capitalization thresholds:

- Establish minimum cost and useful-life based thresholds to avoid the cost of capitalizing immaterial items;
- Establish a minimum capitalization threshold of $5,000 for any individual item;
- Establish a minimum capitalization threshold of at least a two-year useful life for any individual item;
- Consider establishing different dollar capitalization thresholds for different classes of capital assets (i.e. land, infrastructure, buildings and improvements, and equipment);
- Capitalization thresholds are best applied to individual items rather than to groups of similar items (e.g., desks and tables), unless the effect of doing so would be to eliminate a significant portion of total capital assets (e.g., books of a library district);
- Governments should perform a periodic review of their capitalization thresholds;
- In establishing capitalization thresholds, governments that are recipients of federal awards should be aware of federal capitalization thresholds requirements; and
- Governments should exercise control over potentially capitalizable items that fall under the operative capitalization threshold but require special attention.

1) Note that while indirect costs pertaining only to capital projects should be capitalized, general overhead costs such as human resources services or the commissioner's office staff of an agency not exclusively performing capital work should not be allocated to capital projects and capitalized. [Accounting for Capital Assets, A Guide for State and Local Governments, Stephen J. Gauthier, GFOA, 2008].

67.04 Purposes of issuing municipal bonds and notes.

(1) In this section:

(a) "Ancillary charges" include site preparation expenditures, professional fees, legal claims directly attributable to asset acquisition and interest costs incurred prior to and during construction.

(ag) "Operating expenses" include wages, salaries, fringe benefits, materials, supplies, contractual services, equipment with a useful life of less than one year and other costs specified by the department of revenue by rule. "Operating expenses" do not include ancillary charges incurred in the acquisition, development or construction of real property or property with a useful life of one year or more.

(ar) "Project" means the acquisition, leasing, planning, design, construction, development, extension, enlargement, renovation, rebuilding, repair or improvement of land, waters, property, highways, buildings, equipment or facilities.

(b) "Public purpose" means the performance of any power or duty of the issuing municipality.

(2)

(a) Subject to the limitations specified in ss. 67.03 and 67.045, any municipality may borrow money and issue bonds to finance any project undertaken for a public purpose.

(b) Subject to the limitations specified in s. 67.03, any city with a population greater than 75,000 may borrow money and issue bonds to finance the cost of low-interest mortgage loans under s. 62.237.

(3) Subject to the limitations specified in s. 67.03, any municipality may refund municipal obligations including interest on them whether or not the obligations being refunded were issued for any purpose for which the municipal obligations might have been issued in the original instance, if the time for payment of bonds issued to refund bonds and notes authorized under this chapter does not extend beyond the period permitted under s. 67.07. Bonds issued to refund municipal obligations issued under ch. 66 shall be paid within the period permitted under s. 67.07, commencing on the original date of the refunding bonds.

(4) The legislature finds that contracting of debt under this chapter for any project constitutes a public purpose.

(5)

(a) Except as provided in par. (b), the proceeds of any municipal bonds or notes issued by a county under this chapter shall not be used to fund the operating expenses of the general fund of the county or to fund the operating expenses of any special revenue fund of the county that is supported by property taxes.

(b) Paragraph (a) does not apply to notes issued under s. 67.12 (1) to (8m) or to municipal bonds or notes issued by a county for any of the following purposes:

1. To comply with a court order or judgment.

3. To provide liability insurance, property insurance, or risk management services under s. 611.11 (4).

4. To pay unfunded prior service liability contributions under the Wisconsin retirement system, or to pay unfunded prior service liability with respect to an employee retirement system, if all of the net proceeds of the note will be used to pay for such contributions or payments.

History: 1983 a. 207, 236, 368, 538; 1987 a. 197; 1993 a. 16; 1995 a. 227; 1999 a. 9; 1999 a. 150 s. 672; 2003 a. 78; 2007 a. 115.