

## CAPITALIZATION POLICY

April 16, 2015 updated 2019

The capitalization policy of Dartmouth College determines the proper classification of costs for new construction, renovations, improvements, maintenance projects, and equipment. This policy has been developed to assist project managers and others with the important task of distinguishing between capital and non-capital costs. Costs that are capitalized are depreciated over their useful lives. Costs that are not capitalized are recorded as an expense in the year incurred.

### Capital Costs:

Costs of \$50,000 or more incurred for a **single project/purchase** which are considered to be one of the following: (1) construction costs, **fabrication**, or a purchase that creates one new asset; (2) an **improvement, renovation/replacement** that either extends the life or adds value or functionality to an existing asset; (3) costs that correct functional inadequacies, change the use of an existing asset, or are necessary to put an asset into service, or (4) **application/development stage** costs for software/website development.

#### Definitions:

- Single project/purchase – expenditures or purchases related to one asset
- Fabrication – using purchased material and Dartmouth labor to assemble or manufacture equipment
- Improvement – additions to existing systems, space, or components
- Renovation/replacement – removal of existing systems, components, or space and the construction of new systems, components, or space in its place.
- Application/development stage costs – purchase or design, configuration, software interface, coding, testing, develop/purchase data conversion software, or upgrades that result in additional functionality.

#### Examples of Capital Costs:

- Construction of a new building or an addition to an existing building that increases the square footage. Installation of new fixed equipment or building systems such as lockers or a security system.
- Land/site improvements such as new parking lots, paving a gravel parking lot, sidewalks, wells, septic systems, tunnels, or initial landscaping.
- Replacement of a building system such as mechanical, plumbing, and electrical systems or a roof.
- Renovation of the entire interior, an entire floor, classrooms, or offices
- Replace technologically outdated equipment or building stems.
- Moveable equipment such as servers, microscopes, and crew boats.
- Website development to provide information, solicit contributions, etc.

### **Non-Capital/Maintenance Costs (expendable):**

(1) Capital projects and moveable equipment purchases of less than \$25,000; (2) Costs which neither materially add to the value of an existing asset nor appreciably prolong its **economic useful life**, but keep it in ordinary, efficient operating condition. These costs are considered normal, recurring, periodic, and necessary to maintain the asset's economic useful life for the use(s) for which it was acquired or constructed; (3) **Preliminary stage costs** for software development and construction projects; (4) **Post-implementation stage costs** for software development.

#### Definitions:

- Economic useful life – depreciable life, an estimate of how long the asset will last.
- Preliminary stage costs – determination of needs and formulation and evaluation of alternatives.
- Post-implementation stage costs - data conversion, employee training/travel, annual licenses and fees.

#### Examples of Non-Capital Costs:

- Exterior and interior painting of buildings, not part of new construction or a major renovation project. Recurring planned major maintenance activities such as overhauls or refurbishments.
- Re-planting of trees, shrubs, and bushes. Repairs and cleaning of masonry or roofs.
- Evaluating various software solutions to identified software needs.
- Travel, meals, conferences fees for Dartmouth employees.
- Moveable equipment such as laptops, printers, and audio/visual equipment.

### **Construction in Progress:**

Construction in progress (CIP) refers to all construction, renovation, improvement, fabrication, and customization projects where capital costs are greater than or equal to \$50,000 or non-recurring extraordinary repairs and maintenance (such as flood damage repairs) funded by long-term maintenance reserves. Please complete the *CIP Account Setup Form* to request CIP funding and activity values and review the *Org 003 Natural Class Definitions* document for guidance regarding recording CIP transactions in the appropriate capital and non-capital natural classes.

All capital projects must be componentized when they are put into use. Please complete the *Componentization Template* and refer to the *Componentization Guide* for a list of the various components and a reasonable method for allocating total project costs to these components.

**Fabricated Equipment:**

Please refer to the *Fabricated Equipment Policy* for information regarding both capital and non-capital fabricated equipment.

**Capital Equipment:**

Capital equipment refers to single pieces of moveable equipment and equipment systems costing \$25,000 or more. Multiple pieces of equipment that individually cost less than \$25,000 but work together in order to be operational are considered a system. An example of a system: A computer linked to A/V equipment. Since the computer access the functionality of the A/V equipment, the A/V equipment cannot be used without it. An example of multiple pieces working together that are not a system: Storage devices added to a server to add additional storage space. The server can operate without the additional devices.

**Moveable Equipment:**

Although moveable equipment costing \$5,000 to \$24,999 is not capitalized, it is included in the moveable equipment inventory (Fixed Asset System) along with capital moveable equipment for F&A cost proposal purposes. Please see the *Moveable Equipment Inventory Policy* for further information.

**Disposals:**

The Controller's Office must be notified of all disposals of capital equipment through transfer, sale, or retirement in order to properly account for sales proceeds, gain/loss on sale, and removing the asset and corresponding accumulated depreciation from the College's fixed assets. Procurement should be contacted as well to coordinate the disposal with the department and to ensure that the equipment is removed from the Fixed Asset System. Additionally, the Controller's Office must be notified of all partial and complete building demolitions.

**Capital Leases:**

The Controller's Office must be notified of all leases entered into in order to classify the lease as either capital or operating, as each type of lease is accounted for differently. The College owns the equipment acquired under capital leases and therefore an asset must be recorded as well as the corresponding lease payable. Periodic payments under a capital lease are recorded by departments as lease principal and interest expense (natural classes 8642 and 8612, respectively). Dartmouth does not own equipment under operating leases; therefore periodic payments are recorded by departments as rental expense (natural classes 7211 to 7237).

**If you have any questions regarding this policy or need assistance in completing forms or determining the proper classification of specific project costs please contact the Financial Reporting department in the Controllers Office.**

## **Appendix to Capitalization Policy Accounting for Studies and Planning Costs**

This Appendix provides guidance on the accounting for the costs of planning and studies related to potential capital projects.

### *Definition*

The first stage during which costs are incurred related to long-lived assets is the Preliminary Stage. During the Preliminary Stage, activities are performed exploring the opportunities for acquisition or construction of the asset. Typical activities that occur in the Preliminary Stage include the following:

- Studies may be conducted to evaluate whether to propose a project. These may involve general examination of a building to identify whether there are issues needing attention that result in a proposed project, or which project should be proposed first if there are multiple potential projects.
- A Feasibility Study is a formal evaluation of a proposed project. The intent behind this study is often to see whether the project goals can be achieved within an estimated cost target and/or timeframe. The study may also examine whether a project is technologically feasible, and whether it can be achieved within any applicable regulatory or other legal constraints. This evaluation is needed when a project involves a significant investment, so that a decision can be made to continue, alter or cancel the project.
- Planning activities are other preliminary costs necessary to determine whether a proposed project will proceed. These could include surveying, engineering studies, design layouts and other similar items.

### *Accounting treatment*

US GAAP has limited guidance on capitalization policies for facilities constructed for a reporting entity's own use. However, the reference materials listed at the end of this Appendix provide helpful guidelines in this area. These materials indicate that accounting for costs during the Preliminary Stage of a construction project is similar to accounting for costs associated with start-up activities, for which guidance is provided in ASC 720-15, *Other Expenses - Start-up Costs*. ASC 720-15 states that such costs should be expensed as incurred.

### *Setting up a CIP account*

Preliminary Stage costs may be expensed, either in a CIP project (non-operating), charged directly to operations, or charged directly to a deferred maintenance reserve (operating), as appropriate. Preliminary Stage work may be approved as part of the annual Capital Budget, but a CIP account will only be set up when a specific asset-producing project has been identified and approved.

Once the asset-producing project has been identified, the cost of studies or other planning activities can be charged to a CIP account as long as the estimated costs meets the minimum threshold for establishing a CIP account (currently \$50,000). Subactivity 0000-Default must be used to identify these Preliminary Stage costs within the CIP account string. As part of componentization, these costs will be expensed.

### *Closing CIP account*

If the project moves forward to the Design phase, costs should be charged to the same CIP account; however, subactivity 0000 must be disabled and a new subactivity set up for the remainder of the work. The CIP project will be closed after the componentization process is complete. If additional planning dollars are approved, subactivity 0000 should continue to be used.

If the planning work or feasibility study does not lead to an approved capital project within an agreed upon period of time (normally 1-2 years) the CIP account will be closed. The Controller's Office may grant exceptions to this timing for unusual circumstances.

### *Reference Materials*

The proposed Statement of Position issued by the Financial Reporting Executive Committee of the AICPA (FinREC), *Accounting for Certain Costs and Activities Related to Property, Plant and Equipment* (2003).

PwC accounting and financial reporting guide, *Property, plant, equipment and other assets*, issued in June 2017 and partially updated in September 2018.

Effective Date: FY19.