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Survey of Capitalization Threshold and Other Policies for Property, Plant, and Equipment

G A O

Accountability ★ Integrity ★ Reliability

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Abbreviations

BOP	Bureau of Prisons
DOC	Department of Commerce
DOE	Department of Energy
DOI-Rec	Department of the Interior-Bureau of Reclamation
DOJ	Department of Justice
DOT	Department of Transportation
FAA	Federal Aviation Administration
FASAB	Federal Accounting Standards Advisory Board
GAAP	generally accepted accounting principles
GSA	General Services Administration
NASA	National Aeronautics and Space Administration
NOAA	National Oceanic and Atmospheric Administration
OMB	Office of Management and Budget
PMA	Power Marketing Administration
PP&E	property, plant, and equipment
PSC	Private Sector Council
SFFAC	Statements of Federal Financial Accounting Concepts
SFFAS	Statements of Federal Financial Accounting Standards
SSA	Social Security Administration
TVA	Tennessee Valley Authority
USPS	United States Postal Service
USDA	Department of Agriculture
VA	Department of Veterans Affairs

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United States General Accounting Office
Washington, D.C. 20548

October 15, 2002

The Honorable Mark W. Everson
Deputy Director for Management
Office of Management and Budget

Mr. Donald V. Hammond
Fiscal Assistant Secretary
Department of the Treasury

In passing the 1990 Chief Financial Officers (CFO) Act and a range of other financial management reform legislation, the Congress has sought to overcome the historical lack of reliable, useful, and timely information with which to make informed decisions, measure and control costs, manage for results, and ensure financial accountability on an ongoing basis.

The government's general property, plant, and equipment (PP&E), reported at almost $307 billion, net of accumulated depreciation, as of September 30, 2001, represents approximately one-third of the reported assets on the balance sheet of the U.S. government's consolidated financial statements. General PP&E is often referred to as fixed assets, and includes land, buildings, equipment, and improvements acquired by the government to be used in providing goods and services to citizens.[1] Capitalization threshold and useful life policies affect whether and how the costs of acquiring PP&E or construction of PP&E are capitalized and allocated through depreciation to the periods benefiting from such assets, and are critical to the fair presentation of an entity's financial position and results of operations. Excessively high capitalization thresholds can have a significant impact on financial reporting by reducing the amount of federal assets that are reported on the balance sheet and, most important, by jeopardizing the matching of costs to the appropriate period of asset utilization so that the cost of programs and operations are properly measured.

[1]General PP&E does not presently include national defense PP&E, which is the PP&E components of weapons systems and support PP&E owned by the Department of Defense or its component entities for use in the performance of military missions, as well as vessels held in a preservation status by the Maritime Administration's National Defense Reserve Fleet. Existing U.S. generally accepted accounting principles requiring that national defense PP&E be disclosed separately in financial reports are undergoing change, pending final publishing of the Statements of Federal Financial Accounting Standards No. 23, *Eliminating the Category National Defense Property, Plant, and Equipment*, which was approved for issuance by the Federal Accounting Standards Advisory Board in June of 2002.

For the past 5 fiscal years, in our audits of the consolidated financial statements, we have reported[2] that because the government lacked complete and reliable information to support PP&E holdings, we could not satisfactorily determine that all assets were included in the financial statements, verify that certain reported assets actually existed, or substantiate the amounts at which they were valued. PP&E reporting was one of the primary reasons for our disclaiming an opinion on the consolidated financial statements again in fiscal year 2001.[3] As the government continues to make progress in addressing major audit issues, such as PP&E reporting, and the prospect of auditable consolidated financial statements draws closer, issues such as useful lives and capitalization thresholds are now in sharper focus.

Under the Statement of Federal Financial Accounting Standard (SFFAS) No. 6, *Accounting for Property, Plant, and Equipment*, federal agencies are to record as property and equipment all items that meet certain characteristics, such as a useful life of 2 years or more, and are permitted to establish individual capitalization thresholds and useful life policies due to their diverse size and uses of PP&E. SFFAS No. 6 was issued in November 1995 and was effective for fiscal years beginning after September 30, 1997. Previously, the capitalization threshold for federal agencies was $5,000.[4]

We have noted large increases in federal agency capitalization thresholds over the past 5 years, and our audit work at two major agencies has highlighted problems in this area. In prior audit work performed at the Internal Revenue Service (IRS), we found that Treasury's $50,000 capitalization threshold contributed to a material understatement in PP&E. IRS has since revised its capitalization threshold accordingly. We previously raised concerns with the Department of Defense (DOD), which

[2]The Secretary of the Treasury, in coordination with the Director of the Office of Management and Budget, is required to annually submit financial statements of the U.S. government to the President and the Congress. We are required to audit these statements. The Government Management Reform Act of 1994 has required such reporting, covering the executive branch of government, beginning with financial statements prepared for fiscal year 1997. 31 U.S.C. 331 (e). The government has elected to include certain financial information on the legislative and judicial branches in the consolidated financial statements as well.

[3]U.S. General Accounting Office, *U.S. Government Financial Statements: FY 2001 Results Highlight the Continuing Need to Accelerate Federal Financial Management Reform*, GAO-02-599T (Washington, D.C.: Apr. 9, 2002).

[4]Title 2 of the GAO *Policy and Procedures Manual for Guidance of Federal Agencies*.

holds the majority of the U.S. government's reported PP&E, about the basis for its $100,000 capitalization threshold, in part because of issues surrounding the quality of the data available to make such a determination.

As an initial step to address this issue governmentwide and as part of a series of planned work on key audit issues pertaining to the consolidated financial statement audit, we undertook a survey of PP&E capitalization threshold and useful life policies at 14 federal agencies that reported significant amounts of PP&E. We also surveyed 12 private sector companies on these same PP&E policies. Our survey was designed to determine the federal agencies' (1) current capitalization threshold practices for PP&E and how such policies compare to the practices being applied to PP&E in the private sector and (2) useful life policies and how they compare to those used in the private sector. Our survey work was not designed to conclude on the reasonableness of the capitalization threshold levels being applied by federal agencies. Instead, our survey results are intended to provide useful baseline information to responsible parties in federal financial reporting. We plan to review the adequacy of capitalization threshold levels and useful life policies at selected agencies in future work.

Results in Brief

Reported capitalization threshold levels at the 14 agencies we surveyed ranged from zero[5] to $250,000.[6] Federal capitalization threshold levels have risen significantly over the past 5 years. Nine out of the 14 agencies surveyed reported that they had at least doubled their capitalization thresholds in the past 5 years, for at least one category of property. Furthermore, 6 of these 9 agencies' capitalization thresholds were at least 5 times higher, with 2 raising the threshold from $5,000 to $100,000, a 20-fold increase. Two of the agencies cited materiality[7] as a factor that caused the

[5]All PP&E additions would be capitalized.

[6]This capitalization threshold range does not include software. Some participants responded that they have a separate capitalization threshold for software, which ranged from $5,000 to $5,000,000.

[7]Materiality is defined in the GAO/PCIE *Financial Audit Manual* as the magnitude of an item's omission or misstatement in a financial statement 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 inclusion or correction of the item.

increase, while 4 identified the implementation of SFFAS No. 6.[8] Other reasons cited included that the threshold represented a management decision or that it was based on the external auditor's recommendation. The vast majority (12 out of 14) of the federal agencies surveyed responded that they had performed some type of formal analyses or studies to develop or validate the capitalization threshold level. Despite the sharp increase in the capitalization threshold, all but 1 of the 14 agencies responded that they maintained property records for PP&E not capitalized on the balance sheet, citing safeguarding of PP&E and supporting agency operations as the key reasons for maintaining such information.

Federal capitalization thresholds are significantly higher than those reported by the private sector entities we surveyed. In some cases, the federal capitalization thresholds for real property were up to 50 times higher than those noted in the private sector. Interestingly, one of our surveyed federal entities, the United States Postal Service (USPS),[9] which sets its rates and fees to recover its costs, reported capitalization thresholds[10] that are in line with the surveyed private sector companies' capitalization threshold levels. Of the 14 agencies surveyed, capitalization thresholds for equipment were as high as $200,000 in the federal government, compared to a maximum of $5,000 in the 12 private sector companies.

In contrast to the wide variance between federal agency and private sector capitalization threshold policies, federal agency useful life policies were generally similar to those found in the private sector. Estimated useful life classifications within the federal government ranged from 2 years to 40 years for personal property and 5 years to 100 years for real property. For example, the estimated useful life classifications for computer software were within a range of 2 to 10 years for the federal agencies surveyed and 3 to 10 years for the private sector participants. The estimated useful life classifications for motor vehicles were within a range of 3 to 12 years for the federal agencies surveyed and 2 to 10 years for the private sector

[8]Prior to the issuance of SFFAS No. 6, the capitalization threshold for all federal agencies was limited to $5,000, in accordance with Title 2, of the GAO *Policy and Procedures Manual for Guidance of Federal Agencies*.

[9]USPS is an independent establishment of the executive branch, with a goal to operate on a break-even basis and cover its expenses almost entirely through postal revenues.

[10]The USPS capitalization threshold is $3,000 for personal property and $5,000 for real property.

companies. We did identify several differences attributable to the variety of assets owned by the entities that participated in our survey, rather than any systemic differences in useful life classifications. For example, several federal agencies in our survey owned assets such as dams, canals, and reactors for which they reported useful lives of 50 years or more. However, our private sector participants did not include a utility company with similar assets for like comparisons. Given the relatively recent introduction of consolidated financial reporting in the federal government, the appropriate and consistent useful life classification is an area that also needs to be periodically reevaluated for impact on financial reporting, performance measurement data, and the financial statement audits.

We received comments on a draft of this report from the Department of the Treasury, the Office of Management and Budget (OMB), and 4 of the 14 federal agencies that took part in our survey. We also received primarily editorial comments from 7 federal agency survey participants and 3 private sector survey participants. The 3 remaining federal agencies told us they had no comments on a draft of this report. In general, the 6 federal entities that commented on the draft took issue with any comparison of capitalization threshold levels in the federal government to those in the private sector and/or our discussion of the wide range of capitalization thresholds at the various federal agencies surveyed.

Certain operating differences and different financial incentives between the federal government and the private sector and between various federal agencies could account for different threshold levels. At the same time, given the wide variance in capitalization thresholds, the sharp increases in recent years, and the significant differences from private sector companies of comparable size, across government, this issue may have a significant effect on the government's consolidated financial statements. This survey was designed to be the first step in analyzing these significant PP&E policies and their impact on the financial reports of the U.S. government and is being provided as a baseline tool as agencies, Treasury, and OMB consider these issues and their impact on financial reporting.

Objectives, Scope, and Methodology

Our work was performed primarily using survey instruments to gather data on PP&E policies at 14 selected federal agencies and 12 private sector companies. Appendix II provides a list of all survey participants. We also held discussions with certain representatives of the participating federal agencies and private sector companies in developing the survey and in gathering follow-up information based upon the survey responses. We did

not verify the accuracy of the data provided to us by the survey participants. We conducted our work from May 2001 through February 2002 in accordance with U.S. generally accepted government auditing standards. We requested comments on a draft of this report from the Department of the Treasury, OMB, all 14 federal agencies that participated in the survey, as well as the 12 private sector council member survey participants. Further details on our scope and methodology are included in appendix I.

Background

The Secretary of the Treasury, in coordination with the Director of OMB, is required to submit annually to the President and the Congress audited consolidated financial statements of the U.S. government beginning with those for fiscal year 1997. We are required to audit those statements. The principal financial statements required for federal agencies are the Balance Sheet, the Statement of Net Cost, the Statement of Changes in Net Position, the Statement of Budgetary Resources, and the Statement of Financing. These statements are to be prepared in accordance with U.S. generally accepted accounting principles. The balance sheet for the federal government presents the total balances of assets, liabilities, and net position as of a specific point in time. The government's general PP&E, reported at almost $307 billion, net of accumulated depreciation as of September 30, 2001, represents approximately one-third of the assets on its balance sheet.

Federal Accounting Standards

Federal accounting standards, which agency CFOs use in preparing financial statements, are promulgated by the Federal Accounting Standards Advisory Board (FASAB).[11] FASAB develops accounting standards after considering the financial and budgetary information needs of the Congress, executive agencies, other users of federal financial information, and the public. FASAB forwards the standards to the three principals—the Comptroller General, the Secretary of the Treasury, and the Director of OMB—for a review period, after which the standards are considered final, then published on FASAB's Web site and in print. The American Institute of Certified Public Accountants recognizes the federal accounting standards promulgated by FASAB as being generally accepted accounting principles (GAAP) for the federal government. Currently, there are 22 SFFAS and three Statements of Federal Financial Accounting Concepts (SFFAC).[12] The concepts and standards are the basis for OMB's guidance to agencies on the form and content of their financial statements and the government's consolidated financial statements.

FASAB significantly relied upon SFFAC No. 1, *Objectives of Federal Financial Reporting*, in drafting accounting standards for PP&E. The two principle reporting objectives relevant to PP&E are operating performance and stewardship. In developing PP&E standards to meet the operating performance objective, FASAB established the goal of measuring the cost associated with using PP&E and including that cost in entity operating results. In seeking to fulfill the stewardship objective, FASAB developed the PP&E accounting standards to result in reporting information on (1) asset condition, (2) changes in the amount and service potential of PP&E, (3) the cost of PP&E where applicable, and (4) spending for acquisition of PP&E versus noncapital spending.

Capitalization Thresholds and Estimated Useful Lives

Although FASAB established the reporting objectives framework in developing the PP&E accounting standards, it concluded that capitalization thresholds should be established by the federal entities themselves, based

[11]In October 1990, the Secretary of the Treasury, the Director of OMB, and the Comptroller General established FASAB to develop a set of generally accepted accounting standards for the federal government.

[12]Accounting standards are authoritative statements of how particular types of transactions and other events should be reflected in financial statements. Accounting concepts explain the objectives and ideas upon which FASAB develops the standards.

on their diversity in size and uses of PP&E. FASAB's requirements in terms of establishing appropriate capitalization thresholds are that they be based on consideration of the entities' financial and operational conditions, consistently applied, and disclosed in the financial reports. Before 1991, accounting principles, standards, and related requirements for executive agencies were published in appendix I of Title 2, "Accounting," of the GAO *Policy and Procedures Manual for Guidance of Federal Agencies*, in accordance with 31 U.S.C. 3511. The capitalization threshold for federal agencies included in Title 2 was $5,000. In addition, under Federal Acquisition Regulations, government contractors are required to capitalize all assets costing $5,000 or more. Capitalization thresholds are tied to materiality as well, in that they generally are established at a level that would not omit a significant amount of assets from the balance sheet, which could materially misstate the financial statements of an entity or its components.

There is not an authoritative standard issued in the private sector specifically addressing capitalization threshold levels. However, the underlying GAAP state that all normal expenditures of purchasing or constructing an asset and readying it for use are capitalized, thereby achieving the matching principle by distributing the costs of such assets to the periods benefited through depreciation. Capitalization thresholds are set at levels that would not approach materiality in any foreseeable circumstances.

SFFAS No. 6 requires that depreciation expense be recognized on all general PP&E, except land and land rights of unlimited duration. Depreciation is the systematic and rational allocation of the costs of general PP&E to the operating periods benefiting from the asset, also referred to as the estimated useful life. FASAB again did not prescribe specific classifications of estimated useful lives. Instead, it requires that the useful life consider economic, environmental, and technological factors such as physical wear and tear and obsolescence.

In the private sector, GAAP state that depreciation method and rate depend upon such factors as time, usage, maintenance policies, and asset obsolescence, and recognize certain prescribed methods for allocating the cost to the periods benefited.

Federal PP&E

PP&E consists of tangible assets, including land, that have estimated useful lives of 2 years or more, are not intended for sale in the ordinary course of operation, and have been acquired or constructed with the intention of being used or being available for use by the entity. SFFAS No. 6, *Accounting for Property, Plant, and Equipment*, identifies four categories of PP&E: (1) general PP&E, (2) national defense PP&E,[13] (3) heritage assets, and (4) stewardship land. General PP&E is used to provide general government services or goods and is reported on the balance sheet for federal financial reporting. National defense PP&E, heritage assets, and stewardship land are collectively referred to as stewardship PP&E and are reported in Supplementary Stewardship Information for federal financial reporting and are not included on the balance sheet or any other principal statement. FASAB has approved issuing a standard[14] that would eliminate the category of national defense PP&E, and all items previously considered national defense PP&E would be classified as general PP&E. The focus of this report is on general PP&E, reported on the balance sheet of the U.S. government, which under current federal accounting standards does not include national defense PP&E.

General PP&E consists of items that (1) could be used for alternative purposes but are used by the federal entity to produce goods or services or to support the mission of the entity, (2) are used in business-type activities, or (3) are used by entities in activities whose costs can be compared to other entities. SFFAS No. 6 requires that all general PP&E be recorded at cost, which shall include all costs incurred to bring the PP&E to a form and location suitable for its intended use. General PP&E includes land acquired for or in connection with other general PP&E and heritage assets,[15] whose predominant use is general government operations.

[13]National defense PP&E is a term established by SFFAS No. 11 to replace the term federal mission PP&E used in SFFAS No. 6 and SFFAS No. 8. National defense PP&E consists of (1) PP&E weapons systems and support PP&E owned by the Department of Defense or its component entities for use in the performance of military missions and (2) the vessels held in a preservation status by the Maritime Administration's National Defense Reserve Fleet.

[14]In June of 2002, FASAB approved issuing SFFAS No. 23, *Eliminating the Category National Defense Property, Plant, and Equipment*. The standard was submitted to the Congress and the three sponsors of the FASAB. If no member of the Congress and none of the sponsors object, FASAB will publish the standard.

[15]SFFAS No. 16 describes reporting standards for heritage assets that serve dual purposes, in that they have heritage characteristics and are used in general government operations. These assets were referred to as multi-use heritage assets in SFFAS No. 6 and SFFAS No. 8.

General PP&E is often classified into two main categories, personal and real property. Personal property includes vehicles, machinery, furniture, equipment, and software. Real property is land, buildings, and generally anything built or constructed on land, growing on land, or attached to the land.

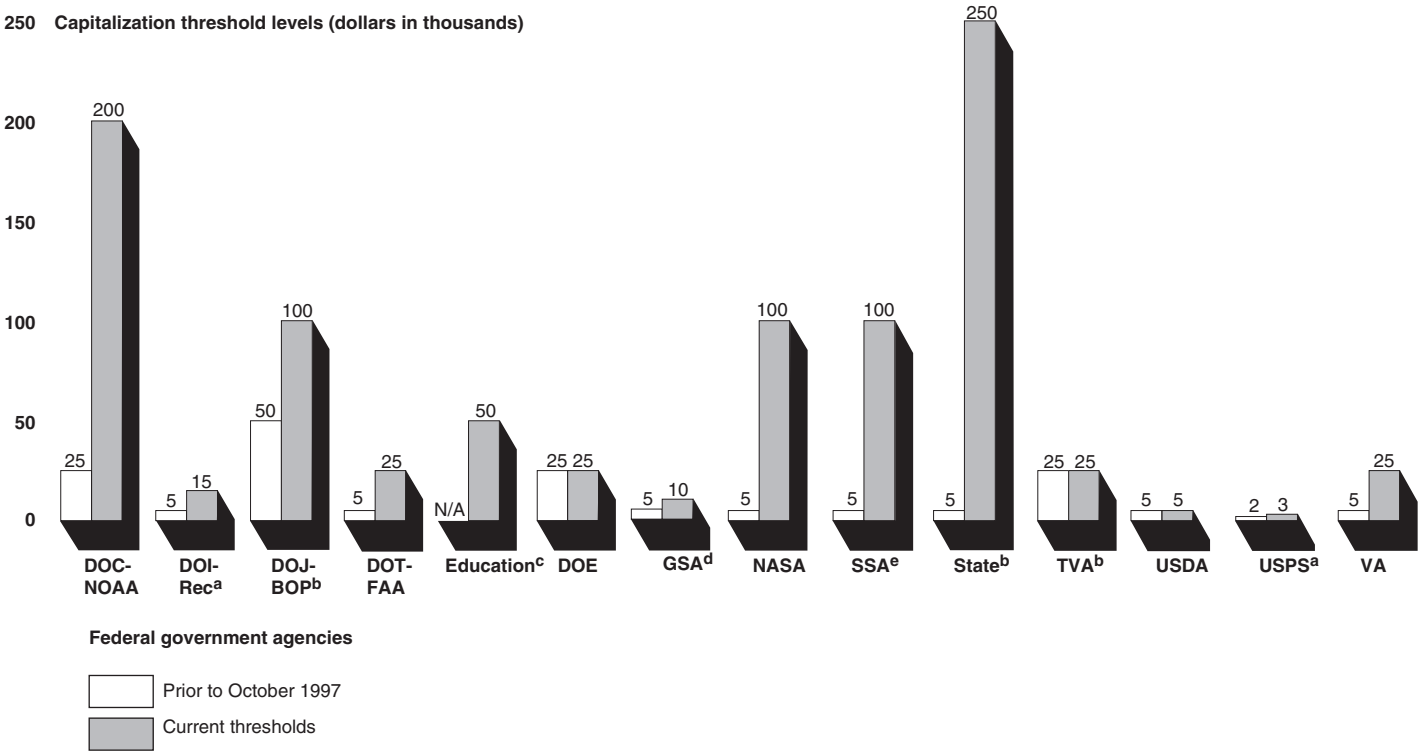
Federal Agency Capitalization Thresholds Have Risen Significantly and Are Substantially Higher than Private Sector Capitalization Thresholds

Capitalization threshold levels at federal agencies have risen significantly over the past 5 years. Over 60 percent of the agencies surveyed have at least doubled their capitalization thresholds in the past 5 years. Further, federal capitalization threshold levels are significantly higher than those reported by the 12 private sector entities we surveyed. The maximum federal capitalization threshold levels reported for personal and real property were much higher than those reported by the private sector companies. Inappropriate or excessive capitalization thresholds have a significant impact on financial reporting and related oversight issues and may not comply with SFFAS No. 6 requirements.

Federal Capitalization Thresholds Have Risen Significantly in the Past 5 Years

Nine out of the 14 agencies surveyed reported that they had increased their capitalization thresholds in the past 5 years by 100 percent or more, for at least one category of property (excluding software). Figure 1 displays the increases by agency. Six agencies increased the capitalization threshold by 400 percent or more, 2 raising the threshold from $5,000 to $25,000, 2 raising the threshold from $5,000 to $100,000, 1 raising the threshold from $25,000 to $200,000, and 1 raising the threshold from $5,000 to $250,000. Appendix III provides detailed lists of the current capitalization level for both personal and real property by federal agency.

Figure 1: Increase in Capitalization Threshold Levels at Federal Agencies



Note: Unless noted below, these are maximum reported capitalization threshold levels for real and personal property (excluding software) at 14 surveyed federal agencies.

[a]The numbers represent maximum reported capitalization threshold levels for personal property.

[b]The numbers represent maximum reported capitalization threshold levels for real property.

[c]Education did not have a consistent capitalization threshold policy prior to October 1997.

[d]GSA established a capitalization threshold of $5,000 in August 1998. Information prior to August 1998 was unavailable. The numbers represent maximum reported capitalization threshold levels for personal property.

[e]SSA increased its capitalization threshold to $100,000 in April 1996. Prior to April 1996, its threshold was $5,000. The numbers represent maximum reported capitalization threshold levels for personal property.

Source: GAO analysis of survey data.

Reasons given by the surveyed federal agencies for changing the capitalization thresholds included materiality, implementation of federal accounting standards, management decision, or external auditor recommendation.

Twelve out of 14 federal agencies surveyed responded that they had performed some type of formal analyses or studies to develop or validate the capitalization threshold level. In some instances, the studies concluded that the threshold level was too low, prompting agency management to increase the capitalization threshold. Many agencies' approaches to the capitalization threshold analyses involved applying varying threshold levels to PP&E balances to identify a capitalization level that resulted in a certain desired percentage of PP&E being captured on the balance sheet in relation to total PP&E. Although our survey asked for a brief description of the methodology used in the analyses, we did not request copies of the analyses from the federal agencies or assess the methodology or conclusions reached. We did note, however, that 5 of the 12 agencies solicited outside assistance in performing the analyses, and of those 5, 2 involved their respective offices of the inspector general.

Although DOD was not included in this review, the department holds a significant portion of federal PP&E. DOD's reported general PP&E holdings for fiscal year 2001 were $113.8 billion, net of accumulated depreciation, representing approximately 37 percent of the federal government's PP&E reported on the U.S. government's consolidated balance sheet. DOD's capitalization threshold has risen from $5,000 in 1994, to $50,000 in 1995, and to $100,000 in 1996, which remains the current level. DOD had contractors perform a study to validate its capitalization thresholds and useful life policies for personal and real property. We reviewed the contractors' work and agreed that certain limitations they cited in their reports—such as that the databases they analyzed may not have been appropriate, complete, and accurate—could directly affect the assessment of the adequacy of the capitalization threshold and useful life policies. The contractor recommended that DOD undertake similar periodic analyses in future years.

Further, federal agency capitalization thresholds varied widely. They ranged from $0 to $250,000, excluding computer software, where the capitalization threshold ranged from $5,000 to $5 million. The lack of consistency in capitalization threshold levels among federal agencies could potentially lead to reporting problems in the U.S. government's consolidated financial statements and performance measurement comparisons. For example, at some agencies major assets such as motor vehicles may be capitalized and at others they may not due to the varying capitalization threshold levels. As a result, the costs of vehicles used by certain agencies could be expensed in 1 fiscal year and not allocated to all the years benefiting from their use. Further, GAAP require that the

capitalization threshold, including any changes in the threshold during the reporting period, be disclosed on the financial statements. Treasury has not disclosed the capitalization threshold used in the consolidated financial statements, or the fact that many reporting agencies have different capitalization thresholds.

Despite the sharp increase in the capitalization threshold, almost all of the surveyed agencies responded that they maintained property records for PP&E not capitalized on the balance sheet, for purposes of safeguarding PP&E, supporting agency operations, or fulfilling external reporting requirements. For example, all surveyed agencies indicated that they have policies and procedures in place, such as bar coding and periodic inventories, for safeguarding and maintaining accountability over pilferable and sensitive items. We did not evaluate the adequacy of the design of the agency policies and procedures or the effectiveness of the controls or their implementation. Even though 13 of the 14 federal agencies in our survey reported that they maintain property records for PP&E not capitalized on the balance sheet, most were unable to provide the cumulative value of PP&E recorded in property records but not capitalized on the balance sheet as of the end of fiscal year 2000. Only the National Aeronautics and Space Administration (NASA) and the Federal Aviation Administration (FAA) responded with the cumulative value of PP&E not reported on their balance sheets as of September 30, 2000—approximately $4.9 billion and $1.6 billion, respectively. However, we noted that NASA's auditors for fiscal year 2001 reported a material weakness related to PP&E, so the amount NASA reported as being expensed may not be reliable.

Federal Capitalization Thresholds Differ Significantly from the Private Sector

Federal capitalization thresholds are significantly higher than those reported by the 12 private sector entities we surveyed. We found that the agency capitalization thresholds for personal property ranged from $3,000 to $200,000, and in some cases were 40 times higher than the maximum levels reported by the private sector participants. Table 1 compares the ranges of capitalization thresholds noted at the federal agencies surveyed to those of the private sector participants. Appendix IV provides the specific personal property responses for all survey participants by category.

Table 1: Capitalization Threshold Ranges for Personal Property

Personal property category	Range of threshold: Levels at federal agencies	Range of threshold: Levels at private sector companies
Equipment	$3,000 - $200,000	$250 - $5,000
Furniture and fixtures	3,000 - 100,000	250 - 5,000
Motor vehicles	0 - 200,000	250 - 5,000

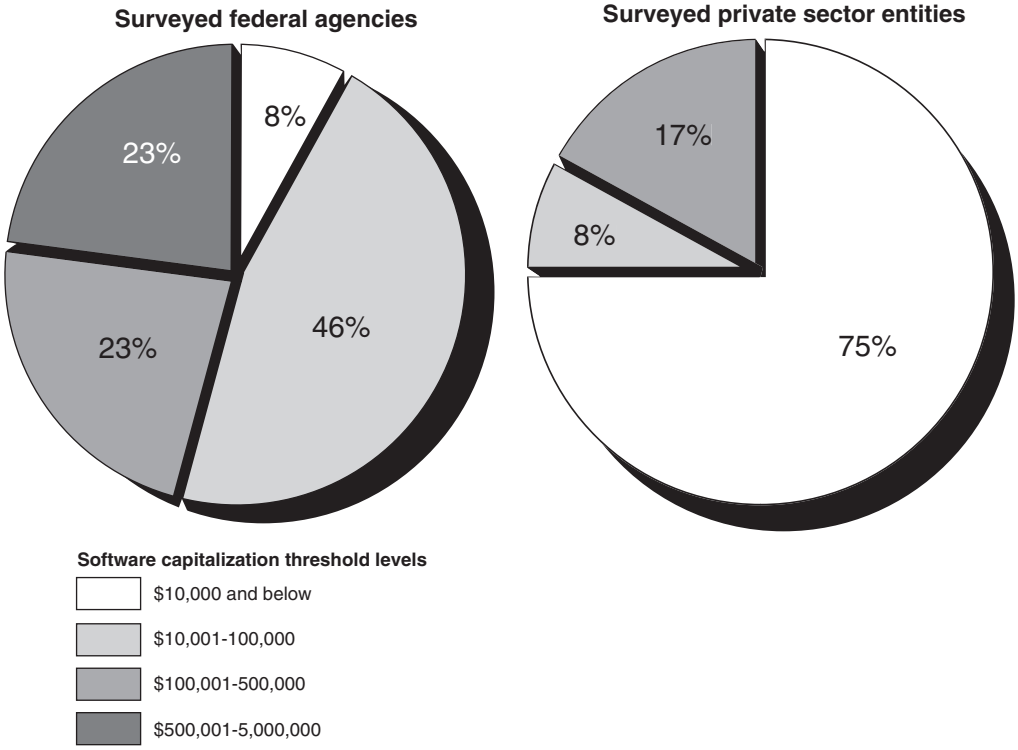
Source: GAO analysis of survey data.

As shown in table 1, private sector respondents' threshold levels for personal property ranged from as low as $250 up to $5,000. Under these threshold levels, office equipment costing $20,000 with an estimated useful life of 5 to 7 years, would not be capitalized at more than half (9 out of 14) of the federal agencies surveyed, but would be capitalized at all of the private sector company participants.

Five of the surveyed federal agencies responded as having a separate capitalization threshold level for bulk purchases. A bulk purchase policy generally refers to capitalization guidelines when acquiring significant asset quantities in bulk at one time, where the individual unit price falls below the original threshold. For example, the National Oceanic and Atmospheric Administration's (NOAA) policy is to capitalize a bulk procurement of $1 million or more for personal property with a unit price from $25,000 to its individual capitalization threshold of $200,000, if the items are identical. The Department of Education has a $500,000 bulk purchase policy, and the Social Security Administration (SSA) has a $10 million bulk purchase policy for computer hardware and software. Personal computers acquired individually would not be capitalized at many surveyed federal agencies under the current capitalization threshold levels, and bulk purchases of personal computers would have to rise to the capitalization threshold level, or higher at some agencies, as noted above, to be capitalized on the balance sheet. The remaining nine federal agencies responded that the capitalization threshold levels apply to both single item and bulk purchases of PP&E, as did the majority of the private sector companies surveyed. However, the few private sector respondents with bulk purchase policies indicate an emphasis on capitalizing assets and minimizing the impact on net income. For example, Pfizer responded that acquisitions of multiple like items would be capitalized if they exceed $10,000 in the aggregate, even though each item is under its $1,000 threshold level.

Certain federal agencies in our survey, as well as some private sector companies, reported capitalization thresholds specifically for software, classified as personal property on the balance sheet. The agencies' capitalization thresholds for software ranged from $5,000 to $5 million, or 20 times higher than the maximum level reported by the private sector participants. The private sector respondents that reported specific capitalization threshold levels for software indicated ranges from $1,000 to $250,000. Figure 2 displays the percentages of surveyed federal agencies and private sector companies at each capitalization threshold level for software. As shown in figure 2, 92 percent of the federal agencies surveyed have threshold levels greater than $10,000 for software, compared to the private sector, with 25 percent of respondents in that category. The majority of the private sector software capitalization threshold levels were $10,000 and below.

Figure 2: Percentage of Federal Agencies and Private Sector Companies at Various Software Capitalization Threshold Levels



Source: GAO analysis of survey data.

SFFAS No. 10, *Accounting for Internal Use Software*, effective for reporting periods after September 30, 2000, was cited by several federal agencies as the basis for establishing a separate threshold just for software or increasing their capitalization threshold levels for software. SFFAS No. 10 requires the capitalization of the full cost (direct and indirect) of internal use software whether it is commercial-off-the-shelf, contractor developed, or internally developed. A specific capitalization threshold for software, separate from the threshold for all other personal property, may be warranted at many agencies due to the varying and incremental nature of the costs that go into software development, such as salaries. However, the threshold level for software also varies quite significantly among the federal agencies surveyed, which could result in the consolidation and comparison problems discussed previously. Appendix V provides the specific software responses for all survey participants.

Capitalization thresholds for real property ranged from zero, or no threshold, indicating that all such assets are capitalized on the balance sheet, to $250,000, which is 50 times the highest level reported by the private sector participants. Table 2 displays the capitalization threshold ranges for real property at the federal agencies surveyed compared to those in the private sector. Appendix VI provides the specific real property responses for all survey participants by category.

Table 2: Capitalization Threshold Ranges for Real Property

	Range of threshold	
Real property category	**Levels at federal agencies**	**Levels at private sector companies**
Buildings	$0 - $200,000	$0 - $5,000
Building improvements	0 - 250,000	500 - 5,000
Other structures and facilities	0 - 200,000	0 - 5,000
Leasehold improvements	0 - 250,000	500 - 5,000

Source: GAO analysis of survey data.

Private sector respondents' threshold levels for real property ranged from $0 to $5,000. Under these threshold levels, a building costing $95,000 with an estimated useful life of 30 years would not be capitalized at some federal agencies surveyed, but would be capitalized at all of the private sector company participants. For example, Gillette, a large corporation with over

$10 billion in assets, has a uniform threshold level of $2,500 for both real and personal property, with the exception of software.

As shown in tables 1 and 2, the threshold levels in the private sector for most personal property and real property are relatively low, and more consistent with the $5,000 capitalization threshold level previously established for federal agencies in Title 2 of the GAO *Policy and Procedures Manual for Guidance of Federal Agencies*, in accordance with 31 U.S.C. 3511. In addition, under Federal Acquisition Regulations,[16] government contractors are required to capitalize all assets costing $5,000 or more.

Potential Impact of High Capitalization Thresholds on Financial Reporting

Our survey work was not designed to conclude on the reasonableness of the capitalization threshold levels being applied at the federal agencies or the private sector companies. However, the widely varying threshold levels among the federal agencies, the sharp increases in recent years, and the differences from private sector companies of considerable size in terms of reported PP&E and total assets raise some concerns. Inappropriate or excessive capitalization thresholds have a significant impact on financial reporting and related oversight issues and may not comply with SFFAS No. 6 requirements to capitalize all items that meet certain characteristics, such as a useful life of 2 years or more. FASAB believed that not specifying a threshold level, and allowing agencies broad latitude in establishing capitalization thresholds suited to their respective financial and operational conditions, would lead to a more cost-effective application of the accounting standard.[17] However, objectives outlined by FASAB in the SFFAC No. 1, such as (1) stewardship responsibility, (2) capturing the full cost of operations, and (3) reliable financial reporting, may not be met as a result of the wide range and significant increase in threshold levels that we identified in our survey.

Excessively high capitalization thresholds reduce the amount of federal assets that are reported on the balance sheet, distorting financial reporting by potentially jeopardizing the matching of costs to the appropriate period of asset utilization. For example, in February 2000, we reported that an

[16]Title 48, U.S. Code of Federal Regulations, Section 9904.404-40.

[17]SFFAS No. 6, *Accounting for Property, Plant, and Equipment*, Appendix A, Basis for Conclusions.

inappropriate capitalization threshold contributed to a material understatement in PP&E of approximately $1 billion, representing about 77 percent of the IRS's total PP&E balances as of September 30, 1999. IRS had been following the Department of the Treasury's standard $50,000 capitalization criterion, and now capitalizes most property and equipment regardless of the dollar amount, based upon the capitalization issues raised as a result of our financial audit of IRS.

Further, six of the agencies surveyed reported that they expensed a total of almost $2 billion in PP&E for the fiscal year ended September 30, 2000, and therefore did not report this amount on the U.S. government's consolidated balance sheet as assets. While the $2 billion is a relatively small amount compared to the total PP&E or total assets reported on the consolidated financial statements of the U.S. government, this amount is incomplete, as the remaining eight agencies surveyed could not readily provide the amount expensed for the same period as a result of the PP&E acquisition costs not meeting the capitalization threshold. An assessment of whether the capitalization threshold has a material effect on financial reporting is difficult to make if agencies cannot provide the amount of assets that does not meet the capitalization threshold and is therefore expensed in a given year.

Interestingly, one of our surveyed federal entities, USPS, which sets its rates and fees to recover its costs, reported a $3,000 personal property capitalization threshold and $5,000 real property threshold, which is more in line with the surveyed private sector companies' capitalization threshold levels. For example, Exxon Mobil Corporation, a global company with net PP&E of $90 billion as of December 31, 2000, also has a capitalization threshold of $3,000, excluding software. In fact, in looking at capitalization threshold levels for personal property in the private sector excluding software, all but 2 of the 12 participants had a threshold of $3,000 or less, and the remaining 2 had a $5,000 threshold.

As reported in our *High-Risk Series*,[18] some federal entities do not yet have reliable financial and operational information to measure performance based on the costs of providing goods and services and therefore appear to have little incentive to maintain assets on the balance sheet through lower capitalization thresholds. For example, we reported[19] in January 2001 that the Department of Agriculture (USDA) lacked financial accountability over billions of dollars of assets. FAA's financial management was also designated as high risk because of serious and long-standing accounting and financial management weaknesses, including property system issues. Reliable information on the costs of federal programs and activities, of which PP&E is a major factor, is crucial for effective management of government operations.

Federal Agencies' Estimated Useful Lives for Like Assets Are Similar

Useful lives for personal property ranged from 2 to 40 years among the surveyed federal agencies, but include a wide array of assets. Upon comparing the recovery periods for like assets, the range narrows. For example, the useful lives for motor vehicles ranged from 3 to 12 years in the federal agencies surveyed. Useful lives for real property at the surveyed federal agencies ranged from 5 to 100 years, which is a wide range that encompasses numerous and varying types of real property. The federal government's real property is quite diverse, and includes items such as office buildings, dams, laboratories, courthouses, postal facilities, and embassies. However, when comparing the useful lives for similar buildings or structures across the federal government, the recovery periods are similar. For example, 12 out of the 14 surveyed federal agencies indicated useful life classifications for buildings of 30 to 40 years.

The useful life policies within the federal government were generally similar to those found in the private sector. No significant differences were noted between the federal government and the private sector survey respondents in the useful life policies for certain personal property categories such as equipment, furniture and fixtures, motor vehicles, and software. The ranges of useful life classifications for both federal and private sector company participants are shown in table 3 for personal property and in table 4 for real property. Appendixes VII and VIII detail the

[18]GAO-01-263 and GAO-01-241 through GAO-01-262.

[19]U.S. General Accounting Office, *Major Management Challenges and Program Risks: Department of Agriculture*, GAO-01-242 (Washington, D.C.: January 2001).

useful life ranges for personal and real property for each survey participant.

Table 3: Useful Life Ranges for Personal Property

Personal property category	Useful life ranges (in years)	
	Federal agencies	Private sector companies
Equipment	2 - 40	2 - 25
Furniture and fixtures	4 - 20	3 - 20
Motor vehicles	3 - 12	2 - 10
Software	2 - 10	3 - 10

Source: GAO analysis of survey data.

As noted above, the useful life ranges by category at the surveyed federal agencies are similar to those at the surveyed private sector companies. The high useful life of 40 years for equipment pertains to certain items at the Department of Energy (DOE), such as compressors and metal tanks. If such equipment were excluded, the maximum useful life classification for equipment at the surveyed federal agencies would be 25 years—identical to that in the private sector.

Table 4: Useful Life Ranges for Real Property

Real property category	Useful life ranges (in years)	
	Federal agencies	Private sector companies
Buildings	5 - 75	10 - 50
Other structures and facilities	5 - 100	10 - 40
Other	5 - 75	5 - 50

Source: GAO analysis of survey data.

The few differences that we identified between federal agency and private sector useful lives are due to the different types of assets owned by the survey participants rather than any systemic differences in the useful life policies. For example, the maximum useful life classification for buildings was reported as 75 years by two surveyed agencies, the Department of the Interior's Bureau of Reclamation and USPS. At the Bureau of Reclamation, the building useful life range of 30 to 75 years was reported for service

facilities, which consist of houses, buildings, garages, and shops owned by the bureau and used in electric, irrigation, municipal and industrial, or multipurpose operations and are not included in the plant accounts of a specific project. At USPS, the 75-year building useful life was reported only for pre-July 1970 monumental (indicating stone or stone ornamentation) buildings. Other than these two specific classifications within the buildings category, the maximum useful life classification for buildings at the surveyed federal agencies would be 50 years, and identical to that in the private sector. Similarly, the 100-year useful life for other structures and facilities at the surveyed federal agencies was for dams and related property at the Bureau of Reclamation. The longest useful life reported by the private sector respondents is 40 years for other structures and facilities, but none of the private sector respondents reported an asset similar to a dam. We did not receive survey results from any private sector utility companies for comparison purposes because we were limited to the Private Sector Council (PSC) members that voluntarily participated in our survey.

Adequate useful life classifications also serve as a mechanism to achieve fair presentation of an entity's financial position and results of operations in accordance with GAAP. New additions to PP&E that replace old or obsolete assets generally occur as the useful lives of the older assets are reaching completion, and the typical financial statement impact of the removal of an almost fully depreciated asset or a fully depreciated asset is minimal to none. However, if the useful life assigned to an asset or a class of assets does not reflect its actual service life, then the financial statement impact could be greater. For example, if an asset is assigned a useful life that exceeds its actual service life, the preliminary result would be an overstatement on the agency's balance sheet and an understatement on its statement of net cost for a period.[20] Conversely, if an asset's designated useful life were lower than its actual service life, the preliminary result would be an understatement on the agency's balance sheet and an overstatement on its statement of net cost for a period.[21]

[20]The period would be equivalent to the difference between the assigned useful life and the actual service life.

[21]See footnote 19.

Observations

Our survey results identified widely varying capitalization threshold levels, sharp increases in recent years, and significant differences from private sector companies of comparable size. Because capitalization thresholds may have a significant effect on the consolidated financial statements of the U.S. government, this survey was designed as the first step in providing baseline information to analyze these significant PP&E policies and assess their impact on the financial reports of the U.S. government. In addition, agency management and auditors also have continuing responsibilities to ensure that established capitalization threshold levels are appropriate. These issues are especially critical for agencies that establish user fees based on actual costs and will become even more important as the government moves toward matching revenues and costs for performance measurement purposes. The information obtained as a result of our survey can be used as a tool for further analysis and assessment of these issues.

Comments and Our Evaluation

We provided a draft of this report to 14 federal agencies and 12 private sector companies that participated in our survey, as well as to the Department of the Treasury and OMB. We received comments from Treasury, OMB, and 4 of the 14 federal agencies surveyed, including USDA, the Department of the Interior (Bureau of Reclamation), NASA, and the Department of State (see appendixes XI through XV). Seven federal agencies, including the departments of Education, Energy, Justice (Bureau of Prisons (BOP)), Transportation (FAA), and Veterans Affairs (VA), as well as the Tennessee Valley Authority (TVA) and USPS, provided primarily editorial comments, which we have incorporated into the report as appropriate. The remaining 3 agencies, which include the Department of Commerce (NOAA), the General Services Administration (GSA), and SSA, reviewed a draft of this report and told us they had no comments. Three PSC members that participated in the survey, Allstate, McGraw-Hill, and PPG Industries, also provided primarily editorial comments, which we have incorporated into the report as appropriate.

The substantive comments we received from the Treasury, OMB, and federal entities had a common theme, in that they all generally took issue with comparing the capitalization threshold levels in the federal government to those in the private sector. For example, the Department of the Treasury stated that the private sector has income tax considerations that affect capitalization thresholds, but these are not an issue at federal agencies. In this regard, our private sector survey instrument (see appendix X) recognized this consideration by specifically asking for information

regarding practices for financial reporting, or book purposes, and not for income tax reporting. USDA referred to inherent differences between the government and the private sector in reporting cost and income. NASA and the State Department commented that the report did not acknowledge the private sector's profit objective, which they viewed as the main force behind its PP&E policies and practices, as distinctly different from the financial reporting objectives of the U.S. government.

Our views on asset capitalization are based upon two fundamental accounting concepts: the matching principle and materiality. The matching principle aims to assign costs to the proper period. In the case of capital assets, this is done through depreciation to recognize the use of the asset and can only occur if the asset is capitalized and not totally expensed when placed in service. The concept of materiality overlays the matching principle to provide relief from capitalizing and tracking assets that are immaterial to an entity's financial statements. The establishment of a capitalization threshold policy must be supported by a detailed analysis, anchored by these two fundamental principles of matching and materiality. Furthermore, capitalization thresholds should be periodically reevaluated to help ensure their continuing relevance. Our report provides baseline data that we believe could be useful to federal agencies in analyzing capitalization thresholds. For example, NASA's reported total assets as of September 30, 2000, were $34.5 billion, similar to Pfizer's reported $33.5 billion at its fiscal year-end of December 31, 2000. NASA's capitalization threshold for both real and personal property is $100,000 compared to Pfizer's $1,000 threshold. Further, NOAA's reported total assets at September 30, 2000, were $5.5 billion, similar to McGraw-Hill's reported $4.9 billion at its fiscal year-end of December 31, 2000. NOAA's capitalization threshold for both real and personal property is $200,000 compared to McGraw-Hill's $2,000 threshold.

Our survey work was not designed to conclude on the reasonableness of the capitalization threshold levels being applied at the federal agencies or the private sector companies nor do we draw any conclusions. However, the widely varying threshold levels among the federal agencies, the sharp increases in recent years, and the large differences from private sector companies of considerable size in terms of reported PP&E and total assets are issues that we plan to review further. Inappropriate or excessive capitalization thresholds can have a significant impact on financial reporting by reducing the amount of federal assets that are reported on the balance sheet and by jeopardizing the matching of costs to the appropriate period of asset utilization.

While certainly differences exist between federal financial reporting objectives and those in the private sector, there are similarities as well. Both federal financial statements and those of private sector companies seek to provide reliable, useful, and timely information to their users. Similar to private sector companies' responsibility to fairly state profits or net income, federal entities have a responsibility to fairly state the net cost of operations. This is also important in determining fees to be charged, in other efforts to recoup costs through any reimbursement arrangement, and in the ability to match costs with performance.

OMB's comments also included similar concerns related to comparing federal capitalization threshold levels to those in the private sector. In addition, OMB noted that a comparison to the capitalization threshold levels of state and local governments would be informative, and referred to a recent survey of state comptrollers, done by the National Association of State Comptrollers (NASC). The results of the survey were reported in the July 2002 newsletter of the National Association of State Auditors, Comptrollers and Treasurers. While the NASC survey and its reported results appeared after we had completed our fieldwork, OMB felt strongly that the survey and its results should be mentioned in our report. Although a review of the NASC survey was not within the scope of our work, we noted that a significant[22] portion of the states participating in the survey reported a $5,000 threshold, which is also the threshold required by the federal government for grant recipients' recovery of costs under OMB Circular A-87.[23] These thresholds, particularly those for personal property, are in line with those used by most of the private sector survey participants. Federal Acquisition Regulations[24] also require federal government contractors to apply a capitalization threshold not to exceed $5,000.

OMB, Treasury, and the Bureau of Reclamation took issue with our statement that the lack of consistency in capitalization threshold levels

[22]Of the 34 states that participated in NASC's survey, 70 percent use a $5,000 capitalization threshold level for personal property, and 30 percent use a $5,000 capitalization threshold level for real property.

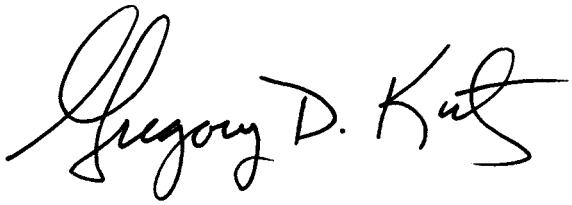
[23]OMB Circular A-87 establishes principles and standards for determining costs for federal awards carried out through grants, cost reimbursement contracts, and other agreements with state and local governments and federally recognized Indian tribal governments (governmental units).

[24]Title 48, U.S. Code of Federal Regulations, Section 9904.404-40.

among federal agencies could potentially lead to reporting problems in the U.S. government's consolidated financial statements and performance measurement comparisons. As stated in our report, individual capitalization threshold levels are permissible under federal accounting standards, and because each federal agency was established with a specific mission, they may possess unique assets to achieve their respective goals. At the same time, consistent treatment of like assets is critical to accurate performance measurement and reliable, relevant consolidated financial reporting. Management has a responsibility to ensure that the financial statements are fairly stated, in all material respects, and the auditor's role is to provide an opinion on that basic assertion, based on its work. As the auditor of the U.S. government's financial statements, we must ensure that the varying capitalization thresholds do not result in or contribute to a material misstatement at the consolidated level. The results of our survey can provide useful baseline data to OMB and Treasury in their respective roles, and to agencies and their auditors as they continue to periodically assess the adequacy of the capitalization threshold in terms of material impact on financial reporting.

We are sending copies of this report to the Chairman and Ranking Minority Member, Senate Committee on Governmental Affairs; the Chairman and Ranking Minority Member, House Committee on Government Reform; the Chairman and Ranking Minority Member, Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations, House Committee on Government Reform; and other interested congressional committees. We are also sending copies to the Chief Financial Officers, the Inspectors General and other interested parties, including the survey participants, the Private Sector Council, and the Chairman of the Federal Accounting Standards Advisory Board. In addition, the report will be available at no charge on the GAO Web site at http://www.gao.gov. If you

have any questions on this report, please contact me at (202) 512-9505 or Mary Arnold Mohiyuddin at (202) 512-3087.



Gregory D. Kutz
Director
Financial Management and Assurance

Objectives, Scope, and Methodology

The objectives of this report were to determine (1) what are the federal government's current capitalization threshold practices for PP&E and how such federal government policies compare to those practices being applied to PP&E in the private sector and (2) what are the useful life policies within the federal government and how they compare to those used in the private sector.

To fulfill these objectives, we developed two surveys, one for federal agencies and one for private sector companies. The surveys were used to collect information on capitalization thresholds and useful life policies, studies or analyses supporting those policies, and other related data that would assist us in determining the rationale for these PP&E policies as well as give us an indication of any differences or similarities between federal practices and private sector practices in the PP&E policy area.

For the federal government, we considered the 24 federal agencies responsible for annual audited financial statements as required under the CFO Act as expanded by the Government Management and Reform Act of 1994. We sent the survey to federal agencies with a reported $4 billion or more of net PP&E at September 30, 2000, except for DOD. For four agencies (Commerce, Interior, Justice, and Transportation), we surveyed a single component of the entire department due to the significant number of reporting components or because of the possibility of differing PP&E accounting policies for the various components. For each of those four agencies, we selected the component with the largest percentage of the total reported PP&E for that department. In addition, we randomly selected two federal agencies with net PP&E as of September 30, 2000, well below $4 billion to participate in the survey. We received completed surveys from all 14 federal agencies we contacted.

Although DOD is the largest holder of PP&E in the federal government, we chose not to include it in this survey. DOD had a study performed by contractors to validate its capitalization thresholds and useful life policies for personal and real property. We reviewed the contractors' work and agreed that certain limitations they cited in their reports pertaining to the reliability and completeness of the data could directly affect the assessment of the adequacy of the capitalization threshold and useful life policies. Nonetheless, the reported value of net PP&E for federal survey participants represents over half of the federal government's reported net PP&E as of September 30, 2000. Appendix II lists all agency survey participants.

We also surveyed member companies of the PSC, a nonprofit, nonpartisan public service organization committed to helping the federal government improve its efficiency, management, and productivity through cooperative sharing of knowledge. We sent our survey to all member companies, approximately 40, and received completed surveys from 12 PSC members. Appendix II contains the complete list of PSC survey participants.

We did not audit or verify the information provided by the federal agency or private sector survey participants in any way. We summarized the data collected from both survey groups, as reported to us by the respondents. We conducted telephone interviews with personnel at certain agencies and PSC members for follow-up questions or clarification purposes as needed.

The practical difficulties of conducting any survey may introduce errors, commonly referred to as nonsampling errors. For example, difficulties in how a particular question is interpreted, in the sources of information that are available to respondents, or in how the data are entered into a database can introduce unwanted variability into the survey results. We took steps in the development of the questionnaires, the data collection, and the data editing and analysis to minimize the nonsampling errors. For example, we pretested the questionnaires with a number of respondents to refine the survey instruments, we edited the surveys and called respondents to clarify answers, and we verified a sample of the survey data that was entered into our database for any keypunch errors.

We reviewed GAAP and concepts that related to PP&E accounting, as well as federal reporting guidelines issued by Treasury and OMB. In addition, we reviewed the financial statements and related notes to the financial statements of the federal agencies and private sector companies that participated in the survey.

We performed our work from May 2001 through February 2002 in accordance with generally accepted government auditing standards. We provided a draft of this report to 14 federal agencies and 12 private sector companies that participated in our survey, as well as to the Department of the Treasury and OMB. We received comments from Treasury, OMB, and 4 of the 14 federal agencies surveyed, including USDA, the Department of the Interior (Bureau of Reclamation), NASA, and the Department of State. Seven federal agencies, including the departments of Education, Energy, Justice (BOP), Transportation (FAA), and Veterans Affairs, as well as TVA and USPS, provided primarily editorial comments, which we have incorporated into the report as appropriate. The remaining 3, which

include the Department of Commerce (NOAA), GSA, and SSA reviewed a draft of this report and told us they had no comments. Three PSC members that participated in the survey, Allstate, McGraw-Hill, and PPG Industries, also provided primarily editorial comments, which we have incorporated into the report as appropriate.

Survey Participants

Federal agencies	Net PP&E at 9/30/00	Total assets at 9/30/00	Net PP&E/total assets (percentage)
Agriculture	$ 5.4	$ 124.4	4.3
Bureau of Prisons (DOJ)	4.6	6.7	68.7
Bureau of Reclamation (DOI)	13.2	20.1	65.7
Education	1.3 million	119.0	0.0
Energy (except PMA PP&E)	13.5	81.4	16.6
FAA (DOT)	11.5	27.2	42.3
GSA	15.7	22.2	70.7
NASA	25.5	34.5	73.9
NOAA (Commerce)	3.6	5.5	65.5
SSA	0.3	1,029.2	0.0
State	4.7	23.0	20.4
TVA	29.1	34.0	85.6
USPS	24.1	58.3	41.3
VA	11.6	44.0	26.4
Total	**$162.8**	**$1,629.5**	**10.0**

Note: All figures in billions, except where otherwise noted.

Source: GAO analysis of agency fiscal year 2000 accountability reports.

Private sector companies	Net PP&E at fiscal year-end in 2000	Total assets at fiscal year-end in 2000	Net PP&E/total assets (percentage)
Allstate	$1.0	$104.8	1.0
Boeing	8.8	42.0	21.0
ExxonMobil	89.8	149.0	60.3
Fluor	0.8	3.7	21.6
Gillette	3.6	10.4	34.6
Kaiser Permanente	7.6	14.2	53.5
McGraw-Hill	0.4	4.9	8.2
Meredith Corp.	0.2	1.4	14.3
Pfizer	9.4	33.5	28.1
PPG Industries	2.9	9.1	31.9
SBC Communications	47.2	98.7	47.8
Xerox	2.5	29.5	8.5
Total	**$174.2**	**$501.2**	**34.8**

Note: All figures in billions, except where otherwise noted.

Source: GAO analysis of financial statements in private sector company annual reports.

Capitalization Threshold Increases by Federal Agency

Federal agencies	Maximum personal property thresholds			
	Previous	Increase	Current	Percentage increase
Agriculture	$5,000	$0	$5,000	0
Bureau of Prisons	5,000	0	5,000	0
Bureau of Reclamation	5,000	10,000	15,000	200
Education	[a]	[a]	50,000	--
Energy	25,000	0	25,000	0
FAA	5,000	20,000	25,000	400
GSA	5,000	5,000	10,000	100
NASA	5,000	95,000	100,000	1900
NOAA	25,000	175,000	200,000	700
SSA	5,000	95,000	100,000	1900
State	25,000	0	25,000	0
TVA	25,000	0	25,000	0
USPS	2,000	1,000	3,000	50
VA	5,000	20,000	25,000	400

[a]Capitalization threshold prior to current level not reported by agency, therefore no increase calculated.

Source: GAO analysis of survey data.

Federal agencies	Maximum real property thresholds			
	Previous	Increase	Current	Percentage increase
Agriculture	$5,000	$0	$5,000	0
Bureau of Prisons	50,000	50,000	100,000	100
Bureau of Reclamation	0	0	0	0
Education	[a]	[a]	50,000	--
Energy	25,000	0	25,000	0
FAA	5,000	20,000	25,000	400
GSA	10,000	0	10,000	0
NASA	5,000	95,000	100,000	1900
NOAA	25,000	175,000	200,000	700
SSA	25,000	0	25,000	0
State	5,000	245,000	250,000	4900
TVA	25,000	0	25,000	0
USPS	5,000	0	5,000	0
VA	5,000	20,000	25,000	400

[a]Capitalization threshold prior to current level not reported by agency, therefore no increase calculated.

Source: GAO analysis of survey data.

Capitalization Thresholds for Personal Property

Federal agencies	Equipment	Furniture and fixtures	Motor vehicles
Agriculture	$5,000	$5,000	$5,000
Bureau of Prisons	5,000	[a]	5,000
Bureau of Reclamation	15,000	[a]	15,000
Education	50,000	50,000	[a]
Energy	25,000	25,000	25,000
FAA	25,000	25,000	25,000
GSA	10,000	10,000	10,000
NASA	100,000	100,000	100,000
NOAA	200,000	[a]	200,000
SSA	100,000	100,000	[a]
State	25,000	25,000	0
TVA	[b]	[b]	[b]
USPS	3,000	3,000	3,000
VA	25,000	25,000	25,000
Minimum federal	3,000	3,000	0
Maximum federal	200,000	100,000	200,000

[a]Federal agency did not report a capitalization threshold for this property category.

[b]TVA was not included in the above because it capitalizes entire projects instead of individual assets.

Source: GAO analysis of survey data.

Private sector companies	Equipment	Furniture and fixtures	Motor vehicles
Allstate	$250	$250	$250
Boeing	5,000	5,000	5,000
ExxonMobil	3,000	3,000	3,000
Fluor	1,500	1,500	1,500
Gillette	2,500	2,500	2,500
Kaiser Permanente	1,000	1,000	1,000
McGraw-Hill	2,000	2,000	2,000
Meredith Corp.	5,000	2,000	5,000
PPG Industries	3,000	3,000	3,000
Pfizer	1,000	1,000	1,000
SBC Communications	2,000	2,000	2,000
Xerox	3,000	3,000	3,000
Minimum private	250	250	250
Maximum private	5,000	5,000	5,000

Source: GAO analysis of survey data.

Capitalization Thresholds for Software

Federal agencies	Maximum
Agriculture	$100,000
Bureau of Prisons	5,000
Bureau of Reclamation	100,000
Education	50,000
Energy	750,000
FAA	200,000
GSA	1,000,000
NASA	100,000
NOAA	200,000
SSA	100,000
State	500,000
TVA	[a]
USPS	5,000,000
VA	25,000
Minimum federal	5,000
Maximum federal	5,000,000

[a]TVA was not included in the above because it capitalizes entire projects instead of individual assets. Also, it has no specific software threshold.

Source: GAO analysis of survey data.

Private sector companies	Maximum
Allstate	$250,000
Boeing	5,000
ExxonMobil	5,000
Fluor	10,000
Gillette	5,000
Kaiser Permanente	100,000
McGraw-Hill	250,000
Meredith Corp.	2,000
PPG Industries	3,000
Pfizer	1,000
SBC Communications	2,000
Xerox	3,000
Minimum private	1,000
Maximum private	250,000

Source: GAO analysis of survey data.

Capitalization Thresholds for Real Property

Federal agencies	Buildings	Building improvements	Other structures and facilities	Leasehold improvements
Agriculture	$5,000	$5,000	$5,000	$5,000
Bureau of Prisons	100,000	100,000	100,000	100,000
Bureau of Reclamation	0	0	0	0
Education	[a]	[a]	[a]	50,000
Energy	25,000	25,000	25,000	25,000
FAA	25,000	25,000	25,000	25,000
GSA	0	10,000	10,000	10,000
NASA	100,000	100,000	100,000	100,000
NOAA	200,000	[a]	200,000	200,000
SSA	0	[a]	[a]	25,000
State	0	250,000	[a]	250,000
TVA	25,000	25,000	25,000	25,000
USPS	0	5,000	[a]	5,000
VA	25,000	25,000	25,000	25,000
Minimum federal	0	0	0	0
Maximum federal	200,000	250,000	200,000	250,000

[a]Federal agency did not report a capitalization threshold for this property category.

Source: GAO analysis of survey data.

Private sector companies	Buildings	Building improvements	Other structures and facilities	Leasehold improvements
Allstate	$0	$500	$0	$500
Boeing	5,000	5,000	5,000	5,000
ExxonMobil	3,000	3,000	3,000	3,000
Fluor	1,500	1,500	1,500	1,500
Gillette	2,500	2,500	2,500	2,500
Kaiser Permanente	0	5,000	5,000	5,000
McGraw-Hill	2,000	2,000	2,000	2,000
Meredith Corp.	5,000	5,000	5,000	5,000
PPG Industries	3,000	3,000	3,000	3,000
Pfizer	1,000	1,000	1,000	1,000
SBC Communications	2,000	2,000	2,000	2,000
Xerox	3,000	3,000	3,000	3,000
Minimum private	0	500	0	500
Maximum private	5,000	5,000	5,000	5,000

Source: GAO analysis of survey data.

Useful Life Ranges for Personal Property (in Years)

Federal agencies	Equipment	Furniture and fixtures	Motor vehicles
Agriculture	5	8	6
Bureau of Prisons	10	N/R	10
Bureau of Reclamation	2 - 25	10 - 20	6 - 10
Education	3	5	N/R
Energy	5 - 40	varies	5 - 8
FAA	7	7	5
GSA	5	5	varies
NASA	5 - 15	10	10
NOAA	8 - 20	N/R	6
SSA	7	10	N/R
State	5 - 8	4 - 12	3 - 6
TVA	5 - 20	5 - 10	6 - 12
USPS	3 - 10	5 - 10	6 - 12
VA	3 - 15	10 - 15	5 - 10
Range	2 - 40	4 - 20	3 - 12

Note: N/R indicates that survey participant either did not respond to a useful life classification for this particular category of personal property or the category did not apply to the participant.

Source: GAO analysis of survey data.

Private sector companies	Equipment	Furniture and fixtures	Motor vehicles
Allstate	3 - 10	10	3
Boeing	3 - 11	10	N/R
ExxonMobil	3 - 5	15	5 - 10
Fluor	5 - 7	10	5
Gillette	5 - 20	3 - 15	3 - 7
Kaiser Permanente	3 - 20	5 - 20	4
McGraw-Hill	2 - 10	10	3
Meredith Corp.	3 - 10	5 - 10	3 - 10
PPG Industries	5 - 25	3 - 20	6 - 10
Pfizer	3 - 5	13	4
SBC Communications	10	15	8
Xerox	3 - 12	15	4 - 5
Range	2 - 25	3 - 20	3 - 10

Note: N/R indicates that survey participant either did not respond to a useful life classification for this particular category of personal property or the category did not apply to the participant.

Source: GAO analysis of survey data.

Useful Life Ranges for Real Property (in Years)

Federal agencies	Buildings	Other structures and facilities	Other[a]
Agriculture	30	20 - 50	10 - 50
Bureau of Prisons	30	20	20
Bureau of Reclamation	30 - 75	25 - 100	30 - 75
Education	N/R	N/R	N/R
Energy	25 - 50	25 - 50	varies
FAA	40	10 - 20	10
GSA	30	30	5 - 20
NASA	40	15	15
NOAA	10 - 40	N/R	varies
SSA	50	N/R	6
State	30	N/R	10
TVA	20 - 40	20 - 40	20
USPS	30 - 75	10	N/R
VA	5 - 40	5 - 40	5 - 40
Range	5 - 75	5 - 100	5 - 75

Note: N/R indicates that survey participant either did not respond to a useful life classification for this particular category of real property or the category did not apply to the participant.

[a]Other includes any real property that is not a building, structure, or facility.

Source: GAO analysis of survey data.

Private sector companies	Buildings	Other structures and facilities	Other[a]
Allstate	40	N/R	N/R
Boeing	45	N/R	10 - 25
ExxonMobil	20 - 50	20 - 30	20 - 30
Fluor	20 - 30	N/R	20 - 30
Gillette	10 - 40	40	14 - 20
Kaiser Permanente	20 - 40	10 - 40	5 - 25
McGraw-Hill	50	N/R	50
Meredith Corp.	10 - 45	20	10 - 20
PPG Industries	20 - 50	N/R	20 - 30
Pfizer	33	N/R	33
SBC Communications	44	N/R	N/R
Xerox	25 - 50	N/R	20
Range	10 - 50	10 - 40	10 - 50

Note: N/R indicates that survey participant either did not respond to a useful life classification for this particular category of real property or the category did not apply to the participant.

[a]Other includes any real property that is not a building, structure, or facility.

Source: GAO analysis of survey data.

Federal Agency Survey

United States General Accounting Office

GAO
Accountability · Integrity · Reliability

Survey of Federal Property, Plant, and Equipment (PP&E) Policies

Introduction

On November 30, 1995, the Federal Accounting Standards Advisory Board (FASAB) issued Statement of Federal Financial Accounting Standards (SFFAS) No. 6, "Accounting for Property, Plant, and Equipment." SFFAS No. 6, effective for fiscal years beginning with 1998, defined property, plant, and equipment (PP&E) and its various categories, as well as the minimum disclosure requirements for reporting general PP&E. Minimum disclosure requirements for reporting general PP&E on the balance sheet include:

- Cost, associated accumulated depreciation, and book value by major class;
- Estimated useful lives for each major class;
- Method(s) of depreciation for each major class;
- Capitalization threshold(s), including any changes in threshold(s) during the period; and
- Restrictions on the use or convertability of general PP&E.

Since organization capitalization thresholds and useful life policies have a direct impact on PP&E information reported on organization financial statements, the propriety of these policies is critical to the reliability and usefulness of reported PP&E and the overall financial statements.

The objective of this survey is to gather information on your organization's capitalization thresholds and useful life category policies, studies or analyses supporting those policies, and other related data to determine how this information may impact financial statement reporting governmentwide. This survey is divided into three areas: (I) Capitalization Thresholds and Accountability; (II) Depreciation/Useful Lives; and (III) Other Comments.

Your participation in this survey is essential for obtaining a governmentwide perspective of PP&E policies and for ensuring the reliability and usefulness of PP&E data. We will be contacting your organization to confirm that the survey has been received and to answer any questions.

Instructions

1. The survey should be completed by your entity's Office of the Chief Financial Officer, or by other organization personnel authorized to provide the information requested.

2. We would appreciate if you would return the survey no later than November 9, 2001. Due to recent events, we request that you fax the completed survey to Mary Arnold Mohiyuddin at (202) 512-9193. We also request that you return the survey by mail using the enclosed postage-paid envelope. We recommend that you keep a photocopy for your records. If the envelope is misplaced, the return address is:

   U.S. General Accounting Office
   Mrs. Mary Arnold Mohiyuddin
   441 G Street, NW, Room 5T45
   Washington, D.C. 20548

If you have any questions, please contact Mrs. Mary Arnold Mohiyuddin at (202) 512-3087 or email mohiyuddinm@gao.gov or Mr. Cleggett Funkhouser at (202) 512-5126 or email funkhouserc@gao.gov.

Thank you for your cooperation and assistance.

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Please provide the following information so that we may contact you if further clarification is needed:

Organization: _____

Contact Name: _____

Title: _____

Phone: (____)_____

Email address: _____

I. Capitalization Thresholds and Accountability

1. What dollar threshold level(s), other factors that impact capitalization, and effective date(s) does your organization use for capitalizing general PP&E assets for financial reporting purposes?

   [Please provide dollar threshold levels for each different asset type(s), including personal property (e.g., equipment and software), real property (e.g., buildings, structures, and land), capital improvements, leasehold improvements, other. Also provide any other factor(s), such as useful life, that impact capitalization. Finally, provide the effective date for each of the current dollar threshold level(s).]

Types of general PP&E Assets	**Dollar Threshold Level**	**Other Factors that Impact Capitalization** *(e.g., useful life)*	**Effective Date** *(mm/yyyy)*
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____

2. Does your organization have a different capitalization dollar threshold for bulk purchases of PP&E than for purchases of a single item? *(Check one.)*

   1. ❒ Yes ➜ Please describe: _____
   _____
   _____

   2. ❒ No

2

3. To what extent, if any, did each of the following factors contribute to the establishment of your organization's current capitalization dollar threshold level(s)? *(Check one box in each row.)*

Factors	To a very great extent (1)	To a great extent (2)	To a moderate extent (3)	To some or little extent (4)	To no extent (5)
External auditor recommendation					
Materiality in relation to the overall financial statements					
Industry practice					
Other - please specify:_____ _____					

4. Have any of your organization's capitalization dollar threshold level(s) changed within the past 5 years? *(Check one.)*

1. ❒ Yes ➜ ***Continue with question 5.***
2. ❒ No ➜ ***Skip to question 7.***

5. For those assets for which capitalization dollar threshold levels have changed in the past 5 years, what was your organization's previous capitalization dollar threshold level(s)?
[Please provide levels for different asset types, if applicable. Also provide any other factor(s) that impact capitalization, such as useful life. Finally, provide the effective date for each of the threshold level(s).]

PP&E Asset Type	Previous Dollar Threshold Level	Other Factors that Impact Capitalization *(e.g., useful life)*	Effective Date *(mm/yyyy)*
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____
_____	$ _____	_____	___/_____

3

6. Which of the following are reasons why the capitalization dollar threshold level(s) changed? *(Check all that apply.)*

   1. ❒ Implementation of Statement of Federal Financial Accounting Standards (SFFAS) No. 6, Accounting for Property, Plant, and Equipment
   2. ❒ Management decision – please explain: _____
   3. ❒ External auditor recommendation
   4. ❒ Other – please specify: _____

7. Within the past 5 years, has there been any formal analyses performed (in-house or external) to develop (or validate) your organization's capitalization dollar threshold level(s)? *(Check one.)*

   1. ❒ Yes ➜ How many analyses were performed? _____ ➜ ***Continue with question 8.***
   2. ❒ No ➜ ***Skip to question 12.***

8. Which of the following group(s) performed your analyses and when were they completed? *(Check all that apply and enter date(s) of completion - mm/yyyy.)*

   1. ❒ Internal ➜ Date of completion: ____/_____
   2. ❒ Consultant ➜ Date of completion: ____/_____
   3. ❒ Inspector General's Office ➜ Date of completion: ____/_____
   4. ❒ Independent Public Accountant ➜ Date of completion: ____/_____
   5. ❒ Other – please specify: _____ ➜ Date of completion: ____/_____

9. Which of the following <u>best describes</u> the conclusion of the <u>most recent</u> analysis? *(Check one.)*

   1. ❒ Dollar threshold level(s) appeared reasonable
   2. ❒ Dollar threshold level(s) did not appear reasonable, new dollar threshold level proposed ➜ Enter proposed dollar threshold: $ _____
   3. ❒ Dollar threshold level(s) did not appear reasonable, but no new dollar threshold level proposed
   4. ❒ Inconclusive analysis
   5. ❒ Other - please specify: _____

10. If a new dollar threshold level was proposed as a result of the most recent analysis, was it implemented at your organization? *(Check one.)*

    1. ❒ Yes
    2. ❒ No ➜ Explain why: _____
    3. ❒ Not applicable, new dollar threshold level was not proposed

4

11. Please describe, in as much detail as possible, the methodology that was applied in performing the most recent analysis?

_____
_____
_____
_____
_____
_____
_____

12. Which of the following factors does your organization consider in determining whether additions/modifications to existing property are capitalized? *(Check all that apply.)*

1. ❒ Capitalize if the cost of additions/modifications meets or exceeds the capitalization dollar threshold
2. ❒ Capitalize regardless of cost if additions/modifications to an existing capitalized asset
3. ❒ Capitalize if the additions/modifications extend the useful life or capacity of the asset
4. ❒ Other – please specify:_____

_____

13. Does your organization maintain property records for PP&E not capitalized on the balance sheet? *(Check one.)*

1. ❒ Yes ➜ ***Continue with question 14.***
2. ❒ No ➜ ***Skip to question 16.***

14. What is your organization's objective in maintaining property records for PP&E not capitalized on the balance sheet? *(Check all that apply.)*

1. ❒ Information needed for agency operations
2. ❒ Information needed to track items for safeguarding and other controls
3. ❒ Information needed for external reporting purposes (e.g., regulatory, Congressional, etc.)
4. ❒ Other – please specify: _____

_____

15. What was the cumulative value of PP&E recorded in property records, **but not capitalized on the balance sheet**, as of September 30, 2000?

$_____ ❒ Information not available

16. Please estimate the value of PP&E expensed as a result of not meeting or exceeding your organization's dollar threshold level for the fiscal year ending September 30, 2000.

$_____ ❒ Information not available

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17. Do your auditors address your organization's capitalization policy, such as the adequacy of the dollar threshold level(s), as part of their audit of your organization's annual financial statements? *(Check one.)*

    1. ❒ Yes
    2. ❒ No
    3. ❒ Not known

18. Does your organization use barcoding or any other asset control procedure(s) for PP&E? *(Check one.)*

    1. ❒ Yes, for all PP&E (i.e., capitalized and non-capitalized)
    2. ❒ Yes, but only for capitalized PP&E
    3. ❒ Yes, but only for non-capitalized PP&E
    4. ❒ No ➜ ***Skip to question 20.***

19. Please describe your asset control procedure(s).

    _____
    _____
    _____
    _____
    _____

20. Other than the asset control procedures you specified in questions 18 and 19, does your organization have a specific policy or procedure(s) for safeguarding sensitive and/or pilferable items (e.g., laptop computers, cell phones, etc.)? *(Check one.)*

    1. ❒ Yes ➜ Please describe policy: _____
    _____
    _____

    2. ❒ No

21. Please describe how your organization accounts for computer hardware. (Please distinguish purchases versus lease arrangements and issues related to personal computers versus mainframes.)

    _____
    _____
    _____
    _____
    _____
    _____
    _____

6

22. Does your organization have internally developed software? *(Check one.)*

    1. ❒ Yes ➜ ***Continue with question 23.***
    2. ❒ No ➜ ***Skip to question 25.***

23. Does your organization capitalize internally developed software in accordance with Statement of Federal Financial Accounting Standard (SFFAS) No. 10, Accounting for Internal Use Software? *(Check one.)*

    1. ❒ Yes
    2. ❒ No ➜ Please explain: _____

24. Does your organization have any process(es) in place to track internally developed software costs? *(Check one.)*

    1. ❒ Yes
    2. ❒ No

25. Does your organization have any leased PP&E recorded as capital leases? *(Check one.)*

    1. ❒ Yes
    2. ❒ No

26. Does your organization have a procedure in place for leased PP&E to determine whether they should be recorded as capital leases? *(Check one.)*

    1. ❒ Yes ➜ Please describe: _____
    2. ❒ No

27. Does your organization currently own property in the possession of government contractors? *(Check one.)*

    1. ❒ Yes ➜ ***Continue with question 28.***
    2. ❒ No ➜ ***Skip to question 31.***

28. Does your organization have only one capitalization dollar threshold for property in the possession of government contractors or does it have multiple thresholds depending on the property type? *(Check one. Please enter dollar threshold amount(s) and property type(s), if applicable.)*

    1. ❒ One dollar threshold for property in the possession of government contractors
       (Please enter dollar threshold amount.)

       $ _____

    2. ❒ Different dollar thresholds for different types of property. *(Please enter dollar thresholds by type of property.)*

       $ _____ ➜ Property Type: _____
       $ _____ ➜ Property Type: _____
       $ _____ ➜ Property Type: _____
       $ _____ ➜ Property Type: _____

29. Is the dollar threshold level for property in the possession of government contractors different from that for agency-held property? *(Check one.)*

    1. ❒ Yes ➜ Please explain: _____
       _____

    2. ❒ No

30. Who maintains the records for property in the possession of contractors? *(Check all that apply.)*

    1. ❒ Your agency
    2. ❒ Government contractor
    3. ❒ Outsource company
    4. ❒ Other - Please specify: _____

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II. Depreciation/Useful Lives

31. For depreciation purposes, how many years (useful life) does your organization use to depreciate the following real property classifications? *(Check all that apply and enter the useful life in years. For your convenience, feel free to attach your own schedule of real property classifications and their useful lives in lieu of responding to this question.)*

1. ❒ Buildings ➜ _____ years
2. ❒ Other Structures - Please specify: _____ ➜ _____ years
   _____ ➜ _____ years
   _____ ➜ _____ years
3. ❒ Leasehold Improvements ➜ _____ years
4. ❒ Facilities - Please specify: _____ ➜ _____ years
   _____ ➜ _____ years
   _____ ➜ _____ years
5. ❒ Capital Leases ➜ _____ years
6. ❒ Other - Please specify: _____ ➜ _____ years
   _____ ➜ _____ years
   _____ ➜ _____ years
   _____ ➜ _____ years

32. For depreciation purposes, how many years (useful life) does your organization use to depreciate the following personal property classifications? *(Check all that apply and enter the useful life in years. For your convenience, feel free to attach your own schedule of personal property classifications and their useful lives in lieu of responding to this question.)*

1. ❒ Equipment ➜ _____ years
2. ❒ Software ➜ _____ years
3. ❒ Furniture and Fixtures ➜ _____ years
4. ❒ Motor Vehicles ➜ _____ years
5. ❒ Property in the possession of contractors (by type) ➜ _____ type _____ years
   _____ type _____ years
   _____ type _____ years
6. ❒ Other – please specify: _____ ➜ _____ years
   _____ ➜ _____ years
   _____ ➜ _____ years
   _____ ➜ _____ years
   _____ ➜ _____ years

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33. Which of the following is used by your organization for assigning useful life categories to PP&E? *(Check all that apply.)*

1. ❒ Organization historical experience
2. ❒ IRS table
3. ❒ OMB circular A-76, Appendix 3 (Useful Life and Disposal Value Table estimated by Defense Logistics Agency.)
4. ❒ Other - please specify:_____

34. Which of the following best describes the depreciation method used by your organization? *(Check one.)*

1. ❒ Straight Line Method
2. ❒ Decreasing Charge Method (such as sum-of-years digits, or double-declining balance)
3. ❒ Activity Method
4. ❒ Accelerated Method
5. ❒ Other - please specify: _____

35. Within the past 5 years, have there been any formal analyses performed (in-house or external) to develop or validate your organization's useful life policies? *(Check one.)*

1. ❒ Yes ➜ ***Continue with question 36.***
2. ❒ No ➜ ***Skip to question 40.***

36. Who performed these analyses and when were they completed? *(Check all that apply and enter date(s) of completion - mm/yyyy.)*

1. ❒ Internal ➜ Date of completion: ____/_____
2. ❒ Consultant ➜ Date of completion: ____/_____
3. ❒ Inspector General's Office ➜ Date of completion: ____/_____
4. ❒ Independent Public Accountant ➜ Date of completion: ____/_____
5. ❒ Other – please specify:_____ ➜ Date of completion: ____/_____

37. Which of the following, if any, <u>best describes</u> the conclusion of the <u>most recent</u> analysis? *(Check one.)*

1. ❒ Useful life policy appeared reasonable
2. ❒ Useful life policy did not appear reasonable, new useful life policy proposed ➜ Please explain:
_____
_____
3. ❒ Useful life policy did not appear reasonable, but no new policy proposed
4. ❒ Inconclusive results
5. ❒ Other, please specify: _____

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38. If a different useful life policy was proposed as a result of the most recent analysis, was it implemented at your organization? *(Check one.)*

    1. ❒ Yes ➜ Please describe the new policy: _____

    2. ❒ No ➜ Explain why: _____

    3. ❒ Not applicable, new useful life category was not proposed.

39. Please describe, in as much detail as possible, the methodology that was applied in performing the most recent analysis?

    _____

40. Do your auditors address the adequacy of your organization's useful life categories as part of their audit of your organization's annual financial statements? *(Check one.)*

    1. ❒ Yes
    2. ❒ No
    3. ❒ Not known

41. Approximately what percentage of your organization's PP&E that is still in use is fully depreciated? *(Check one.)*

    1. ❒ None
    2. ❒ 1-5%
    3. ❒ 6-10%
    4. ❒ 11-15%
    5. ❒ 16-20%
    6. ❒ Greater than 20%
    7. ❒ Not known

42. Which of the following best describes how your organization treats fully depreciated PP&E assets? *(Check one.)*

    1. ❒ Fully depreciated PP&E are removed from property records immediately
    2. ❒ Fully depreciated PP&E are maintained on subsidiary records if asset is still in use
    3. ❒ Fully depreciated PP&E are removed from property records but tracked by another means
    4. ❒ Other - please explain: _____

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III. Other Comments

43. If you have any comments concerning PP&E policies or you would like to elaborate on any of your answers, please use the space below. Be sure to indicate the question number beside your comment. If you wish, you may attach additional pages to this survey.

Thank you for your assistance!

12

Private Sector Company Survey

United States General Accounting Office

GAO
Accountability • Integrity • Reliability

Survey of Private Sector Council Members Regarding Certain Property, Plant, and Equipment (PP&E) Policies

Introduction

On November 30, 1995, the Federal Accounting Standards Advisory Board (FASAB) issued Statement of Federal Financial Accounting Standards (SFFAS) No. 6, "Accounting for Property, Plant, and Equipment." SFFAS No. 6, effective for fiscal years beginning with 1998, defined property, plant, and equipment (PP&E) and its various categories, as well as the minimum disclosure requirements for reporting general PP&E. Minimum disclosure requirements for reporting general PP&E on the balance sheet include:

- Cost, associated accumulated depreciation, and book value by major class;
- Estimated useful lives for each major class;
- Method(s) of depreciation for each major class;
- Capitalization threshold(s), including any changes in threshold(s) during the period; and
- Restrictions on the use or convertability of general PP&E.

Since organization capitalization threshold and useful life policies have a direct impact on PP&E information reported on organization financial statements, the propriety of these policies is critical to the reliability and usefulness of reported PP&E and the overall financial statements. Therefore, we are surveying capitalization threshold and useful life policies in effect at federal agencies and seeking similar information from private industry.

The objective of this survey is to gather information on private sector companies' capitalization threshold and useful life category policies, studies or analyses supporting those policies, and other related data to obtain a perspective on how these policies are applied in private industry. This survey is divided into three areas: (I) Capitalization Thresholds and Accountability; (II) Depreciation/Useful Lives; and (III) Other Comments.

Your participation in this survey will assist us in obtaining information that could potentially be used by federal agencies to strengthen financial reporting and asset accountability government-wide.

Instructions

1. The survey should be completed by your entity's Office of the Chief Financial Officer, or by other organization personnel authorized to provide the information requested.

2. We would appreciate if you would return the survey no later than November 30, 2001. We request that you fax the completed survey to Mary Arnold Mohiyuddin at (202) 512-9193. You may mail it in addition to the facsimile to the following address:

   U.S. General Accounting Office
   Mrs. Mary Arnold Mohiyuddin
   441 G Street, NW, Room 5T45
   Washington, D.C. 20548

If you have any questions, please contact Mrs. Mary Arnold Mohiyuddin at (202) 512-3087 or email mohiyuddinm@gao.gov or Lisa Warde at (404) 679-1936 or email wardel@gao.gov.

Thank you for your cooperation and assistance.

1

Please provide the following information so that we may contact you if further clarification is needed:

Organization: _____

Contact Name: _____

Title: _____

Phone: (_____) _____

Email address: _____

I. Capitalization Thresholds and Accountability

1. What dollar threshold level(s) and effective date(s) does your organization use for capitalizing general PP&E assets for financial reporting purposes?

   [Please provide dollar threshold levels for each different asset type(s), including personal property (e.g., equipment and software), real property (e.g., buildings, structures, and land), capital improvements, leasehold improvements, other. Also, provide the effective date of implementation for each of the current dollar threshold level(s).]

Asset Type	Dollar Threshold Level	Date Threshold Level Implemented *(mm/yyyy)*
_____	$ _____	___/_____
_____	$ _____	___/_____
_____	$ _____	___/_____
_____	$ _____	___/_____
_____	$ _____	___/_____
_____	$ _____	___/_____
_____	$ _____	___/_____
_____	$ _____	___/_____
_____	$ _____	___/_____

2. Does your organization have a different capitalization dollar threshold for bulk purchases of PP&E than for purchases of a single item? *(Check one.)*

   1. ❒ Yes ➜ Please describe: _____
   _____
   _____

   2. ❒ No

2

3. Which of the following statements best describes the origin of your organization's current capitalization dollar threshold levels? *(Check one.)*

   1. ❒ Established internally by management, based on materiality
   2. ❒ Established internally by management, based on industry practice
   3. ❒ Established internally by management, based on other ➜ Please describe: _____
   4. ❒ Recommended by auditors
   5. ❒ Recommended by others ➜ Please describe: _____
   6. ❒ Other not indicated above ➜ Please describe: _____

4. Within the past 5 years, has there been any formal analyses performed (in-house or external) to develop or validate your organization's capitalization dollar threshold level(s)? *(Check one.)*

   1. ❒ Yes ➜ How many analyses were performed? _____ ➜ ***Continue with question 5.***
   2. ❒ No ➜ ***Skip to question 9.***

5. Which of the following group(s) performed your analyses and when were they completed? *(Check all that apply and enter date(s) of completion - mm/yyyy.)*

   1. ❒ Internal ➜ Date of completion: ____/_____
   2. ❒ Consultant ➜ Date of completion: ____/_____
   3. ❒ Independent Public Accountant ➜ Date of completion: ____/_____
   4. ❒ Other – please specify: _____ ➜ Date of completion: ____/_____

6. Which of the following best describes the conclusion of the most recent analysis? *(Check one)*

   1. ❒ Dollar threshold level(s) appeared reasonable
   2. ❒ Dollar threshold level(s) did not appear reasonable, new dollar threshold level proposed ➜ Enter proposed dollar threshold: $ _____
   3. ❒ Dollar threshold level(s) did not appear reasonable, but no new dollar threshold level proposed
   4. ❒ Inconclusive analysis
   5. ❒ Other - please specify: _____

7. If a new dollar threshold level was proposed as a result of the most recent analysis, was it implemented at your organization? *(Check one.)*

   1. ❒ Yes
   2. ❒ No ➜ Explain why: _____
   3. ❒ Not applicable, new dollar threshold level was not proposed

3

8. Please describe in as much detail as possible, the methodology that was applied in performing the most recent analysis?

_____
_____
_____
_____
_____
_____
_____

9. Which of the following factors does your organization consider in determining whether additions/modifications to existing property are capitalized? *(Check all that apply.)*

1. ❒ Capitalize if the cost of additions/modifications meet or exceed the capitalization dollar threshold
2. ❒ Capitalize regardless of cost if additions/modifications are to an existing capitalized asset
3. ❒ Capitalize if the additions/modifications extend the useful life or capacity of the asset
4. ❒ Other – please specify:_____

10. Does your organization maintain property records for PP&E not capitalized on the balance sheet? *(Check one.)*

1. ❒ Yes ➜ ***Continue with question 11.***
2. ❒ No ➜ ***Skip to question 13.***

11. What is your organization's objective in maintaining property records for PP&E not capitalized on the balance sheet? *(Check all that apply.)*

1. ❒ Information needed for company operations
2. ❒ Need to track all items for safeguarding and other controls
3. ❒ Need information for tax reporting
4. ❒ Other – please specify: _____
_____

12. What was the cumulative value of PP&E recorded in property records, **but not capitalized on the balance sheet**, as of your company's most recent fiscal year-end?

$_____ ❒ Information not available

13. Please estimate the value of PP&E expensed as a result of not meeting or exceeding your organization's dollar threshold level during your company's most recent fiscal year?

$_____ ❒ Information not available

4

14. Do your auditors address your organization's capitalization policy, such as the adequacy of the dollar threshold level(s) as part of their audit of your annual financial statements? *(Check one.)*

    1. ❒ Yes
    2. ❒ No
    3. ❒ Not known

15. Does your organization use barcoding or any other asset control procedure(s) for PP&E? *(Check one.)*

    1. ❒ Yes, for all PP&E (i.e., capitalized and non-capitalized)
    2. ❒ Yes, but only for capitalized PP&E
    3. ❒ Yes, but only for non-capitalized PP&E
    4. ❒ Yes, but only for certain types of capitalized PP&E
    5. ❒ No → ***Skip to question 17.***

16. Please describe your asset control procedure(s).

    _____
    _____
    _____
    _____
    _____
    _____

17. Other than the asset control procedures you specified in questions 15 and 16, does your organization have a specific policy or procedure(s) for safeguarding sensitive and/or pilferable items (e.g., laptop computers, cell phones, etc.)? *(Check one.)*

    1. ❒ Yes → Please describe policy: _____
    _____
    _____

    2. ❒ No

18. Please describe how your organization accounts for computer hardware. (Please distinguish between purchases versus lease arrangements and issues related to personal computers versus mainframes.)

    _____
    _____
    _____
    _____
    _____
    _____

5

19. Does your organization have internally developed software? *(Check one.)*

    1. ❒ Yes ➜ ***Continue with question 20.***
    2. ❒ No ➜ ***Skip to question 22.***

20. Does your organization capitalize internally developed software in PP&E? *(Check one.)*

    1. ❒ Yes
    2. ❒ No

21. Does your organization have any processes in place to track internally developed software costs? *(Check one.)*

    1. ❒ Yes
    2. ❒ No

22. Does your organization currently own property in the possession of another organization? *(Check one.)*

    1. ❒ Yes ➜ ***Continue with question 23.***
    2. ❒ No ➜ ***Skip to question 25.***

23. Is the dollar threshold level for property in the possession of another organization different from that described in question one? *(Check one.)*

    1. ❒ Yes
    2. ❒ No

24. Does your organization have only one capitalization dollar threshold for property in the possession of other organizations or does it have multiple thresholds depending on the property type? *(Check one. Please enter dollar threshold amount(s) and property type(s), if applicable.)*

    1. ❒ One dollar threshold for property in the possession of other organizations
       (Please enter dollar threshold amount.)

       $ _____

    2. ❒ Different dollar thresholds for different types of property. *(Please enter dollar thresholds by type of property.)*

       $ _____ ➜ Property Type: _____
       $ _____ ➜ Property Type: _____
       $ _____ ➜ Property Type: _____
       $ _____ ➜ Property Type: _____

6

25. Which of the items listed below describe factors attributable to the differences between your organization's book and tax basis of property, plant, and equipment? *(Check all that apply.)*

1. ❒ IRS Section 179 deduction
2. ❒ Different dollar threshold levels used for book and tax reporting
3. ❒ Certain costs capitalized on book basis but expensed on tax basis
4. ❒ Certain costs capitalized on tax basis but expensed on book basis
5. ❒ Other - Please describe: _____
6. ❒ Not applicable, book and tax basis of PP&E are the same

II. Depreciation/Useful Lives

Please note: For questions 26 through 37, please base your responses on depreciation for financial reporting (i.e., book basis) and **not** depreciation for income tax reporting.

26. For depreciation purposes, how many years (useful life) does your organization use to depreciate its real property classifications? *(Check all that apply and enter the useful life in years. If more space is needed, please use the space in question 38 to respond. For your convenience, feel free to attach your own schedule of real and personal property classifications and their useful lives in lieu of responding to this question)*

1. ❒ Real Property (Please specify type, e.g., office buildings, plants, warehouses, sheds, etc.)

Real Property Type		Useful life
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years

2. ❒ Personal Property (Please specify type, e.g., furniture, machines, office equipment, motor vehicles, software, computer equipment, etc.)

Personal Property Type		Useful life
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years
_____	→	_____ years

7

27. Which of the following, if any, is used by your organization for assigning useful lives to PP&E? *(Check all that apply.)*

    1. ❒ Organization historical experience
    2. ❒ Industry practices
    3. ❒ IRS table
    4. ❒ Internal study/tables
    5. ❒ Other - please specify:_____

28. Which of the following best describes the book depreciation method used by your organization? *(Check one.)*

    1. ❒ Straight Line Method
    2. ❒ Decreasing Charge Method (such as sum-of-years digits, or double declining balance)
    3. ❒ Activity Method
    4. ❒ Accelerated Method
    5. ❒ Different methods for different types of PP&E ➜ Please describe or attach sheet detailing methods:

       _____
       _____
       _____

    6. ❒ Other - please specify: _____

29. Within the past 5 years, have there been any formal analyses performed (in-house or external) to develop or validate your organization's useful life policies? *(Check one.)*

    1. ❒ Yes ➜ ***Continue with question 30.***
    2. ❒ No ➜ ***Skip to question 34.***

30. Who performed these analyses and when were they completed? *(Check all that apply and enter date(s) of completion - mm/yyyy.)*

    1. ❒ Internal ➜ Date of completion: ____/_____
    2. ❒ Consultant ➜ Date of completion: ____/_____
    3. ❒ Independent Public Accountant ➜ Date of completion: ____/_____
    4. ❒ Other – please specify:_____ ➜ Date of completion: ____/_____

31. Which of the following, if any, <u>best describes</u> the conclusion of the <u>most recent</u> analysis? *(Check one.)*

    1. ❒ Useful life policy appeared reasonable
    2. ❒ Useful life policy did not appear reasonable, new useful life policy proposed ➜ Please explain:

       _____

    3. ❒ Useful life policy did not appear reasonable, but no new policy proposed
    4. ❒ Inconclusive results
    5. ❒ Other, please specify: _____

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32. If a different useful life policy was proposed as a result of the most recent analysis, was it implemented at your organization? *(Check one.)*

    1. ❒ Yes ➜ Please describe the new policy: _____
    _____
    2. ❒ No ➜ Explain why: _____
    _____
    3. ❒ Not applicable, new useful life category was not proposed.

33. Please describe, in as much detail as possible, the methodology that was applied in performing the most recent analysis?

    _____
    _____
    _____
    _____
    _____

34. Do your auditors address the adequacy of your organization's useful life categories as part of their audit of your organization's annual financial statements? *(Check one.)*

    1. ❒ Yes
    2. ❒ No
    3. ❒ Not known

35. Approximately what percentage of your organization's PP&E that is still in use is fully depreciated? *(Check one.)*

    1. ❒ None
    2. ❒ 1-5%
    3. ❒ 6-10%
    4. ❒ 11-15%
    5. ❒ 16-20%
    6. ❒ Greater than 20%
    7. ❒ Not known

36. Which of the following best describes how your organization treats fully depreciated PP&E assets? *(Check one.)*

    1. ❒ Fully depreciated PP&E are removed from property records immediately
    2. ❒ Fully depreciated PP&E are maintained on property records if asset is still in use
    3. ❒ Fully depreciated PP&E are removed from property records but tracked by another means
    4. ❒ Other - please explain: _____

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37. Which of the following best describes your organization's depreciation policies for financial reporting (book) purposes as compared to those for tax reporting? *(Check one.)*

    1. ❒ Accelerated methods of depreciation used for tax depreciation causing depreciation expense to typically exceed depreciation expense for financial reporting
    2. ❒ Depreciation expense recorded for financial reporting and tax purposes are the same
    3. ❒ Organization useful life categories are such that depreciation expense for financial reporting typically exceeds depreciation expense for tax reporting
    4. ❒ Other - Please describe: _____

III. Other Comments

38. If you have any comments concerning PP&E policies or you would like to elaborate on any of your answers, please use the space below. Be sure to indicate the question number beside your comment. If you wish, you may attach additional pages to this survey.

_____
_____
_____
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_____
_____
_____

Thank you for your assistance!

10

Comments from the Department of Agriculture

United States
Department of
Agriculture

Office of the Chief
Financial Officer

1400 Independence
Avenue, SW

Washington, DC
20250

JUL 10 2002

Ms. Mary Arnold Mohiyuddin
Assistant Director
Financial Management and Assurance
United States General Accounting Office
Washington, D.C. 20548

Dear Ms. Mohiyuddin:

Thank you for the opportunity to comment on your draft report entitled "Financial Management: Survey of Capitalization Threshold and Other Policies for Property, Plant, and Equipment (GAO-02-607)".

Our review focused on the areas where the Department of Agriculture (USDA) and its survey responses specifically are mentioned. In addition, we offer some observations for your consideration on the contents of the report and the methodology used to conduct the survey.

Please consider the following corrections and/or comments regarding USDA survey responses:

Now on p. 11.

1. Page 17, "USDA did not report a capitalization threshold level prior to October 1997."

   The effective date of USDA's capitalization threshold for personal and real property should have been February 1994, in accordance with Departmental Regulation 2200-2, Capitalization and Depreciation of Real and Personal Property instead of October 1997, as indicated in the survey response.

Now on p. 30.

2. Page 38, "Capitalization threshold prior to current level not reported by agency, therefore, no increase calculated."

   At the time of the survey, USDA's capitalization threshold had not changed in the past five years. USDA established new thresholds for real and personal property in June 2002.

Now on p. 38.

3. Page 41, "Federal agency did not report a capitalization threshold for this property category."

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A capitalization threshold for building improvements was not separately disclosed, but the capitalization threshold for buildings also applies to building improvements.

In addition to the editorial points above, we would like to offer some comments about the contents and the research methodology used in the report for your consideration.

Now on p. 4.

On page 8 the report states that government agencies would be using lower capitalization thresholds if they were doing a better job of measuring performance based on cost. However, we believe it would also be useful to note that there are inherent differences in the ways government and private sector entities approach cost and income.

The private sector's drive for shareholder value through higher net income is difficult to compare with the government's drive to control costs and better manage assets. In their push to increase short-term net income, private sector companies are likely to capitalize as many assets as possible and spread out the costs over the longest justifiable useful life. Government agencies do not have the same incentives when it comes to managing their costs and may be less likely to use lower capitalization thresholds.

Now on p. 4.

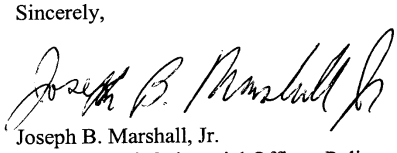
On pages 5 and 6 the report mentions that most of the federal agencies that had increased their capitalization thresholds have still retained lower accountability thresholds in order to properly account for and safeguard their assets. We believe this factor should be emphasized in more detail in the report analysis. In the private sector, if you do not capitalize an asset, you do not usually track it; therefore there is an incentive to capitalize at a lower level in order to safeguard your assets. Government agencies have typically used other tools to properly account for and track assets, and therefore shouldn't need to capitalize property at a lower threshold to safeguard assets.

Finally, we recommend that your office discuss the methodology used to prepare the survey and the limited amount of follow-up in this report. While it is helpful to provide examples of the best practices used by private companies in the financial management arena, these comparisons to government-wide practices must also recognize and compare the inherent differences. Additional face-to-face discussions with private sector companies and federal agencies may be needed to determine the best course of action for federal agencies.

Ms. Mary Arnold Mohiyuddin 3

If you have any questions or wish to discuss these comments, please call me at (202) 720-8345 or have a member of your staff call Kathy Donaldson at (202) 720-1893.

Sincerely,



Joseph B. Marshall, Jr.
Associate Chief Financial Officer, Policy and Planning

Comments from the Department of the Interior

United States Department of the Interior

OFFICE OF THE SECRETARY
Washington, D.C. 20240

JUN 2 4 2002

Ms. Mary Arnold Mohiyuddin
Assistant Director
U.S. General Accounting Office
441 G Street, N.W.
Washington, DC 20548
mohiyuddinm@gao.gov

Dear Ms. Mohiyuddin:

Thank you for the opportunity to comment on your proposed report, "Financial Management: Survey of Capitalization Threshold and Other Policies for Property, Plant and Equipment" (GAO-02-607).

The information included in the draft report as it relates to the Bureau of Reclamation is correct with one exception. In Appendix VII on page 42, Useful Lives for Personal Property, for Furniture & Fixtures,"N/R" should be changed to "10 - 20".

Now on p. 13.

In addition, on page 19, the draft report states that: "The lack of consistency in capitalization threshold levels among federal agencies could potentially lead to reporting problems in the U.S. government's consolidated financial statements and performance measurement comparisons". It should be noted, however, that certain Federal agencies, including the Bureau of Reclamation, have unique characteristics which necessitate the use of specific capitalization thresholds, including the use of a zero threshold by Reclamation.

The Bureau of Reclamation's policies regarding capitalization threshold levels and useful lives are based on the potential recoverability of the costs of major water projects. The majority of Reclamation's property, plant, and equipment capital costs pertain to its multipurpose water projects. A portion of the costs of these water projects are reimbursable from project beneficiaries. For example, capital costs allocated to irrigation, municipal and industrial water, and power generation are generally reimbursable from the respective beneficiaries. Conversely, some costs, such as those allocated to flood control, fish and wildlife, and recreation are generally non-reimbursable. Reimbursements generally occur over the useful life of the project which may exceed 40 years.

To ensure that all reimbursable costs are recovered, Reclamation specifically defines costs that should be capitalized versus those costs that should be expensed. All water infrastructure costs, including additions and replacements, are capitalized. Since Reclamation's water projects have a long useful life, this zero threshold ensures that project beneficiaries will repay these costs over the repayment period, as provided for by legislation. This treatment also provides a more accurate measure of net cost by depreciating these facilities over their useful lives. The use of any

other capitalization threshold by Reclamation would adversely impact Reclamation's recovery of reimbursable capital investment costs from the public.

The Federal Accounting Standards Advisory Board concluded in Statement of Federal Financial Accounting Standards #6 that Federal entities should have the discretion to set appropriate capitalization thresholds. We believe that this conclusion remains valid. Additional guidance may be needed regarding the determination of appropriate capitalization thresholds to reduce the significant variance in established thresholds and ensure accurate cost reporting of government operations. This could narrow the range of capitalization thresholds used in capitalizing Federal assets. However, we do not believe that the capitalization thresholds across the government must be identical to produce consistent and accurate financial and management reporting. As long the capitalization thresholds are developed using consistent standards, are appropriate to the individual agencies and do not distort full cost reporting, these variations will not misstate the consolidated financial statements. The range of capitalization thresholds would be disclosed in the notes to the consolidated government-wide financial statements in the same manner that useful lives are commonly reported as a range.

Thank you for the opportunity to comment on this draft. Please contact R. Schuyler Lesher at (202) 208-4701 if you need any further information.

Sincerely,

P. Lynn Scarlett
Assistant Secretary, Policy Management and Budget

Comments from the National Aeronautics and Space Administration

National Aeronautics and
Space Administration
Office of the Administrator
Washington, DC 20546-0001

June 24, 2002

Mary Arnold Mohiyuddin, Assistant Director
Financial Management and Assurance
United States General Accounting Office
Washington, DC 20548

Dear Ms. Mohiyuddin:

Thank you for the opportunity to review and comment upon the draft report on your "Survey of Capitalization Threshold and Other Policies for Property, Plant and Equipment." As you requested, we focused our review upon the areas where NASA and its survey responses were discussed. We have no comments on those parts of the draft report, but we do have a more general comment for your consideration.

Now on p. 5.

Now on p. 18.

On page 7 of the report, it is stated that "…the widely varying threshold levels among the federal agencies, the sharp increases in recent years, and the drastic differences from private sector companies of considerable size in terms of reported PP&E and total assets raise some questions." Further discussion of this matter appears on page 25 of the draft. In drawing comparisons with private sector companies' practices, however, the report does not recognize that the private sector's objectives in capitalizing and depreciating property differ dramatically from the Government's. The profit motive driving the private sector clearly leads to different policies and practices than those established by the Federal Accounting Standards Advisory Board for the Government. In addition, Internal Revenue Service regulations regarding depreciation are a significant contributing factor to private companies' policies. Without recognition of these differing objectives and restrictions, the comparison drawn in the report could be misleading to some readers.

We believe the report provides useful and interesting information.

Cordially,

Michael D. Christensen
Associate Deputy Administrator
for Institutions

Comments from the Department of State

United States Department of State

Washington, D.C. 20520

JUN 14 2002

Dear Ms. Westin:

We appreciate the opportunity to review your draft report, "FINANCIAL MANAGEMENT: Survey of Capitalization Threshold and Other Policies for Property, Plant and Equipment," GAO-02-607, GAO Job Code 192021.

The enclosed Department of State comments are provided for incorporation with this letter as an appendix to the final report.

If you have any questions concerning this response, please contact Jim Fishenden, Director, Office of Financial Policy and Management Control, Bureau of Resource Management, at (202) 261-8643.

Sincerely,

Christopher B. Burnham
Assistant Secretary and
Chief Financial Officer

Enclosure:

As stated.

cc: GAO/FMA - Gregory Kutz
State/OIG - Mr. Berman
State/RM - Mr. Chris Flaggs

Ms. Susan S. Westin,
Managing Director,
International Affairs and Trade,
U.S. General Accounting Office.

Department of State Comments on GAO Draft Report

FINANCIAL MANAGEMENT: Survey of Capitalization Threshold and Other Policies for Property, Plant and Equipment, (GAO-02-607, GAO Code 192021)

The Department of State welcomes the opportunity to comment on GAO's survey of Capitalization Threshold and Other Policies for Property, Plant and Equipment. The report is well done, but overlooks two important factors, which require attention or the report may risk misleading the reader:

1. The distinct differences between private sector and public sector capitalization in threshold capitalization thresholds; and

2. The factors that cause Cabinet Departments to change threshold levels in the first place.

The comparison of capitalization thresholds between private industry and the Federal government may be useful in some ways, but we believe there are some distinct differences that should be indicated in the report. The profit motive, along with income tax consequences of transactions, sometimes dictate accounting treatment in private industry. An across-the-board comparison of private industry to Federal government capitalization thresholds may not be useful in that some companies may lease large amounts of PP&E and not apply the lower thresholds being reported.

The comparison of thresholds for personal property and real property throughout the document is misleading to the reader. Overall comments are made regarding changes in capitalization thresholds without respect to personal versus real property. As a result, Figure 1: Increase in Capitalization Threshold Levels at Federal Agencies is confusing and difficult to interpret. This chart leads the reader to a conclusion that a major percentage of the capitalization thresholds have been substantially increased in the past five years. In fact less than 25% of the total thresholds (personal and real property) have increased substantially. We recommend either comparing like categories (personal and real) or include all thresholds in the illustrative charts to alleviate any confusion.

Now on p. 10.

We suggest that the events that occurred in the past five years that required the analysis and review of capitalization thresholds be explained in the discussion on page 15. Namely, the primary motivating impetus for analysis of capitalization thresholds and PP&E in general, was the requirement to prepare audited financial statements. In addition, the implementation of the Statement of Federal Financial Accounting Standards No. 6 Accounting for Property, Plant, and Equipment on September 30, 1997 was also a factor in the review and analysis of capitalization thresholds. These two major events prompted departments or agencies to review carefully their capitalization thresholds determining the levels for real vs. personal property that present fairly the financial position without overburdening those actually completing the accounting

2

transactions. Readers of the report may reach an erroneous conclusion that departments simply changed capitalization thresholds without appropriate empirical analysis if the report is not modified.

3

Technical Comments:
Footnote 8 referred to on page 5 is not found on that page. The actual footnotes are numbered 7, 7, 9 so 8 is missing. The second footnote 7 which is located on page 6 is, we believe, footnote 8 that should be reflected on page 5.

Page 41 Appendix VI: Capitalization Thresholds for Real Property illustrates that the Department of State did not report thresholds for Building Improvements, Other Structures & Facilities and Leasehold Improvements. Some numbers were reported in the initial survey and subsequently additional numbers were reported during phone conversations requesting additional information. In reality, the $250,000 threshold is applicable for Building Improvements and Leasehold Improvements as well as Capital Improvements. Once this information in included in Appendix VI, footnote "b" should be deleted.

Comments from the Department of the Treasury

DEPARTMENT OF THE TREASURY
WASHINGTON

ASSISTANT SECRETARY

June 19, 2002

Ms. Mary Arnold Mohiyuddin
Assistant Director
Financial Management and Assurance Team
General Accounting Office
441 G Street, NW
Mail Stop 5T45
Washington, DC 20548

Dear Ms. Mohiyuddin:

I appreciate the opportunity to offer comments on your draft report entitled Financial Management: Survey of Capitalization Threshold and Other Policies for Property, Plant, and Equipment (GAO-02-607). Our detailed comments are included as an enclosure.

Sincerely yours,

Donald V. Hammond
Fiscal Assistant Secretary

Enclosure

Comments on
Financial Management: Survey of Capitalization Threshold and Other Policies for Property, Plant, and Equipment
(GAO-02-607)

Now on p. 10.

Page 15: "Inappropriate or excessive capitalization thresholds have a significant impact on financial reporting and related oversight issues and may not comply with SFFAS No. 6 requirements".

Now on p. 22.

Page 32: "In addition, agency management and auditors also have individual responsibilities to ensure that established capitalization thresholds levels are not resulting in significant departure from GAAP."

Consideration of whether established capitalization thresholds are a significant departure from GAAP is already a required part of the financial statement audits at the federal agencies cited. None of these agencies were found to have a major audit finding for capitalization thresholds. Ten of the Federal agencies cited were audited by CPA firms that have many years' experience auditing large entities. These same CPA firms also audit the private sector entities that were cited by GAO. As these CPA firms have been recognized experts in financial reporting and auditing for many years, we are confident in their findings, and those of the IG auditors, that the Federal agencies cited are not in significant departure from GAAP with regards to capitalization thresholds.

The private sector may have lower capitalization thresholds as a result of risk associated with corporate income tax. This is an additional risk that is obviously not a factor in Federal agencies as they are not subject to income tax. Private sector companies would have an incentive to raise their capitalization thresholds, which would lead to increased expenses, lower net income, and thus, lower income taxes. Therefore, private sector companies have to be wary of not being prone to this potential tax audit finding. Accordingly, auditors of private sector companies also pay additional attention to this area to compensate for this additional risk. This is not a risk that is present in Federal agencies as they are not subject to potential income tax audits.

Now on pp. 18-19.

Page 7 and page 27: "Further, six of the agencies surveyed reported that they expensed a total of almost $ 2 billion in PP&E for the fiscal year ended September 30, 2000, and therefore did not report this amount on the U.S. government's consolidated balance sheet as assets. While the $2 billion may not approach overall audit materiality for the consolidated financial statements, this amount is incomplete, as the remaining eight agencies survey could not readily provide the amount expensed for the same period as a result of the PP&E acquisition costs not meeting the capitalization threshold."

The paragraph leads the reader to believe that there may be a governmentwide materiality problem with regards to PP&E. However, PP&E materiality problems were not cited as financial statement audit findings at any of the surveyed agencies.

Now on p. 12.

Page 19 "The lack of consistency in capitalization threshold levels among Federal agencies could potentially lead to reporting problems in the U.S. government's consolidated financial statements and performance measurement comparisons."

This statement appears to be contrary to the FASAB standard, which allows variances in the threshold levels between agencies.

> SFFAS No. 6, ¶13 CAPITALIZATION THRESHOLDS The Board believes that capitalization thresholds should be established by Federal entities rather than centrally by the Board. Because Federal entities are diverse in size and in uses of PP&E, entities must consider their own financial and operational conditions in establishing an appropriate capitalization threshold or thresholds. Once established, this threshold(s) should be consistently followed and disclosed in the financial reports.

Now on pp. 17-18.

Page 26 – bottom paragraph.

This paragraph leads the reader to think that an inappropriate capitalization threshold caused the $1 billion material understatement of PP&E at IRS. However, according to the testimony by Gregory Kutz before the Subcommittee on Government Management, Information and Technology on February 29, 2000, the inappropriate capitalization was only one of several components contributing to the $1 billion adjustment. The IRS had numerous problems with its PP&E records, which resulted in there being no reliance on the records and IRS hiring a consulting firm to develop a balance based primarily on a statistical estimate, resulting in the $1 billion adjustment.

Editorial Comments
Page 1 – 2nd sentence - add comma after "financial information."

Page 2 – 2nd paragraph, first sentence – "property, plant, and equipment (PP&E)" should be changed to just "PP&E" since the acronym had already been defined on page 1.

Page 5 – In the text, there is a footnote #8 being referenced, but it does not show up on the page. However, there is a second #7 footnote that shows up on the bottom of page 6.

Page 9 – last sentence before Background section. Need to add an "s" to "threshold."

Page 11 – The footnote printing on the bottom of the page is on the incorrect page. It should be showing up on page 10.

Page 12 – The footnote printing on the bottom of the page is on the incorrect page. It should be showing up on page 11.

GAO Contact and Staff Acknowledgments

GAO Contact

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Acknowledgments

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