



FIXED ASSET ACCOUNTING AND MANAGEMENT PROCEDURES MANUAL

SECTION 6

Depreciation

1 Purpose

The purpose of this section is to establish procedures for calculating and recording depreciation of fixed assets.

2 Scope

Depreciation will be calculated and recorded for the City's depreciable fixed assets (excluding land) in accordance with the applicable financial reporting model.

Financial accounting and reporting for depreciation of fixed assets must be in accordance with the *Codification of Governmental Accounting and Financial Reporting Standards* (the *Codification*) and any future revisions and applicable pronouncements by the Governmental Accounting Standards Board (GASB) or other governing boards, as well as applicable pronouncements of the Financial Accounting Standards Board (FASB).

3 Guidelines

3.1 Depreciation Charges

Depreciation costs associated with the depreciable assets of proprietary funds, regardless of funding source, will be budgeted, calculated, and charged annually to the operations of the fund. Depreciation begins in the month the fixed asset is placed into service.

3.2 Method

All depreciable fixed assets will be depreciated using the straight-line method. Land is not depreciated. Depreciation will be calculated based upon the estimated useful lives outlined in Section 4 (Fixed Asset Classification and Useful Lives).

3.3 Salvage Values

In general, the salvage value of City fixed assets will be \$0. The City's Fixed Asset Management Program administrator will conduct a review of the amounts and calculation methods used for any exceptions to these guidelines.

Available guidelines and judgment will be used by the departments to estimate a salvage value for assets that may be operational or useable beyond their designated useful lives.



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3.4 Changes in Asset Life or Value

If the estimated useful life or value of an asset is changed at some point during its service (e.g., through improvement or betterment), no adjustment of prior depreciation will be made.

If a change is made to useful life, the remaining book value will be depreciated over the remainder of the adjusted useful life.

If a change is made to the book value of an asset (change in salvage value), the adjusted book value will be depreciated over the remaining useful life.

3.5 Depreciation of Grant Funded Assets

In accordance with the *Codification*, Section G60, assets acquired wholly or in part through grant funding will be recorded as fixed assets with a corresponding credit to a contributed capital account equaling the amount of the grant funding.

Depreciation and accumulated depreciation will be calculated and recorded in the normal manner. However, the annual depreciation expense for grant funded assets will be closed directly to the contributed capital account, rather than the retained earnings account, as is the case with non-grant assets.

4 Assigning Useful Life and Salvage Value

4.1 Useful Life – General

An estimated useful life will be assigned to each asset at the time the asset is entered into the FAMS, based on the listing of assets by class and associated useful lives, as outlined in Section 4 (Fixed Asset Classification and Useful Lives) and as maintained in the Class Table of the FAMS. The FAMS Class Table will be maintained in accordance with the following guidelines:

- Useful lives will be standardized for each asset class as defined in the FAMS Class Table.
- The DFAC will be responsible for assigning assets to the appropriate asset class, which in turn will determine the standard useful life of the asset for depreciation purposes.
- The FAMS will include a table of standard asset classes, useful lives, and salvage values for department use.
- F&A Information Services (IS), as directed by the Director of Finance & Administration and the City FAMS Program Administrator, will be responsible for maintaining the FAMS table of standard asset classifications and associated useful lives.



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Standard useful lives for vehicles and rolling stock will be established in coordination with and with input from Fleet Management.

4.2 Useful Life – Used Assets

If a “used” asset is acquired, the DFAC will determine whether the useful life associated with the class assigned to the asset is appropriate. If the estimated remaining life of the used asset is different from the standard life in the Class Table, an adjustment reflecting a change in estimate will be entered into the FAMS for the asset. See the depreciation adjustment procedure in subsection 7 in this section for the specific steps involved in making the estimate adjustment.

4.3 Salvage Value

Salvage value for assets will be assigned to each asset at the time the asset is entered into the FAMS based on the listing of assets by class and associated useful lives, as outlined in Section 4 (Fixed Asset Classification and Useful Lives) and as maintained in the Class Table of the FAMS. Salvage values are determined as follows:

- Unless otherwise determined for a specific asset class, the salvage value for all City of Houston fixed assets and controlled items will be \$0.
- Salvage value will be standardized for each asset class as defined in the FAMS Class Table. Salvage value normally is not assigned at the individual asset level; rather it is pulled from the FAMS based on the class code assigned to the asset.
- The DFAC will be responsible for properly assigning assets to the appropriate asset class, which in turn will determine the standard salvage value of the asset for depreciation purposes.
- The FAMS will include a table of standard asset classes, useful lives, and salvage values for department use.
- F&A IS, as directed by the Director of Finance & Administration and the City FAMS Program Administrator, will be responsible for maintaining the FAMS table of standard asset classifications and associated useful lives. Salvage values for vehicles and rolling stock, if applicable, will be established in coordination with and with input from Fleet Management.
- If the DFAC determines the standard salvage value needs to be changed, an adjustment reflecting a change in estimate will be entered in the FAMS for the asset. See the depreciation adjustment procedure in subsection 7 in this section for the specific steps involved in making the change in estimate adjustment.



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4.4 Secondary Useful Life

Where it is appropriate and allowable (e.g., Enterprise Funds for rate-setting purposes), the FAMS will provide the capability, and departments may assign a secondary useful life to be used for rate-setting purposes only.

Note: Financial reporting information provided to Asset Management will always be based on the standard useful life and not the secondary useful life.

5 Methodology and Calculation

5.1 Depreciation Method

Depreciation will be calculated using the straight-line method only. The basis used in straight-line depreciation is calculated by subtracting the salvage value, if any, from the acquisition cost. The result is the adjusted basis. Depreciation is then calculated by dividing the adjusted basis by the useful life. The total amount depreciated can never exceed the adjusted basis. At the end of the asset's estimated life, any salvage value will remain until the asset has been disposed of.

Example of straight-line depreciation

Asset Cost	\$21,000
Estimated Useful Life	5 years (60 months)
Monthly Depreciation	$\$21,000 \div 60 = \350
Annual Depreciation	$\$350 \times 12 = \$4,200$

5.2 Acquired Assets

Depreciation for acquired assets will be computed using the following *mid-month rule*: If an asset is acquired on or before the 15th of the month, depreciation will be charged for the full month. If the asset is acquired after the 15th of the month, no depreciation is charged for that month.

The same mid-month rule applies to disposals: If an asset is disposed of on or before the 15th of the month, the FAMS will not charge depreciation for the last month. If the asset is disposed of after the 15th of the month, depreciation is charged against the last month.



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5.3 Calculation Frequency and Scope

Depreciation will be calculated at least annually, prior to closing the fiscal year processing for the FAMS.

For management reporting purposes, depreciation will be calculated on all assets in the FAMS, regardless of fund (including general fund) or whether they are capital or controlled items.

5.4 Group Assets

The DFAC will depreciate assets normally as individual units under the single-unit method of depreciation. The group method of depreciation will only be used for group assets or where single-unit depreciation is not feasible (with the prior agreement of the City's FAMS Program Administrator).

5.5 Idle and Reserved Assets

In the case of assets that are temporarily idle or being held in reserve pending future use, the DFAC will continue to depreciate the asset without adjustment to the remaining useful life or periodic depreciation charges.

5.6 Related Accounting Transactions

The FAMS will identify and assign depreciation charges for an asset to the appropriate balance sheet accumulated depreciation account and fund. The accumulated depreciation accounts to be used for each asset category are those defined in the chart of accounts.

Where multiple funding sources are involved for an asset, calculated depreciation will be allocated by funding source, according to the percentage of cost funded by each source. Accumulated and year-to-date depreciation by funding source will be reported for each fixed asset.

6 Period Processing

The DFAC will initiate depreciation processing in the FAMS and will ensure that depreciation is processed, at a minimum, for the last period of the fiscal year, prior to the fiscal-year-end close. After the depreciation process is run, the DFAC will review the Depreciation Register and other available reports for *reasonableness* of the processing and posting.



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7 Depreciation Adjustment Procedure

1. When an adjustment is made to an asset value that affects calculated depreciation, the DFAC will determine the nature of the change for financial reporting purposes, with assistance from accounting staff as appropriate.

If the adjustment involves a change to cost, salvage value, or useful life (i.e., class code), and the change is the result of an error in the original information or data entry, the depreciation adjustment will be classified as an accounting error for financial reporting purposes.

If the adjustment involves a change to either salvage value or useful life of the asset, and the change is the result of new events, changing conditions, more maintenance service life experience, or additional information, the depreciation adjustment will be classified as a change in accounting estimate for financial reporting purposes.

2. The depreciation adjustment for an accounting error will be calculated as follows:
 - Depreciation will be recalculated based upon the new information from the asset's acquisition date through the last date depreciated.
 - The adjustment will be taken in full (cumulative effect) in the period the adjustment is made, using the last date depreciated for the asset as the accounting transaction date for the adjustment.

3. The depreciation adjustment for a change in accounting estimate will be calculated as follows:

- The depreciation adjustment is not accounted for by restatement of prior years' financial statements. The effect of the change will be accounted for in the period of change, if the change affects only that period, or in the period of change and future periods, if the change affects both.
- The FAMS will provide the following support to calculate a change in estimate:

If the change does not result in full depreciation of the asset's cost basis as of the last date the asset was depreciated, the remaining balance will be depreciated over the remaining useful life after the change.

If the change does result in full depreciation of the asset's cost basis as of the last date the asset was depreciated, the remaining balance will be charged to depreciation using the last date the asset was depreciated as the date of the additional (close-out) depreciation charge.

4. Upon determination of the type of adjustment to be made, the DFAC will complete a FAMS Capitalization Form—Financial Adjustments/Other Changes (FA-3) indicating the



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information to be adjusted (acquisition cost, salvage value, useful life) and the type of adjustment to be made (accounting error or change in accounting estimate).

5. The FA-3 will be signed by the DFAC and forwarded to the data entry clerk for entry into the FAMS.
6. The item will be entered into the FAMS as a financial adjustment.



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