



Financial Management Program

Budgeting for Short-Term Capital Assets

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PROMOTING EXCELLENCE IN GOVERNMENT

Learning Objectives

At the end of this session, you will be able to -

- Define short-term capital assets
- Recall the importance of internal control as it relates to the budget process
- Explain how strategic planning impacts the budget
- Discuss characteristics of a budget policy
- Discuss different funding options for financing short-term assets



CAPITAL ASSETS DEFINED

Capital Assets Defined

Capital assets include tangible or intangible assets that are used in operations and that have initial useful **lives** extending beyond a **single reporting period**

Short-Term Capital Assets Defined

There is no standard definition of **short-term** capital assets.

- Useful life < Infrastructure type capital assets
- Replace more often than capital assets such as infrastructure
- Typically use pay-as-you-go or lease purchase to acquire these assets
- Vehicles, IT infrastructure, software, heavy equipment, etc.

CIP = Capital Improvement Program



- A long term plan for capital expenditures
- Dollar amounts of projects included in plan may vary by government
- Time period covered by plan may vary by government
- Overall, CIP is plan important to the future of the government

What is included in CIP?

- Capital assets which require improvement or replacement
- Capital projects which are new infrastructure
- Examples include land, buildings, equipment or vehicles



Components of a CIP Policy



- *Definition of the time horizon* (for example, a five year plan)
- *Definition of major expenditure* (for example, minimum cost of \$25,000)
- *Definition of useful life* (for example, a useful life of ten years or longer)
- Direction regarding spending priorities
- Details of evaluation process



CIP Policy

Capital Improvement Program Policies

- The City will adopt the first year of a multi-year plan for capital improvements, update it annually and make every attempt to complete all capital improvements in accordance with the plan.
- A Capital Improvement Project is defined as infrastructure, equipment or construction which results in a capitalized asset costing more than \$10,000.00 and having a useful life of two or more years.
- The City will coordinate the development of the Capital Improvement Program with the development of the operating budget to ensure future operating expenditures and revenues associated with new capital improvement will be projected and incorporated into the current and future operating budgets.
- The City will adopt the first year of a multi-year Asset Management Program for maintenance of capital improvements (for the purpose of taking care of what currently exists rather than replace it new), and update it annually and make every attempt to complete the maintenance when it is scheduled.
- The City will determine the least costly financing method available for all new capital improvement projects.
- All projects in the Comprehensive Improvement Element (CIE) of the Comprehensive Plan will be included in the Capital Improvement Program.

What is more important?

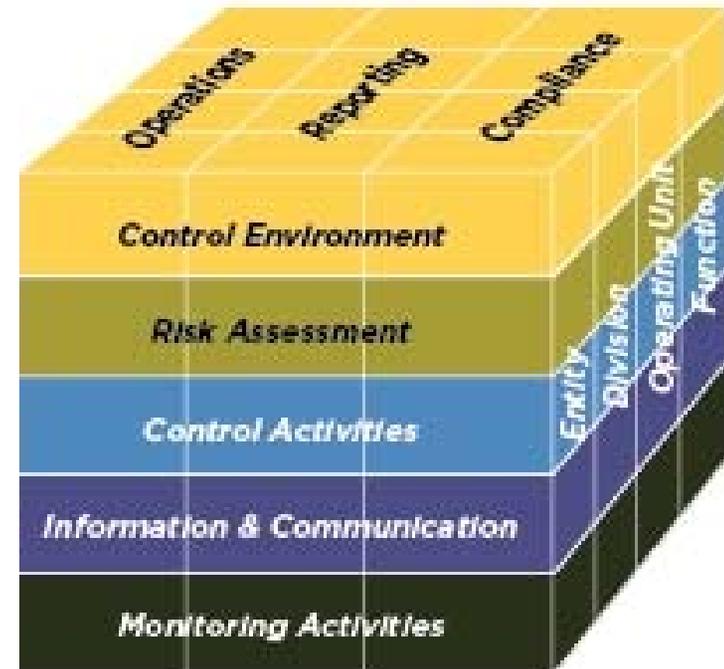




INTERNAL CONTROL & THE BUDGET

Five Components

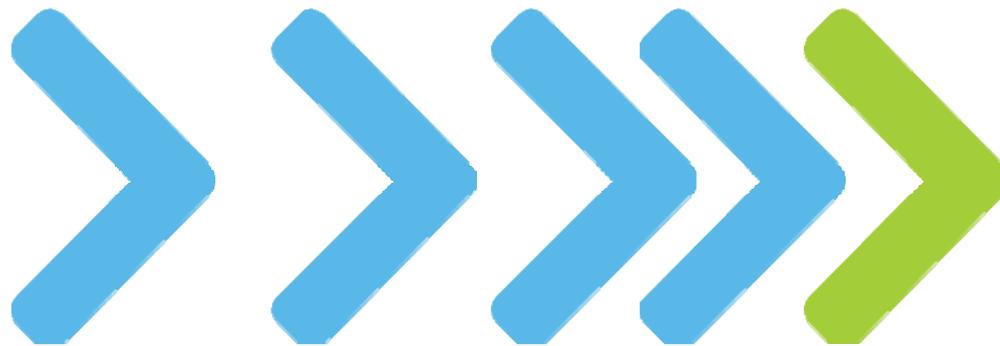
- Control Environment
- Risk Assessment
- Control Activities
- Information and Communication
- Monitoring Activities





Class Discussion

How can we relate each component of internal control to budgeting for short-term capital assets?



STRATEGIC PLAN'S ROLE IN BUDGET PROCESS

Strategic Planning is

- A systematic process that helps you identify:
 - why your organization exists,
 - whom it serves,
 - what benefits it provides, and
 - the vision of how citizens can best be served

Strategic Planning

Why do it?

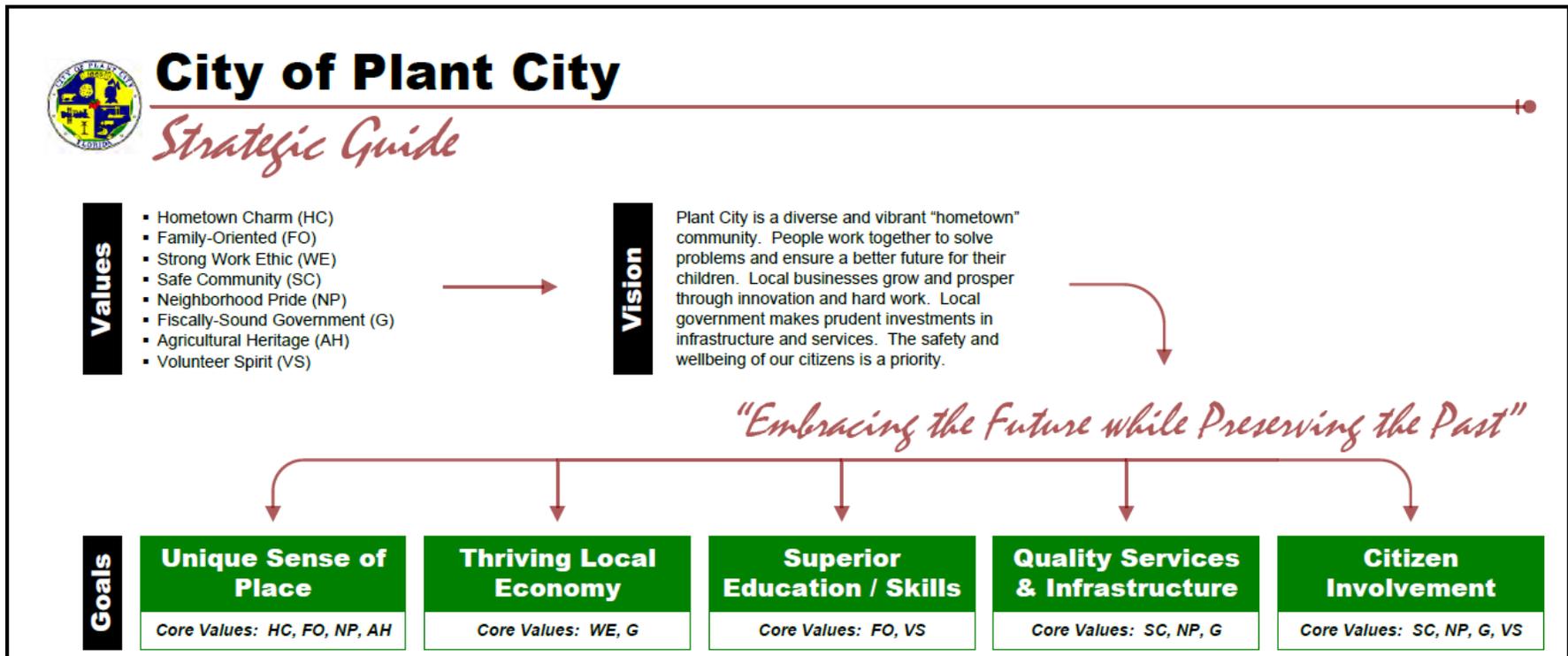
- Reflects mission
- Communicates goals and objectives
- Develops ownership

Strategic Planning

Why do it?

- Focuses resources
- Measures progress
- Ensures that everyone is working towards the same mission and vision
- Focuses organization

City of Plant City Vision Statement



Question

How does your government's vision and mission translate to the budget?

Strategic Plan

- Long term plan
- Provides a focus for development of CIP
- Strategic plan defines core values
- Clear picture of the priorities of the government
- Plan of action for achieving desired results

1

2

3

4

5

What is a Budget Policy?

Set of guidelines or statements which set the parameters, or boundaries within which the budget process takes place

Budget Policy Addresses

- Balanced budget
- Level of control
 - Authority levels for budget changes
- Amendments to budget
- Contingency options
- Capital expenditures vs operating expenditures

Budget Process

- Elements of a successful process
 - Goals and objectives (sense of direction)
 - Performance measures
 - Administrative plan
 - Budget calendar

Administrative Plan

- Administrative Plan
 - Describes the various steps involved
 - Describes the persons responsible
 - It is a *policy statement*

Budget Calendar

- WHO
 - is responsible for the task
- WHAT
 - is to be accomplished within the task
- WHEN
 - is the task to be completed

Budget Policy

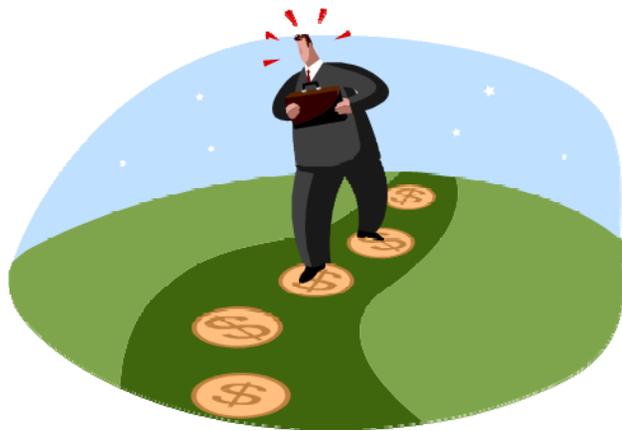
Budget policy provides plan of action
for strategic plan

*SHOULD NOT CONTRADICT GOALS OF
STRATEGIC PLAN*

Financial Policies

At a minimum, policies should be adopted for the following areas





CAPITAL BUDGETING

Two Components of Financial Planning

- Operating budget
 - Ongoing costs for staffing, materials, supplies
- Capital budget
 - Equipment and vehicle replacement and additions
 - New facilities

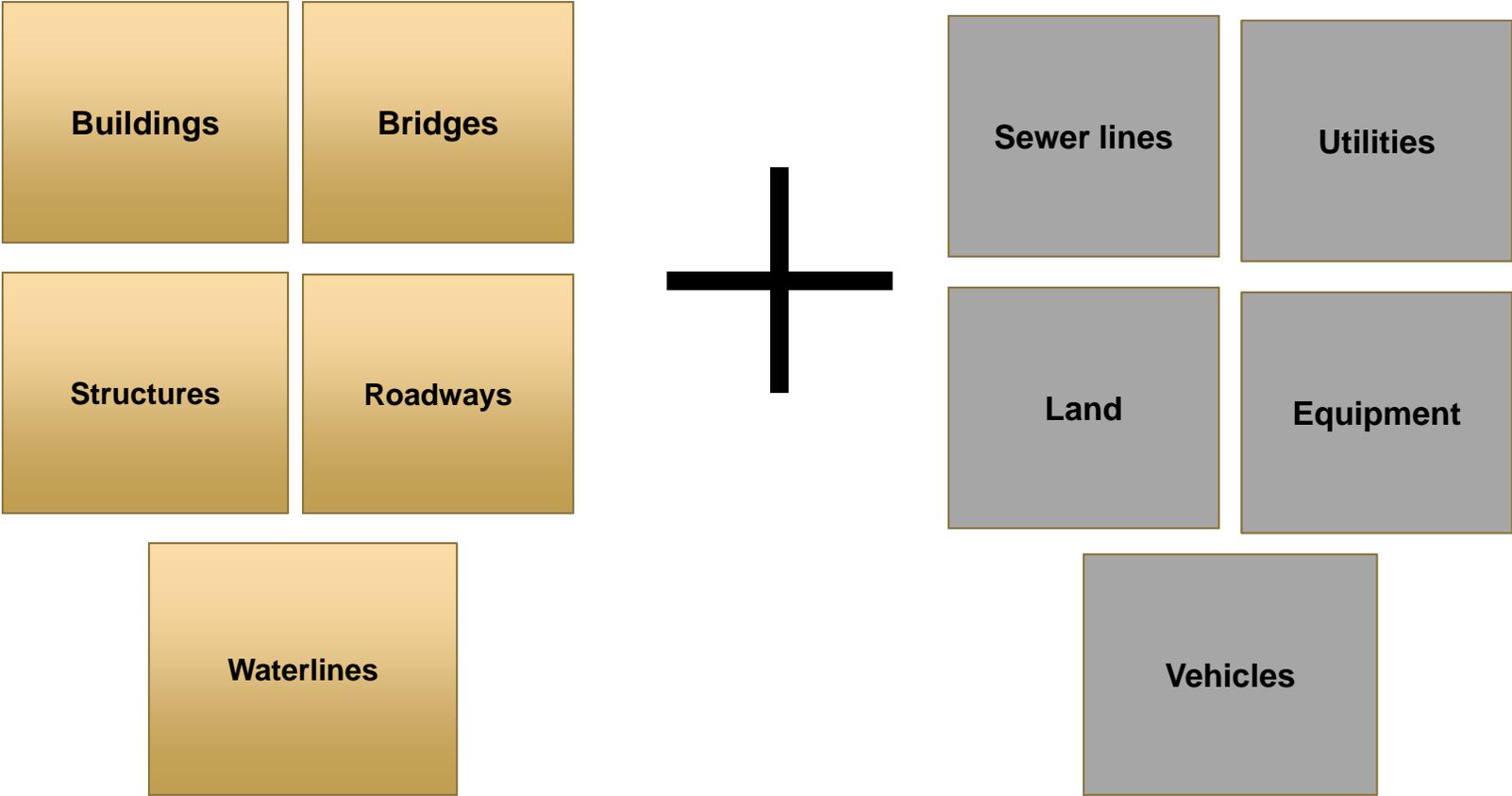
Key Point

- If new facilities are planned, make sure the operating costs have been determined
- Often initial capital outlay funds are available
- Ongoing operating costs are problematic

Ongoing Operating Costs

- Staff required
- Utilities cost per square foot
- Maintenance cost for cleaning, grounds, repairs

Capital Asset Inventory



Asset Details

- ***Acquisition Date*** – the date the asset was purchased or built by the local government
- ***Condition*** – the general state of the asset
- ***Cost*** – the original purchase price of the asset
- ***Description*** – a clear statement of the asset so it is easily identifiable

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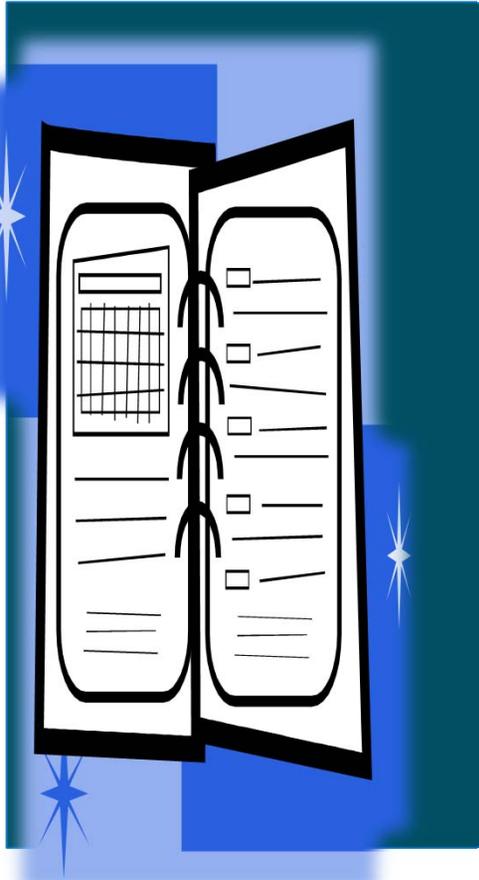
Asset Details

- **Location** – the address where the asset is located
- **Service History** – any repairs or maintenance required to keep the asset in service
- **Use** – the departments or segments of the population that utilize the asset
- **Useful Life** – the anticipated length of time that the asset can be utilized for its intended purpose

Capital Replacement

- Maintain listing of all items such as computers, servers, printers, and other costly equipment
- Include original purchase date and cost
- Estimated date for replacement with associated costs
- Include in annual budget costs of those capital assets to be replaced in the current year

Capital Replacement Schedule



- ✓ Brings attention to the need for maintenance of existing infrastructure
- ✓ Encourages regular replacement and maintenance of assets
- ✓ Commits regular funding to the replacement and maintenance of assets

Advantages of Capital Worksheet

- Facilitates planning for the current and future years' capital replacement
- Provides information in the event an unexpected funding source becomes available
- Provides information to elected officials when planning for future facilities

Budgeting for Capital

- Determine funding options
 - Restricted Taxes
 - Grants
 - Bonds
 - Leases
- Include cost escalations

Strategic Focused Planning

GFOA Newsletter

October 6, 2016

EMPLOYMENT ADS | TRAINING | BEST PRACTICES

Agency Develops Strategic Plan to Manage Short-Term Capital Assets

The Hillsborough Area Regional Transit Authority (HART) understood the importance of properly managing short-term capital assets. Even so, the organization often found itself in reactive rather than planning mode. Many support items that were required to achieve the organization's primary mission had never been looked at from a strategic standpoint. Information technology, for example, was often treated as an afterthought. This reactionary approach of "fix it when it breaks" was the norm; there were no replacement schedules for much of the organization's technology.

As this approach became increasingly unsustainable, HART completely changed its organizational paradigm for short-term capital assets. The first step was to establish a comprehensive IT asset inventory database that included all desktops, tablets, software, switches, routers, servers, phones, etc. Next, the agency developed short- and long-term replacement programs for all IT assets. Finally, HART refined its budget development process, making it more inclusive by assessing user and organizational needs, and building business cases to support CIP needs for short-term capital assets.



Strategic Focused Planning

Hillsborough Area Regional Transit Authority's Seven Step Process:

1. IT Asset Identification
2. Asset Replacement Program
3. Inclusive Budgeting
4. Project Management Office
5. Cost Model
6. Diversify Revenue
7. Programmatic approach





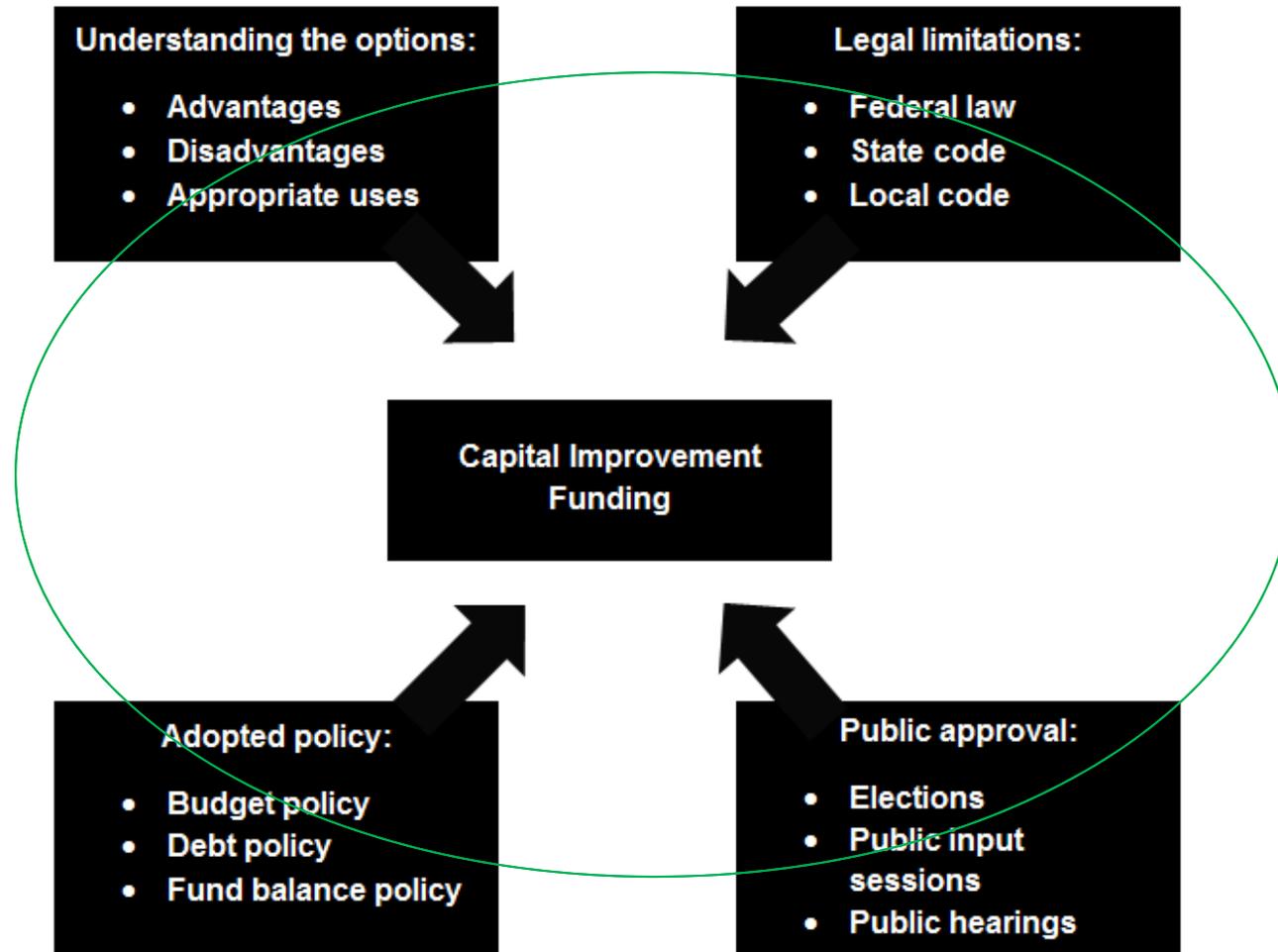
FUNDING SHORT-TERM ASSETS

Typical Funding Methods

- Pay As You Go
- General Obligation Bonds
- Revenue Bonds
 - Non Ad Valorem Pledge
- Restricted Taxes
- Grants
- Partnerships
- Impact Fees
- Fund Balance

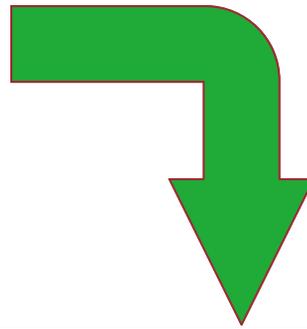


Selecting the Funding



Evaluating the Funding Source

Important for local government to reference the following for guidance on selection of the funding option



- Strategic plan
- Budget policy
- Financial plan

Evaluating the Funding Source

- Who will pay for the project in relation to who benefits from it?
- *Will the money be available when needed?*
- How costly is the financing method?
- *Is the financing method legally permissible?*
- What are the administrative requirements associated with the financing option?

Pay As You Go

Advantages:

- No interest costs
- No bond issuance costs
- Maintains low debt capacity
- Conservative fiscal approach

Disadvantages:

- Long useful life projects paid for by current users only
- Higher taxes may be required to consistently fund CIP
- Needed projects may be unnecessarily delayed
- Delayed projects may result in higher project costs

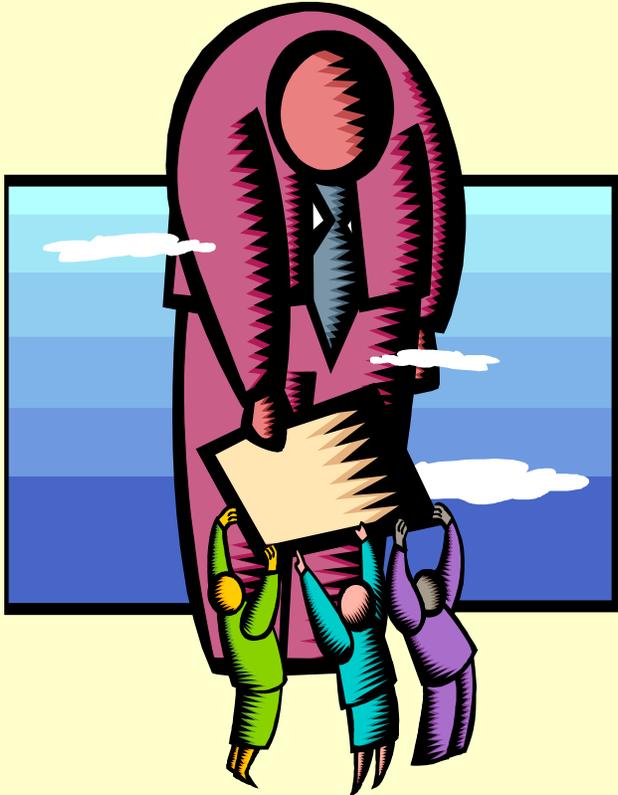
Best used to fund:

- Items with a shorter useful life, such as vehicles

Legal restrictions per Georgia Code/Constitution:

- None

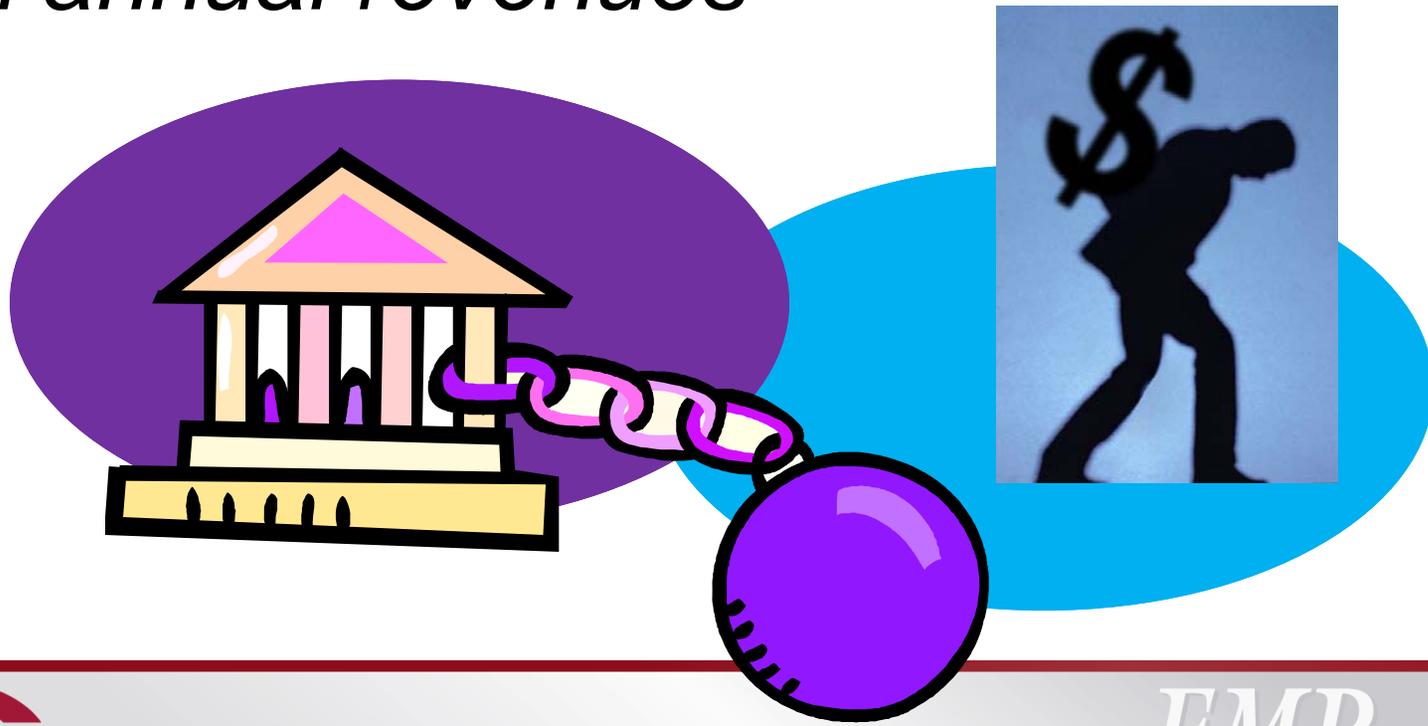
Pay As You Go



- Least complex of the funding options
- Project is executed as funds are available
- Source of revenue from current-year revenue collections, including property taxes
- Dependent on adequate revenue to fund operations, reserves, and capital in a fiscal year

Pay As You Go

Some capital improvements and replacements may be too costly to fund from annual revenues



General Obligation Bonds

Advantages:

- Low interest costs
- Funds readily available to execute projects
- Cost of project is spread over a longer period of time
- Cost is shared by more users

Disadvantages:

- Complicated administrative process
- Lengthy approval process
- Revenue is committed for long term repayment of bonds

Best used to fund:

- Items with a longer useful life, such as buildings and infrastructure

Legal restrictions per Georgia Constitution:

- Advertisement and election required
- Funds must be spent in manner advertised
- Sufficient taxes levied to pay the principal and interest within 30 years
- Debt may not exceed 10 percent of the assessed value of all taxable property

Revenue Bonds

Advantages:

- Funds readily available to execute projects
- Cost of project is spread over a longer period of time
- Cost is shared by the users who directly benefit

Disadvantages:

- Complicated administrative process
- Users are committed to the repayment of the debt

Best used to fund:

- Items such as water treatment plants that have access to user fee revenue

Legal restrictions per Georgia Code:

- Resolution of the governing authority
- Establishment of debt service reserve
- Repayment period not to exceed 40 years
- Interest rate not to exceed 9 percent per annum

Grants

Advantages:

- Funds are provided by state and/or federal government

Disadvantages:

- Complicated administrative process
- Restrictions associated with funds
- Unreliable funding source

Best used to fund:

- Items that deliver a service identified through the strategic plan

Legal restrictions per Georgia Constitution:

- State may provide grants with limited purposes
- Local governments may accept grants from federal government that comply with federal law

Partnerships

Advantages:

- Costs are shared with another government or private entity

Disadvantages:

- Complicated administrative process
- Agreements can restrict future growth or expansion

Best used to fund:

- Items that would be delayed due to lack of funds

Legal restrictions per Georgia Constitution:

- Intergovernmental agreements are limited to 50 years
- Intergovernmental agreements are limited to activities, facilities, and services authorized by law

Partnerships

Evolve as a result of:

- Lack of improvement funds, land, or facilities
- One local government may lack adequate facilities to provide a service
- Another may lack the funds to properly improve facilities or land



Impact Fees

Advantages:

- Costs are supported by the user

Disadvantages:

- Projects may be delayed until adequate fees are collected
- Impact fees may be unattractive to developers

Best used to fund:

- Items that are clearly identified as beneficial to a group

Legal restrictions per Georgia Code:

- Development impact fees are allowed to finance new services and infrastructure required due to new growth
- Local governments are required to adopt a schedule of development impact fees
- Development impact fees can be collected after the issuance of a building permit
- Development impact fees are calculated based on the service provided due to new growth
- Fees must be spent within six years of collection

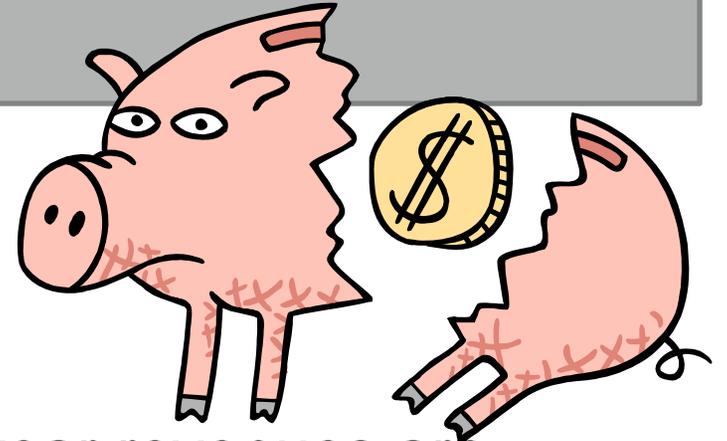
Fund Balance

Advantages:	Disadvantages:
<ul style="list-style-type: none">• No interest costs• No bond issuance costs• Maintains low debt capacity• Conservative fiscal approach	<ul style="list-style-type: none">• Long useful life projects paid for by current users only• Higher taxes may be required to consistently fund CIP• Delayed projects due to lack of funds may result in higher project costs
Best used to fund:	
<ul style="list-style-type: none">• Items that are a one-time expenditure	
Legal restrictions per Georgia Code/Constitution:	
<ul style="list-style-type: none">• None	

Fund Balance

- $[\text{Current assets} + \text{Deferred Outflows}] - [\text{Current Liabilities} + \text{Deferred Inflows}] = \text{Fund Balance}$
- Local governments typically are not required by law to maintain a set level of fund balance
- Many local governments adopt a policy that specifies levels of fund balance to be maintained and appropriate uses of excess fund balance

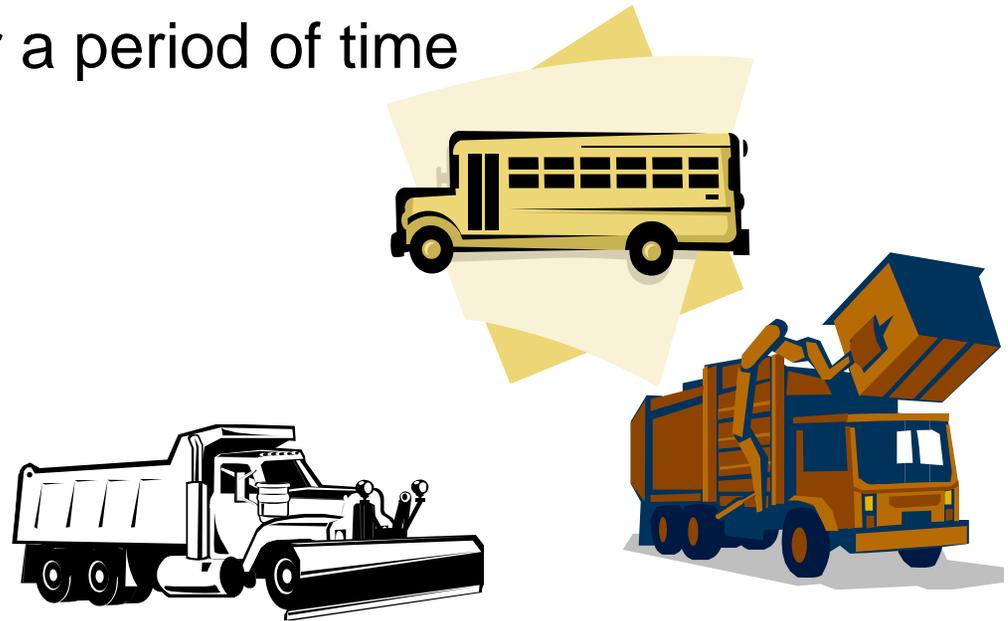
Fund Balance



- Similar to pay-as-you-go
- Assumes the availability of cash
- Pay-as-you-go assumes that current-year revenues are available
- Fund balance may be accumulated over several fiscal years in order to fund an improvement

Lease/Purchase Agreements

- Alternative purchase methods that may expedite capital improvements or replacements should be considered
- Typically used for acquisition of equipment
- Allows a local government to contract with a vendor to purchase equipment over a period of time



Lease/Purchase Agreements

Not a funding source, but a purchasing method

Advantages

- A variety of projects can be funded without incurring voter approved debt
- Allows a flexible financing structure
- Purchase of equipment is not limited by availability of current year revenue
- Avoids depletion of reserves

Disadvantages

- Potential to pay more for capital improvements due to financing rates
- Premature termination of contract forfeits the asset and the payments made to date

Selecting the Funding



Appropriate funding source more readily identifiable once a local government understands the funding options

Examples:

- general obligation bonds might be more appropriate for funding the construction of a jail, administrative city hall, police station, courthouse
- Purchasing replacement vehicles might be more appropriately funded on a pay-as-you-go basis

Suggested Resources

- Government Finance Officers Association
 - www.gfoa.org, Best Practices & Advisories

Related Best Practices:

- › Technology in Capital Planning and Management
- › Determining the Estimated Useful Lives of Capital Assets
- › Asset Maintenance and Replacement
- › Role of the Finance Director in Capital Asset Management

Upcoming Trainings:

- › Accounting for Capital Assets

Past Conference Presentations:

- › Budgeting for Short-Term Capital Assets
- › Case Studies in Capital Asset Management

Related Publications:

- › Capital Confusion: 12 Misunderstandings about Accounting for Capital Assets

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