

SECTION: **POLICY STATEMENT - GENERAL AND ADMINISTRATIVE**

SUBJECT: **DEPRECIATION POLICY**

PURPOSE: To provide general direction to management in the definition of depreciable assets, the determination of useful lives, and the method of allocating depreciation costs.

EFFECTIVE DATE: **March 12, 1993**

HISTORICAL: April 17, 1992

DEPRECIATION POLICY

I. BACKGROUND AND PURPOSE

- A.** The American Institute of Certified Public Accountants, in its Accounting Terminology Bulletin, provides the following accounting definition of depreciation:

"Depreciation accounting is a system of accounting which aims to distribute the cost or other basic value of tangible assets, less salvage (if any), over the estimated useful life of the unit (which may be a group of assets) in a systematic and rational manner. It is a process of allocation, not of valuation. Depreciation for the year is the portion of the total charge under such a system that is allocated to the year."

The prevailing view is, therefore, that the basic purpose of depreciation accounting is the spreading of the cost of a fixed asset over its useful life and the reflection of this cost in the statements of operation. There is a corresponding systematic reduction in the "book value" of the fixed asset, but this effect is secondary to the cost distribution function.

With the basic purpose of cost allocation established, this policy statement is intended to provide general direction to Corporation management in the definition of depreciable assets, the determination of useful lives, and the method of allocating depreciation costs.

II. POLICY

A. Depreciable assets will be classified as Equipment, Computer Software, Facility Improvements, Leasehold Improvements, or Extraordinary Repairs and Replacements. These items have a cost factor which must be recovered by matching income and expense.

1. Criteria for capitalization and depreciation.

a. Cost to be recovered from one of the Corporation's auxiliary activities, including commercial operations, conferences and workshops, indirect cost recovery funds held by the Corporation, research centers, and institutes.

b. Corporation restricted or designated funds.

2. Criteria for direct expense.

a. Assets received by the Corporation as gifts.

b. Assets purchased with externally sponsored program funds.

c. Requests from the University to purchase equipment or renovate facilities which generate no revenue for the Corporation, or in supportive programs for which the Corporation has no direct management responsibility.

B. Classification of Assets.

1. Equipment

a. Equipment is defined as movable articles of nonexpendable property which have all of the following characteristics:

(1) A normal useful life of three years or more.

(2) An identity which does not change with use.

(3) A nature that makes formal property accountability practical.

(4) An approximate unit cost of \$500.00 or more.

- b. Note: Sensitive property, which is defined as any highly desirable and portable item (e.g., personal computer, equipment, calculators, dictaphones, cameras, etc.) may not meet the minimum cost criteria and may be included as equipment for accountability purposes.

2. Improvements

- a. Improvements consist of all structures, additions to structures, replacement of fixtures permanently attached to structures, and remodeling of structures. All such improvements, additions, or replacements with a cost of \$2,500 or more will be capitalized when installed and depreciated over a useful life period as determined by the Executive Director.

3. Extraordinary Repairs and Replacements

- a. Repairs and replacements are expenditures that keep the property in good condition or put it back in good condition, but do not create a new facility better than the old one was when it was acquired. Repairs and replacements can be either "ordinary" or "extraordinary." Ordinary repairs and replacement expenditures are those which keep a facility in efficient operating condition without significant benefit to future periods and are therefore not capitalized.
- b. Extraordinary Repairs and Replacements expenditures are those which extend the life of the facility or those which that are significant in cost and cyclical in nature. Expenditures for carpeting, exterior painting, replacement of conveyor belts and draperies, or reconditioning of ovens are examples of Extraordinary Repairs and Replacements.

4. Determination of Useful Life

- a. The service life of an asset or group of assets represents the period of usefulness to its owner. To provide a basis for depreciating the cost of fixed assets, an estimated useful life is determined after consideration of the following factors:
 - (1) Physical factors:
 - (a) Wear and tear
 - (b) Deterioration and decay

- (c) Damage or destruction
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- (2) Functional factors:
 - (a) Inadequacy
 - (b) Obsolescence
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- b. These factors relate to physical deterioration as well as to the suitability of the asset in functioning as an economically productive unit. Physical factors are generally more predictable than functional factors. Historical data and planned usage provide management guidance on the effect of the physical factors. Inadequacy and obsolescence, however, are generally not anticipated.
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- c. Since Corporation fixed assets must be funded from retained earnings, with the cost recovered from operations, and since there is known risk in estimating the service life of any fixed asset, it shall be the policy of the Corporation Board that a conservative approach be utilized by management in estimating service lives. The procedure for determining the useful life of any fixed asset shall be as follows:
 - (1) The departmental request for approval of a capital outlay expenditure shall provide management with the department head's estimate of:
 - (a) The minimum service life.
 - (b) The requested service life for depreciation purposes.
 - (c) The estimated replacement date for reserve purposes.
 - (2) The Executive Director will approve the requested service life, or modify the service life if deemed necessary, prior to submission of the capital outlay request to the Corporation Board of Directors, or authorization of the expenditure if Board approval is not required.
 - (3) The approved service life and the estimated replacement date will be utilized by the Corporation Business Office when this item is added to the Plant Ledger.

III. PROCESS

- A.** The Straight-Line Method shall be used in depreciating all fixed assets. This method is based on the passage of time and recognizes equal periodic charges over the service life of the asset. For depreciation purposes, the service life will be expressed in months and will begin on the first day of the month following the acquisition date. Salvage values will not be assigned to any fixed asset.