



TOWN OF ELIZABETH

PATRICK G. DAVIDSON, TOWN ADMINISTRATOR

TO: Honorable Mayor, Mayor Pro Tem, and Members of the Board of Trustees
FROM: Patrick Davidson, Town Administrator
DATED: October 10, 2024
SUBJECT: Proposed Changes to Financial Policies for the Town of Elizabeth

BRIEF SUMMARY

This Memorandum discusses some of the complexities of capital improvement funds and a brief summary is likely helpful for the analysis. Currently, computers and software are not funded through the Capital Improvement Fund. This means that even if the Town purchases a dozen computers, at \$1,000 each, this \$12,000 is not a capital expense. The same is true for computer software, even though it may cost tens of thousands of dollars per year for licensing and upgrades. With Board approval, recent changes to accounting standards allow for IT equipment and software to be combined to meet capital expenditure requirements.

The overall impact of the policy change is that computers and software would no longer be expensed as operating expenditures, but rather treated as long-term capital expenditures. The effect is that it lessens the impact on the General Fund and transfers the expenses to the Capital Fund where the costs can be readily absorbed.

BACKGROUND

1. Aggregating Capital Expenditures to Meet the \$5,000.00 Threshold. The Town of Elizabeth follows the capitalization rules proscribed by the Governmental Accounting Standards Board (GASB) with regard to the capitalization of assets. For purposes of Elizabeth, two conditions must exist to be considered a capital expense: (1) the purchase price for the property or equipment is valued over \$5,000.00; and (2) the acquired asset must have a useful life of more than one-year.¹

For several years, GASB struggled with how to acknowledge items such as computers, furniture, office equipment, and library books that, individually, could never meet the capitalization standards; while recognizing that in sum these expenditures could far exceed the \$5,000.00 threshold. GASB Implementation Guide No. 2021-1 has clarified this distinction to allow – under certain circumstances – *for individual assets, whose aggregate is significant*. Further, the language seems to imply that capitalization *is required* to capitalize individual assets that are below the threshold when *significant* in the aggregate. With the passage of Question 5.1 in Implementation Guide 2021-1, this change to capital expenditures may be effective for all reporting periods

¹ See generally, GASB Statement #34. Capital Assets and Depreciation Guidance, August 31, 2001. (Useful life beyond a single reporting period.)



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beginning after June 15, 2023. Furthermore, the change appears to allow retroactive application of the rule from 2021 to 2023 by restating the financial statements for the periods impacted.²

For the Town of Elizabeth, with a comparatively small budget, items such as computers and other equipment are quite expensive in the aggregate. For example, within 2024, and expected in 2025, a total of \$54,901.53 will be spent solely to acquire computers/tablets, not including monitors, updated printers, etc. Individually, no single computer can, or likely ever will, approach the \$5,000.00 threshold, yet the impact on the operating budget for the Town cannot be ignored.

The question in the application of GASB Implementation Guide No. 2021-1 is one of *significance*. The term, while used consistently by GASB in analyzing Statement #34, is not defined. As such, it is for the individual governmental entity to determine if something is significant when viewed in its totality. Additionally, care must be taken not to aggregate items which have substantially different useful lives or that are not of the same kind or nature. [For example, commingling computers with phones and police radios and labeling them as “Communication.”]

2. Update to Treat Computer Software Acquisition as a Capital Expenditure. Under some circumstances, capital expenditures may include intangible assets. While in general, we think of capital expenditures as vehicles, desks, heavy equipment, and land, they may also include intangible items such as water rights, easements, and computer software. Both GASB Statement 51 (in this instance software acquisition) and GASB Statement 96 (in this instance software subscription agreements) underscore the need to accurately account for the intangible asset of computer software. Most of the discussion is based on the value of upgrades to existing software, the value of coding, or the process of creating software for sale to others. In the case of Elizabeth, much of this discussion is irrelevant.

To complicate the matter, in many instances, government entities not only directly purchase software, but may also purchase software updates and enhancements to existing software packages. [For example, an upgrade from Adobe Acrobat to Adobe Acrobat Pro, or in the case of EPD including additional services to existing police programs.] For Elizabeth, oftentimes the computers purchased include basic operational software, which likewise is updated by Phoenix Technologies. Lastly, Phoenix Technologies maintains certain types of security software on the computers. Consequently, there are times that the initial purchase of software is combined with future licensing agreements and subscriptions.

GASB 51 was published in June 2007 and became effective after June 15, 2009. The goal was to clarify the categories of intangible assets for accounting purposes. GASB 51 clearly includes computer software (purchased or licensed from a third party) as an intangible asset and is a capital

² This change in capital expenditures was not taken into consideration within prior audits and has not been brought to the attention of staff through the Town’s auditors.



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asset. As such, the Capital Improvement Fund may be used for such purchases if authorized by the governing body.³

Similar to the item discussed above, new computer software, and annual licensing agreements do have a substantial impact on the Town's budget. For example, New World Reporting for the EPD has a price of \$35,000 in 2025 if approved by the Board of Trustees, with annual licensing thereafter starting at \$3,000 per year. In total, the Town is expected to spend at least \$103,500 on new software and licensing. If implemented, it is an appropriate expenditure for the Capital Improvement Fund, which is not only capable of supporting the expenditure, but also assists in relieving the strains on the General Fund.

ANALYSIS

1. Aggregating Capital Expenditures to Meet the \$5,000.00 Threshold. Should the Board of Trustees adopt a change to the Financial Policies, it would allow the Town to combine smaller like-kind purchases into Capital Improvement Fund expenditures.
2. Update to Treat Computer Software Acquisition as a Capital Expenditure. Should the Board of Trustees adopt a change to the Financial Policies, smaller purchases like computers may be combined to meet the standards for using Capital Improvement Funds.

STAFF RECOMMENDATION

Staff recommends the Board of Trustees consider the application and acceptance of the attached Capital Fund Expenditure Policy to reflect the changes implemented by GASB as more fully set forth herein and in the associated Resolution.

BUDGET CONSIDERATIONS

While the passage of the Policy does not, in itself, create a budget expenditure, it has substantial budgetary impacts for the General Fund.

ATTACHMENTS

Capital Expenditure Policy

³ There are substantially different lines of thought on this matter, particularly within the private sector. Those include the acquisition of new software, internal upgrades to developer software, and specially developed and purchased software from third parties. While those concerns are important, including for tax purposes, they do not overall impact the analysis for the Town of Elizabeth.

CAPITAL EXPENDITURE POLICY

The purpose of this Capital Expenditure Policy is to establish updated policies and procedures regarding the definition of a "Capital Expenditure" for the Town of Elizabeth. The underlying goals of the policy are to: (1) provide specific guidance to the Town Staff as to how budgetary items should be considered for purposes of capital expenditures; (2) provide guidance to Staff as to when it may be appropriate to aggregate capital expenditures under Governmental Accounting Standards Board (GASB) Statement #34 and Implementation Guide No. 2021-1 (effective June 15, 2023); (3) provide guidance to Staff as to the potential use of capital funds for the acquisition, maintenance, and licensing of computer software under GASB Statement 51 and GASB Statement 96; and (4) provide guidance for future Boards.

GENERAL REQUIREMENT:

The Town of Elizabeth, in keeping with GASB, shall consider a capital expense to encompass any single purchase for which: (1) the purchase price for any asset, property, or equipment is valued over five thousand dollars (\$5,000.00); and (2) when the acquired asset, property, or equipment has a useful life of more than one-year.

EXCEPTION UNDER GASB IMPLEMENTATION GUIDE NO. 2021-1:

The Town's Finance Manager, in consultation with the Town Administrator, may consider aggregating capital expenditures which do not meet the General Requirement if:

1. The expenditure is considered significant when viewed in the totality of the specific operating budget for the department in which the expenditure arises; OR
2. Such an expenditure is considered significant when viewed in the totality of the Town's General Fund operating budget.

By way of example the purchase of portable radios for the Elizabeth Police Department, wherein each individual portable radio would not meet the \$5,000.00 expense requirement. The final determination as to the appropriateness of aggregating expenditures under this provision shall be by the Elizabeth Board of Trustees.

EXCEPTION FOR INFORMATION TECHNOLOGY:

The Town's Finance Manager, in consultation with the Town Administrator, may consider aggregating capital expenditures which do not meet the General Requirement if:

1. Such an expenditure is for the purchase of computer equipment, including but not limited to, computers, monitors, switches, firewalls, printers, scanners, and related hardware which function either separately or in unison to provide useable technology for Staff and the Public; OR
2. Such an expenditure is for the purchase, installation, and/or upgrade of any computer software determined to be important or necessary in meeting the demands of the Town's operations or the organization, and such computer software is valued at over five thousand dollars (\$5,000.00); and (2) when such software has a license of at least one (1) year.

The final determination as to the appropriateness of aggregating expenditures under this provision shall be by the Elizabeth Board of Trustees.

BUDGET CONSIDERATIONS:

During the Budget Process, the Finance Manager and the Town Administrator shall inform the Board if any of the exceptions detailed herein are being used in the preparation, drafting, and passage of the Town's Budget. Further, a majority of the Elizabeth Board of Trustee, should determine within each Budget, if the public's needs are met through the exercise of the exceptions herein.

RESOLUTION 24R42

A RESOLUTION AMENDING THE CAPITAL EXPENDITURE POLICES FOR THE TOWN OF ELIZABETH TO REFLECT CHANGES TO THE CAPITALIZATION RULES AUTHORED BY THE GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB).

WHEREAS the Town of Elizabeth adheres to the rules and guidance provided by the Governmental Accounting Standards Board (GASB) as part of its financial management; and

WHEREAS, GASB has authored changes to its capitalization rules which: (1) allow the Town to aggregate smaller like-kind purchases for capital expenditures should certain conditions exist; and (2) allow for computer software to be considered as capital expenditures if certain conditions exist; and

WHEREAS the Board of Trustees seeks to update and amend existing capital expenditure policies to reflect updates to GASB standards.

NOW THEREFORE BE IT RESOLVED BY THE BOARD OF TRUSTEES OF THE TOWN OF ELIZABETH, COLORADO AS FOLLOWS:

SECTION 1. The Board of Trustees hereby approves and adopts the revised and updated changes to the Town's Capital Expenditure Policy as attached hereto as Exhibit A.

PASSED, APPROVED, and ADOPTED this 22nd day of October 2024, by the Board of Trustees of the Town of Elizabeth, Colorado, on first and final reading, by a vote of _____ for and _____ against.

Tammy Payne, Mayor

ATTEST:

Michelle M. Oeser, Town Clerk

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