Summary of Business Rule With Corresponding Analysis on The Department of Defense Military Equipment Capitalization Threshold

Background

The Department is moving away from a standard capitalization threshold for all types of General Property, Plant, and Equipment (GPP&E) to one that is tailored to real property, military equipment, and general property asset categories.

All items of military equipment, which previously were considered National Defense PP&E, are now classified as General PP&E, pursuant to Statement of Federal Financial Accounting Standards (SFFAS) No. 23, *Eliminating the Category National Defense Property, Plant, and Equipment.*

For financial reporting purposes the Department is treating military equipment (ME) as a subset of General PP&E and reporting it separately. The primary difference between ME and the balance of General PP&E is that ME is generally procured for tactical/battlefield situations.

Prior to SFFAS No. 23, the acquisition costs for military equipment items classified as National Defense PP&E were expensed in the period incurred. Now that military equipment is classified as General PP&E, the Department is pursuing a major initiative to capitalize and depreciate military equipment end items.

Paragraph 13 of SFFAS No. 6, *Accounting for Property, Plant, and Equipment,* states that capitalization thresholds should be established by Federal entities rather than centrally by the Federal Accounting Standards Advisory Board. Federal entities are diverse in size and uses of PP&E, and must consider their own financial and operational conditions in establishing an appropriate threshold or thresholds.

Issue

The capitalization threshold for General Property and Equipment had been set at the then existing threshold for using procurement funding, i.e., generally assets with a unit cost of $100,000. Some within the audit community have expressed concern that this threshold might be too high and might exclude significant amounts of equipment from valuation.

Initially $100,000 was the threshold used to identify the military equipment (ME) that should be capitalized. However, during the valuation effort, this threshold was modified for two reasons. First, accounting systems were not always able to associate individual military equipment items with the related expenditures. When this occurred the concept of Group and Composite depreciation was used and the entire line was valued as a single asset. Second, the Department "owned" billions of dollars in wheeled vehicles, with unit costs between $50 thousand and $100 thousand. The Department judgmentally

determined that, based on the magnitude of the dollars involved, these vehicles should be capitalized.

A study was initiated to assess the revised threshold, however, absent a consolidated universe of military equipment assets, the study could not be structured in a way to make it statistically valid.

Alternatively, an assessment of the three tier threshold focused on Marine Corps assets that had unit costs between $50 thousand and $100 thousand and that would therefore be expensed under the proposed three tier threshold criteria. Most of these assets could be categorized as personal equipment (including weapons), radios, commercial items, vehicles or shelters. The Department believes that most items in this dollar category will have a useful life of less than two years when they are used for the purpose intended and that as such the items should be expensed.

Approach

The Department believes that the analysis referenced above, plus the language in Statement of Federal Financial Accounting Standards No. 23, that gave the Department flexibility in establishing the ME baseline, support a decision to value ME using the following three criteria.

1. ME assets with a unit cost equal to or greater than $100,000, where the cost of individual end items is known or can be calculated using the baseline valuation methodology, and where end items can be uniquely identified, will be capitalized as separate items.

2. ME assets having a unit cost of all or some of the end items is in excess of $100,000 and where end items cannot be uniquely identified will be capitalized at the total program cost level.

3. ME assets that have a unit cost of $50,000 or more, where the information is unavailable or it is impractical to assign costs by end item, and where the items to be acquired are homogenous self propelled vehicles, will be capitalized on a group basis.