**U.S. Department of Justice**
Federal Bureau of Prisons

# Program Statement

**OPI:** FPI
**NUMBER:** 8563.08
**DATE:** 12/13/2001
**SUBJECT:** Depreciation of Fixed Assets

1. **PURPOSE AND SCOPE.** To provide policy and procedures for computing and recording depreciation charges for all Federal Prison Industries (FPI) fixed assets at both Central Office and field locations.

Depreciation is a systematic and rational allocation of the acquisition cost of an asset, less its estimated salvage or residual value, over its estimated useful life. The system of allocation should match cost with related revenue correctly, while recognizing the asset's declining service value.

Depreciation expenses are to be recognized on all fixed assets that meet FPI's capitalization criteria as outlined in the Program Statements on Machinery and Equipment and Building and Improvements. All factories are to use the straight-line method of depreciation.

2. **SUMMARY OF CHANGES.** The more significant revisions to this directive are:

- Procedures have been modified to reflect FPI's implementation of **Millennium**, its Enterprise Resource Planning (ERP) system;
- Criteria for depreciating internal use software has been included.

3. **PROGRAM OBJECTIVES.** The expected results of this program are:

a. The cost of a capitalized asset will be uniformly and periodically matched with revenues over the estimated useful life of that asset.

b. Depreciation charges will be consistently applied throughout the Corporation.

c. Depreciation charges, and the resulting effect on the income of the Corporation, will be determined in accordance with generally accepted accounting principles and with the Federal Accounting Standards Advisory Board's (FASAB) Federal Financial Accounting Standards.

4. **DIRECTIVES AFFECTED**

a. **Directives Rescinded**

| | |
|---|---|
| PS 8563.05 | Depreciation of Fixed Assets, FPI (3/19/99) |

b. **Directives Referenced**

| | |
|---|---|
| PS 8563.04 | Building and Improvements (7/8/98) |
| PS 8563.06 | Machinery and Equipment - Fixed Assets (6/11/99) |
| DOJ 2400.3 | Justice Property Management Regulations (8/6/98) |
| SFFAS No 6 | Accounting for Property, Plant, and Equipment June 1996 |
| SSFAS No 10 | Accounting for Internal Use Software June 1998 |

5. **STANDARDS REFERENCED.** None.

6. **DEFINITIONS**

a. **Straight-line Depreciation Method.** A method of allocating depreciation whereby the cost of the asset is allocated uniformly over the asset's life. This method results in period charges of equal amounts.

b. **Estimated Useful Life.** An asset's estimated useful life is the total number of years service expected from that asset. Useful life is influenced by both physical factors (i.e., wear and tear, deterioration) and operative factors (i.e., obsolescence, usefulness).

All property, plant, or equipment with a useful life of less than five years, except for internal use software, must be charged to expense when it is acquired. Internal use software that has an estimated useful life of two or more years and meets

the requirements contained in the Program Statement on Machinery and Equipment is to be capitalized.

c. **Salvage (Residual) Value.** The amount (dollar value) that can reasonably be expected for the asset at the end of its useful life. For depreciation calculation purposes, FPI assumes the salvage value of all assets to be zero.

d. **Idle Equipment.** Equipment that is expected to remain idle (out of use) for at least 90 days.

7. **DETERMINING THE USEFUL LIFE OF AN ASSET.** Upon acquiring an asset, the Business Manager must determine its useful life.

a. Factors to be considered in making that determination are:

- physical wear and tear,
- past experience with similar assets,
- the asset's present condition,
- the factory's maintenance policy, and
- technological/industry trends (e.g., obsolescence).

The Business Manager is to consult one or more of the following sources to help determine an asset's useful life:

- Manufacturer specifications, literature, etc;
- FPI's Product Support Center (PSC) at Englewood, CO;
- The latest Internal Revenue Service publication on Depreciation or the estimated service life of classes of equipment as published by the Department of Commerce's Bureau of Economic Analysis.

b. The Department of Justice has provided the following guidance for estimating the useful life of internal use software (as defined in the Program Statement on Machinery and Equipment):

- Business software, including those applications used to manage individual business functions (i.e., financial, procurement, inventory, warehouse, production scheduling, etc.) has a recommended useful life of seven years;

- Personal productivity and desktop operating software (i.e., word processing, spreadsheet, graphics, etc) have a recommended useful life of three years;

- Operating systems and systems administration middleware, layered software, E-mail, run-time services, and development tools and utilities have a recommended useful life of five years.

c. An asset's estimated useful life is to be included in the Request for Special Authorization or equipment request form submitted to Central Office for acquiring that asset.

d. Any changes in estimated useful life are to be accounted for in the period of the change and future periods. No adjustments are to be made to previously recorded depreciation.

8. **CALCULATING THE STRAIGHT-LINE DEPRECIATION METHOD.** All assets classified as Building and Improvements and as Machinery and Equipment (unless waived by the Controller) are to be depreciated using the straight-line depreciation method.

a. To maintain consistency of depreciation rates between locations, the following schedule is to be applied:

| RATE NUMBER | LIFE RANGE IN YEARS | NUMBER OF YEARS TO DEPRECIATE |
|---|---|---|
| - | Less than 5 | None |
| 1 | 5 - 8 | 5 yrs |
| 2 | 9 - 14 | 10 yrs |
| 3 | 15 - 20 | 16 yrs |
| 4 | 21 - 30 | 24 yrs |
| 5 | 31 - 50 | 40 yrs |

**Note:** When estimating useful life for internal use software, refer to the guidance in Section 7.b. in consultation with staff in the Management Information Systems Branch.

- Rates 1, 2, and 3 generally are to be used for equipment. Although most production equipment and forklifts have a useful life of 10 years, some equipment, such as heavy metal presses, may have a longer depreciable life. Business Managers are to consult the sources mentioned in Section 7.

- Rates 4 and 5 generally are to be used for buildings and improvements. For example, a pole barn type of warehouse may have a shorter life (i.e., 20-30 years) than a more solid structural building with footings (i.e., 40 years).

b. The Business Manager must use the table in Section 8.a. to ascertain the number of years to depreciate an asset by determining the life range in years for the asset.

> **Example:** A press in a Metal Factory has a useful life of 12 years. Since the life range is between nine and 14 years, the number of years to depreciate is 10. The useful life, 10 years, is to be entered into the Master Asset Record. The **Millennium** system then calculates the monthly rate of depreciation.

9. **RECORDING DEPRECIATION CHARGES.** Monthly depreciation charges on all machinery and equipment and building and improvements begin on the first day of the month in which the items are acquired and ready for use.

a. The following class codes and corresponding accounts are to be established in **Millennium**:

| Class Codes | Description | Asset Account | Accum Depreciation | Depreciation Expense |
|---|---|---|---|---|
| 1000 | Building & Impr | 173000 | 173900 | 614700 |
| 2000 | Mach & Equip | 175100 | 175900 | 614500 |
| 2500 | Assets Under Capital Lease | 181000 | 181900 | 614500 |
| 3000 | Non Capitalized | ----- | ----- | ----- |
| 4000 | Assets Under Const | 172000 | ----- | ----- |
| 5000 | Donated B&I | 173000 | 173900 | 614700 |
| 5100 | Donated M&E | 175100 | 175900 | 614500 |

b. At the beginning of each month, the Financial Manager or designee in the Financial Management Branch (FMB) is to calculate and post the depreciation for the preceding month. After the depreciation expense has been posted, the Financial Manager or designee is to close the previous posting period for assets.

c. The accountant at each location is to review the monthly depreciation charges for fixed assets at his or her location for accuracy. Errors to review include incorrect depreciation amounts, assets in service with no depreciation charges, and assets that are fully depreciated, retired, or disposed and still being depreciated.

The Business Manager is to report any errors immediately to the Deputy Controller or designee in FMB in Central Office.

10. **COST ACCOUNTING.** Generally, whenever a special tool, die, jig, or other equipment is purchased or manufactured for a special job or contract, the cost of that equipment is to be charged to that job. However, if it is definitely known that such equipment will be used on future contracts or other production and the equipment meets FPI capitalization criteria, that equipment is to be capitalized and depreciated over its useful life.

11. **DEPRECIATING IDLE EQUIPMENT.** When Machinery and Equipment is classified as "idle," depreciation at the established rate is to continue until that asset is:

- fully depreciated,
- retired,
- disposed, or
- no longer functional.

12. **RECAPTURE OF DONATED PROPERTY EXPENSE.** Although Donated Machinery and Equipment is depreciated the same as other M&E, the expense is recaptured monthly to prevent distortion of the results of the Corporation's operations. Depreciation expenses are to be recaptured on Donated M&E by debiting account 322000, Donated Property--Current Year (or 322500, Donated Property -- Prior Year, if applicable), and crediting account 713000, Recapture of Donated Property.

**Note:** Field locations may need to contact the Financial Manager in FMB in order to affect the 322000 account.

At fiscal year end, the Corporate Accountant in FMB is to prepare a manual journal entry transferring the amounts in the Donated Property -Current Year account (322000) to the Donated Property - Prior Years account (322500).

The Business Manager is to maintain a separate schedule to ensure that the recapture of depreciation expenses associated with donated equipment agrees with the depreciation expenses for that equipment.

/s/
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Director