Capital Asset Best Practice Overview

Wednesday, May 22, 2019 10:30 AM to 12:10 PM

Los Angeles, California

Merill King (Moderator)
Finance Director/Treasurer, City of Minnetonka, Minnesota

Grace O. Martinez
Director of Accounting, San Mateo County Transit District (SamTrans); Caltrain; San Mateo County Transportation Authority

Natalie Kent
Local Government Specialist, Local Government Finance Professionals Queensland Inc.

Kent Austin
Bond Program Manager, City of Dallas, Texas
“Money is the wheel to give motion to the machine . . . .”

--Pierre Charles L’Enfant, 1791
CAPITAL ASSET BEST PRACTICE OVERVIEW

Moderator
Merrill King, Minnetonka, MN, USA

Panelists
Kent Austin, Dallas, TX, USA
Grace Martinez, San Mateo, CA, USA
Natalie Kent, Burpengary, QLD, Australia
Why is there a need for the capital budget to be separate from the operating budget? Isn’t it all spending?
1. Why is there a need for capital budget to be separate from the operating budget? Isn’t it all spending?

**Capital Expenditures vs Operating Expenditures**

- Non-recurring
- Longer to complete
- Multi-year funding
- Generally become a capital asset when completed
- Dollar amount is generally huge

- Occur yearly
- Funded from current revenues
- Single-year funding
- Expensed / R&M
What should I consider in managing and replacing capital assets, and how should a government manage its capital assets program?
2. What should I consider in managing and replacing capital assets, and how should a government manage its capital assets program?

- Inventory of capital assets
- Written policies
- Performance standards

- Evaluation of existing capital assets
- Financial policies
- Allocation of sufficient funds
- Report on capital assets
Who should be in charge of the CIP? The finance department, the public works department, or someone else?
3. Who should be in charge of the CIP? The finance department, the public works department, or someone else?

- Often the budget or finance department
- Important thing is to have someone designated
- “When everyone is in charge, no one is in charge”
What areas should Finance Directors consider when engaging in capital management discussions, and what are their challenges in capital asset management?
4. What areas should Finance Directors consider when engaging in capital management discussions, and what are their challenges in capital asset management?

**Areas to Consider**
- Development of written policies
- Status and understanding of assets inventory
- Asset valuation
- Business procedures
- Level of service and condition
- Contribution of assets to overall performance
- Budgeting for repair, replacement, and retirement
- Integration of asset management to financial models
- Use of automated tools

**Challenges**
- Centralized vs decentralized
- On-going communication with stakeholders
- On-going engagement of Finance Director
What data and information elements need to be collected and evaluated to develop a robust long-term financial plan/forecast?
5. What data and information elements need to be collected and evaluated to develop a robust long-term financial plan/forecast?

- Population growth
- Property value growth
- Consumer cost index, inflation
- Anticipated property tax rates
- Anticipated changes in other revenues
- CIP forecast
- Opening cash or fund balance
How does the long-term financial plan interact with the annual budget, asset management plans, and financial management policies of the public sector entity?
6. How does the long-term financial plan interact with the annual budget, asset management plans, and financial management policies of the public sector entity?

Queensland example:
What are the considerations, and what basis should be used, in estimating the useful lives of capital assets?
7. What are the considerations, and what basis should be used, in estimating the useful lives of capital assets?

- Determination of useful life:
  - Own past experience with similar assets
  - General guidelines from professional or industry organizations
How does the source of a project’s funding impact its implementation or the use of leftover funds?
8. How does the source of a project’s funding impact its implementation or the use of leftover funds?

- Can be very significant

- Conditions or restrictions may accompany source—e.g., bond proceeds for a specific proposition

- Pay as you go usually less restrictive
Question 9

Why do we need to depreciate capital assets, and what does accumulated depreciation tell us? Is there cash reserved in that account to replace the asset?
9. Why do we need to depreciate capital assets, and what does accumulated depreciation tell us? Is there cash reserved in that account to replace the asset?

- GAAP requires that capital assets be depreciated
- Accumulated depreciation:
  - Allocation of an asset’s cost
  - Allocation is based on estimated useful life
  - Accumulated depreciation ≠ Market value
How should a local government decide which projects to fund? There will always be more needs than resources.
10. How should a local government decide which projects to fund? There will always be more needs than resources.

- GFOA recommends “a structured process for prioritizing need and allocating limited resources.”

- Example—weighted criteria and scoring
  - Health/Safety: 30 points
  - Savings/Cost Avoidance: 10
  - Legal Mandate: 40
  - Quality of Life: 10
  - Improved Mobility: 10
  - Total: 100
10. How should a local government decide which projects to fund? There will always be more needs than resources.

- Example—weighted criteria and scoring

Project: Middle Cove Dr. street reconstruction

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Weight</th>
<th>Score</th>
<th>Weighted Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health/Safety</td>
<td>30 points 3</td>
<td>90</td>
<td></td>
</tr>
<tr>
<td>Savings/Cost Avoidance</td>
<td>10</td>
<td>3</td>
<td>30</td>
</tr>
<tr>
<td>Legal Mandate</td>
<td>40</td>
<td>2</td>
<td>80</td>
</tr>
<tr>
<td>Quality of Life</td>
<td>10</td>
<td>5</td>
<td>50</td>
</tr>
<tr>
<td>Improved Mobility</td>
<td>10</td>
<td>5</td>
<td>50</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100</strong></td>
<td><strong>300</strong></td>
<td></td>
</tr>
</tbody>
</table>
10. How should a local government decide which projects to fund? There will always be more needs than resources.

- **Example**—weighted criteria and scoring results

<table>
<thead>
<tr>
<th>Project</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Arapaho Road traffic signal replacement</td>
<td>400</td>
</tr>
<tr>
<td>La Manga street resurfacing</td>
<td>350</td>
</tr>
<tr>
<td>Middle Cove Dr. street reconstruction</td>
<td>300</td>
</tr>
<tr>
<td>Meadow Creek Dr. curb and gutter replacement</td>
<td>250</td>
</tr>
<tr>
<td>La Cabeza street resurfacing</td>
<td>250</td>
</tr>
</tbody>
</table>
Considering both the technical and financial aspects of capital planning and management, what are some of the modern technologies that bring rigor to the process?
11. Considering both the technical and financial aspects of capital planning and management, what are some of the modern technologies that bring rigor to the process?

- **Financial Technological Tools**
  - Programs to determine optimal use for funding, capitalization, asset activity

- **Technical Tools**
  - Programs to measure pavement condition, digitize images onto mapping database and for valuation purposes
Question 12

What are the guidelines in using technology in capital planning and management?
12. What are the guidelines in using technology in capital planning and management?

- Systems available in the market
- Alignment with the organization’s IT strategic plan
- Stakeholder expectations
- Cost and benefits
- Users of the system
- Scope of the system
- Process for collecting, verifying and transferring data
- Communication of information
- Ongoing support for the system
In your opinion, what is the most challenging consideration in using technology in capital planning and management?
13. In your opinion, what is the most challenging consideration in using technology in capital planning and management?

- Accurate and reliable data
- Coordination of purchases in a decentralized organization
How should local governments pay for the cost of managing a capital program? Do the personnel costs of the managers need to be part of the public works department in the operating budget, or can capital program management costs be charged to the projects themselves?
14. How should local governments pay for the cost of managing a capital program?

- Include personnel costs in operating budget departments

  or

- Use internal service fund approach to budget for personnel costs then charge to project funds
Who is best situated to identify the operating costs of a capital project, if any? It seems like it would be easy to overlook the operating impact of some capital projects. Who is in charge of making sure those impacts are identified and considered in the operating budget?
15. Who is best situated to identify the operating costs of a capital project, and make sure those impacts are considered in the operating budget?

- Joint responsibility

- Types of operating impacts
  - Increased revenues
  - Increased expenditures
  - Savings
Question 16

Why do some local governments have so much difficulty implementing the projects approved in a bond election? How can governments ensure that they follow through timely and accomplish what they said they would do?
16. How can governments ensure that they follow through timely and accomplish what they said they would do?

- Capital projects prone to problems

- Ways to improve execution of capital program
  - Have capital policies and practices in place
  - Establish accountability and sense of urgency
  - Provide regular reporting to staff, Council, public
  - Review/improve processes from design to procurement to management to inspection and close-out
  - Have the right quantity and quality of project managers
What are some commons problems or pitfalls in building and implementing a CIP? What can be done to prevent or minimize project cost overruns and change orders?
17. What are the solutions to common CIP problems?

<table>
<thead>
<tr>
<th>Building the CIP</th>
<th>Potential Solutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Problems</td>
<td></td>
</tr>
<tr>
<td>Omitting important projects</td>
<td>Include all appropriate parties in planning</td>
</tr>
<tr>
<td>Underestimating costs</td>
<td>Be realistic-use professional sources-build in contingency</td>
</tr>
</tbody>
</table>
17. What are the solutions to common CIP problems?

<table>
<thead>
<tr>
<th>Implementing the CIP</th>
<th>Potential Solutions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Problems</strong></td>
<td><strong>Potential Solutions</strong></td>
</tr>
<tr>
<td>Delays from ROW acquisition, neighborhood opposition</td>
<td>Keep pressure on, shift efforts to other projects while process continues</td>
</tr>
<tr>
<td>Bureaucratic malaise</td>
<td>Re-engineer processes, align authority and responsibility</td>
</tr>
<tr>
<td>Cost overruns</td>
<td>Invest time and effort in design stage, inspect closely</td>
</tr>
</tbody>
</table>
What is the best way to make sure a project is completely closed out, both physically and financially?
18. What is the best way to make sure a project is completely closed out, both physically and financially?

Importance of having established procedures for review and closure of projects:

- More meaningful capital projects reports
- Reprogramming of unspent balances
- Financial accountability to stakeholders, e.g., project partners, bondholders
How should I present capital assets and capital budgeting as they relate to the fiscal health and service performance as a whole of my local government? Does this vary for different services within the entity?
19. How should I present capital assets and capital budgeting as they relate to the fiscal health and service performance as a whole of my local government? Does this vary for different services within the entity?

- Capital and Borrowing Costs
- Life Operating Costs
- Other Options – Often Need to Involve Those Arm’s Length from the Process
- Risk Needs to be Considered
- Use the PESTLE model: Political, Economic, Social, Technical, Legal, and Environmental
19. How should I present capital assets and capital budgeting as they relate to the fiscal health and service performance as a whole of my local government? Does this vary for different services within the entity?

<table>
<thead>
<tr>
<th>Risk Matrix</th>
<th>Consequences</th>
<th>Insignificant</th>
<th>Minor</th>
<th>Moderate</th>
<th>Major</th>
<th>Catastrophic</th>
</tr>
</thead>
<tbody>
<tr>
<td>Likelihood</td>
<td></td>
<td>High (15)</td>
<td>High (10)</td>
<td>Extreme (6)</td>
<td>Extreme (3)</td>
<td>Extreme (1)</td>
</tr>
<tr>
<td>Almost</td>
<td>Certain</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Likely</td>
<td>Moderate (19)</td>
<td>High (14)</td>
<td>High (9)</td>
<td>Extreme (5)</td>
<td>Extreme (2)</td>
<td></td>
</tr>
<tr>
<td>Possible</td>
<td>Low (22)</td>
<td>Moderate (18)</td>
<td>High (13)</td>
<td>High (8)</td>
<td>Extreme (4)</td>
<td></td>
</tr>
<tr>
<td>Unlikely</td>
<td>Low (24)</td>
<td>Low (21)</td>
<td>Moderate (17)</td>
<td>High (12)</td>
<td>Extreme (7)</td>
<td></td>
</tr>
<tr>
<td>Rare</td>
<td>Low (25)</td>
<td>Low (23)</td>
<td>Moderate (20)</td>
<td>High (16)</td>
<td>High (11)</td>
<td></td>
</tr>
</tbody>
</table>
How does the public sector entity best communicate the strategies to improve its capital position and investment? How does the communication differ for internal and external stakeholders?
20. How does the public sector entity best communicate the strategies to improve its capital position and investment? How does the communication differ for internal and external stakeholders?

- Transparency—budget, long term financial forecast, asset management plans, financial ratios

- Influencing strategies
How does a public sector entity best establish a reporting framework for management, monitoring, or reporting on its capital projects? Are there different levels of reporting for sectors within the organization?
21. How does a public sector entity best establish a reporting framework for management, monitoring, or reporting on its capital projects? Are there different levels of reporting for sectors within the organization?

- Different reporting needs for Council, project managers
- Goal of all reports: ensure reader has enough information to know project is being managed, monitored, and on track
- Commitments (purchase orders) vs. expenditures
What are some of the benchmark metrics that can be used to measure the improvement of asset management and capital investment from both a financial management and strategic management perspective?
22. What are some of the benchmark metrics that can be used to measure the improvement of asset management and capital investment from both a financial management and strategic management perspective?

➢ Financial measures—Queensland examples:

- **Operating Result**
  - 2015: $194m
  - 2016: $271m
  - 2017: $613m (+126%)

- **Net Assets**
  - 2015: $100,543b
  - 2016: $103,322b
  - 2017: $106,323b (+3%)

- **Total Revenue**
  - 2015: $11,516b
  - 2016: $11,586b
  - 2017: $12,300b (+6%)

- **Total Assets**
  - 2015: $108,796b
  - 2016: $111,068b
  - 2017: $114,485b (+3%)

- **Total Expenses**
  - 2015: $9,905b
  - 2016: $9,726b
  - 2017: $9,918b (+2%)

- **Total Liabilities**
  - 2015: $8,254b
  - 2016: $7,746b
  - 2017: $8,162b (+5%)

Source: Queensland Audit Office.
22. What are some of the benchmark metrics that can be used to measure the improvement of asset management and capital investment from both a financial management and strategic management perspective?

- Financial measures—Queensland examples:
  - Operating surplus ratio %
  - Net financial liabilities ratio %
  - Asset sustainability ratio %
  - Relative risk assessment
22. What are some of the benchmark metrics that can be used to measure the improvement of asset management and capital investment from both a financial management and strategic management perspective?

- Strategic measures—Queensland example: National Asset Management Assessment Framework (2009)
Should I consider anything else in monitoring and reporting on capital projects?
23. Describe the process chain for monitoring and reporting on the capital projects once they are approved?

- Monitoring and reporting needs to be two fold:
  1. Progress of the work
  2. Money Spent

If the focus is just on the spend, this can lead to a situation where 100% is spent and 80% of the work is completed. Manage contingency and you manage the project!!
How can a local government’s website help communicate information about its CIP?
24. How can a local government’s website help communicate information about its CIP?

- Integrate website with project management and financial software
- Use GIS to display project locations
- Provide individual project detail—schedule, budget, activity to date, contact information
24. How can a local government’s website help communicate information about its CIP?
24. How can a local government’s website help communicate information about its CIP?
24. How can a local government’s website help communicate information about its CIP?

STREET AND TRANSPORTATION $533.98M

The proposition includes Traffic Signals, Alley Reconstruction, Bridge Repair, Railroad Crossing Quiet Zones, Sidewalks, Street Reconstruction, and Street Resurfacing Projects.

$62.63M
Current Amount Committed

PROJECTS

1,037 Total Projects
360 Projects Started
141 Projects Completed

10003-10119 Shayna Dr & 10002-10106 Hymie Cir
10106-10140 Caribou Trail & 10127-10140 Ferndale Rd
10143-10199 Victorville Dr & 10200-10200 Trailside #1 Dr
24. How can a local government’s website help communicate information about its CIP?

![PROJECT TIMELINE]

**Project Details**
- **Bond Program Year**: 2017
- **Project Status**: Under Award - Construction
- **Date Created**: 03/15/2018
- **Category**: Street Resurfacing
- **Last Modified Date**: 04/26/2019
- **Council District**: 12
- **Department**: PBW
- **Project ID**: PB17V572

**PROJECT FUNDING**
- **Bond Project Total**: $232,500
- **Current Budget**: $232,500
- **Committed**

**Project Schedule**
- **Estimated Design Start**: TBD
- **Estimated Design Completion**: TBD
- **Estimated Construction Start**: 03/19/2019
- **Estimated Construction Completion**: 09/30/2019
Questions?
Thank you!