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## FISCAL IMPACT REPORT

SPONSOR Sandoval DATE TYPED 3/2/03 HB 1074

SHORT TITLE Value of State Property to Be Inventoried SB \_\_\_\_\_

ANALYST Geisler

### APPROPRIATION

Appropriation Contained		Estimated Additional Impact		Recurring or Non-Rec	Fund Affected
FY05	FY06	FY05	FY06		
			Indeterminate		

(Parenthesis ( ) Indicate Expenditure Decreases)

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Department of Finance and Administration (DFA)

State Auditor (SA)

General Services Department (GSD)

Energy, Minerals, and Natural Resources (EMNRD)

### SUMMARY

#### Synopsis of Bill

House Bill 1074 amends the state audit act Section 12-6-10 pertaining to the inventory of owned equipment. Under HB 1074, all state and local agencies that have an annual audit (as required by statute) would only be required to perform an annual inventory of equipment costing more than five thousand dollars (\$5,000), rather than one thousand dollars (\$1,000), which is the current statutory requirement.

#### Significant Issues

Title 1, Chapter 1, Part 2, SUB-Part 1 of the New Mexico administrative code requires all agencies to perform an annual physical inventory of all fixed assets. Fixed assets are defined as any property or equipment that has an initial value to an agency, whether in cash or trade value, of more than one thousand dollars (\$1,000). Fixed assets must be tagged, the physical location recorded, and the asset assigned to the fund and government entity that purchased the asset. If an

asset is transferred, the accounting records need to be updated if the relocation affects a different fund.

Advantages of Increasing Inventory Threshold from \$1,000 to \$5,000

By changing the definition of a fixed asset from property or equipment exceeding one thousand dollars (\$1,000) in value to property or equipment exceeding five thousand dollars (\$5,000) in value, the number of items requiring inventory will be reduced and the process of recording, monitoring, and performing a physical inventory on fixed assets will be greatly simplified. At the lower threshold of one thousand dollars (\$1,000), many assets that may be well past their useful lives and no longer in use will still have to be monitored and inventoried if they are not disposed of. At the higher threshold of five thousand dollars (\$5,000), assets will typically have a longer useful life.

Many local governments have struggled to maintain fixed asset inventories, and as a result of inadequate records have received “qualified” opinions on their financial statement audits. Raising the threshold will likely ease the task of maintaining adequate fixed asset inventories.

Disadvantages of Increasing Inventory Threshold from \$1,000 to \$5,000

Unless an agency maintains a separate inventory of items of value less than \$5,000, GSD notes that accountability for asset management will be decreased and their could be increased exposure for asset loss or abuse. ENNRD notes that a lack of control over assets that are valued under \$5,000 (like many computers) may make it difficult to identify out dated equipment that needs to be replaced and accountability of equipment that is replaced. The State Auditor notes that over time it might make sense to increase the threshold due to inflation, but questions the need to increase the limit by such as a large amount (\$4,000) at this time.

**FISCAL IMPLICATIONS**

Indeterminate. The reduced administrative burden will save agencies staff time but if assets are managed inefficiently it will cost the state in the long run. House Bill 1074 raises the state threshold for capitalizing fixed assets to match federal rules. Agencies will no longer have to reduce charges to federal programs for purchases of equipment with an initial cost of five thousand dollars (\$5,000) or below. This should increase the recovery of federal dollars for agencies that administer federal programs.

**ADMINISTRATIVE IMPLICATIONS**

The administrative burden of conducting yearly inventories for all equipment with an initial value of greater than one thousand dollars (\$1,000) will be greatly reduced as the requirement for physical inventory is changed by House Bill 1074 to assets with a cost basis of above five thousand dollars (\$5,000).

## **OTHER SUBSTANTIVE ISSUES**

### Asset Depreciation and Proprietary Fund Operations

DFA notes that assets purchased from proprietary funds are required to be depreciated. Proprietary funds provide services to other government entities or the public and recover full costs including depreciation through user charges. For example, the General Services Department (GSD) provides numerous services to state agencies. Depreciation is incorporated into agency assessments for information systems processing, printing services, telephone and data communication, and vehicle lease rates. House Bill 1074 will change the rate structures for these internal services by requiring GSD to expense all equipment purchases of five thousand dollars (\$5,000) or below, rather than including depreciation costs over the useful life of the asset. This may cause rates to fluctuate more from one year to the next since the cost based rates will now include more expenses and less depreciation for certain classes of equipment purchases. Charging depreciation over the useful life of an asset tends to "smooth out" the rates, rather than incorporating the full cost of the asset in the rate calculations in the year the asset is purchased.

The federal government limits capital purchases charged to federal programs to the lesser of the current state rule (over \$1,000) or the federal rule (over \$5,000). Therefore, all state purchases of equipment of five thousand dollars (\$5,000) or less cannot be charged to federal programs unless otherwise approved. House Bill 1074 will allow conformity with current federal capitalization rules and allow the state to charge more small capital purchases to federal programs, that would otherwise have to be depreciated over the useful life of the asset.

### **WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL?**

If House Bill 1074 is not enacted, the state will not be able to charge the cost of small equipment purchases between one thousand dollars (\$1,000) and five thousand dollars (\$5,000) directly to federal programs.

State agencies will continue to be required to perform yearly physical inventories of all equipment with an initial value of more than one thousand dollars. (\$1,000).

GGG/yr