

### 3.

## ACCOUNTING

### 3.3 Capital Assets

#### 3.3.4 Capital Asset System Accounting

3.3.4.10 Once the capital asset system is in operation, the government needs to make sure that assets which should be capitalized are properly recorded and that records are brought up to date when assets are disposed. Use of a standard form assures that the information needed for recording capital asset transactions is promptly collected and processed. A sample form for this purpose is contained in [Individual Capital Assets Records](#). In addition, periodic physical inventories must be taken to verify the existence and condition of the assets. These inventories must be reconciled to capital asset records and reports (see [Physical Inventory](#)).

#### TRANSACTIONS TO RECORD

3.3.4.20 Each time the local government acquires or disposes of a capital asset, transfers an asset between locations, charges depreciation expense or makes an adjustment, an entry must be made on the individual capital asset record. Internal controls must be established to insure that these transactions are properly and promptly recorded. If capital asset disposals or transfers are numerous, a capital asset journal should be used to record and control these changes. It is a good idea to always write detailed explanations of these entries, especially for disposals of assets, because it is difficult to reconstruct the circumstances of a transaction at a later date. If a capital asset journal is used, the general ledger and subsidiary capital asset accounts should be posted from this journal.

1. Capitalization policy defines what assets should be added to the system by specifying dollar limits; that policy should also specify the treatment of capital leases, procedures for accumulating costs for self-constructed assets, requirements for controlling small attractive assets that are not capitalized and accounting for infrastructure. Personnel should be thoroughly familiar with and trained to recognize and code capital outlays properly and to understand the government's capitalization policy.
2. For additions, procedures must be implemented to assure that the property systems accountant automatically receives a copy of the receiving report or the invoice. He/she should also receive a copy of all lease agreements, progress billings on construction contracts, and worksheets that itemize the costs of assets constructed in-house.
3. For deletions, procedures must be implemented to assure that the property systems accountant automatically receives all resolutions/ordinances that declare property surplus, all property insurance claims, and itemized invoices for acquisitions that involve trade-ins. Oversights are difficult to avoid entirely, but they will be detected and corrected when physical inventories are taken.
4. For small attractive assets that are not capitalized, a policies and procedures manual should contain instructions for adding and deleting these assets from the control lists used to monitor them.
5. Procedures must be established to account for transfers whenever an asset changes location, custody or fund. These procedures should list the steps for preparing and approving of transfer documents and notifying the accountant responsible for maintaining the capital asset records.

6. The property accountant must perform several different reconciliations and analyses:
  - a. Reconcile physical inventory to individual capital asset records (see [Physical Inventory](#));
  - b. Reconcile individual capital asset records to general ledger asset accounts;
  - c. Reconcile capital outlay expenditures (594) to total additions of capital assets;
  - d. Analyze subobject detail for additions to lists of not capitalized small attractive assets;
  - e. Reconcile significant capital grants shown on the grant inventory with increases to the capital asset accounts.
  - f. Analyze proceeds from insurance claims and sales or auction lists, claims reports, etc., to total capital asset disposals;
  - g. Reconcile capital assets transferred to other locations, custody or funds with capital assets transferred from other locations, custody or funds.

### COST

3.3.4.30 *Original cost* (historical cost) is the amount spent to acquire an asset. This cost is based on the actual price paid, including related taxes, commissions, installation costs and any other costs related to acquiring the asset or preparing the asset for use. The actual price should approximate fair market value. If the information regarding original cost is not available, the government needs to estimate the original cost. This cost principle applies to both governmental and proprietary capital asset acquisitions.

3.3.4.40 Several unique circumstances arise when determining cost, particularly in utility accounting. The following are the more frequent accounting problems related to *cost*, but the discussion is not meant to be all-inclusive.

### Excess Costs

3.3.4.50 A basic accounting concept is that capital assets should be recorded at cost. However, GAAP does provide that expenditures/expenses, which do not add to the utility of an asset, should not be capitalized. For example, expenditure to repair a piece of equipment that was damaged during shipment should be expensed. Each capital asset purchase should be analyzed carefully to determine which portions of the cost should be capitalized.

3.3.4.60 Similar treatment is mandated by certain regulatory agencies. For example, FERC provides that any amounts incurred for plant additions that are in excess of just and reasonable charges should be included in the account *Other Deductions*. Likewise, if excess costs are incurred to replace individual units of property damaged in a storm so as to restore the utility system to operating condition without delay, then only the normal or fair cost is charged to plant, the balance to maintenance.

### Acquisition Adjustments

- 3.3.4.70 *Original cost* in the FERC and NARUC accounting systems means the cost of such property to the person first devoting it to public service. When a system or plant already in operation is purchased by a utility, the NARUC and FERC accounting systems require charging the difference between the cost to the acquiring utility and the *original cost* (estimated if not known and net of accumulated depreciation) to an intangible asset account *Plant Acquisition Adjustments*. Such debits would then be amortized over a period not to exceed the remaining life of the property.

### Capitalization of Interest

- 3.3.4.80 No interest should be capitalized in internal service funds that are incorporated within governmental activities.

### Donated Assets

- 3.3.4.90 Assets are sometimes donated to a government. If the donation is cash to be used in conjunction with the construction of a specific asset, the donation is reported as revenue (367, *Contribution and Donations from Nongovernmental Sources*) in governmental funds; in proprietary funds, 374/379, *Capital Contributions*. If the government receives a capital asset and intends to use it in operations, the receipt of the asset would not be reflected at all in governmental fund financial statements, although it would be reflected in the governmental activities column of the government-wide financial statements. (The capital asset donated to a proprietary fund should be recognized as a capital contribution.)
- 3.3.4.100 Contributed capital assets should be reported at the acquisition value. Acquisition value is the price that would be paid to acquire an asset with equivalent service potential in an orderly market transaction at the acquisition date, or the amount at which a liability could be liquidated with the counterparty at the acquisition date. ([GASB Statement 72, Fair Value Measurement and Application](#))
- 3.3.4.110 If the government intends to sell the donated general capital assets, the following treatment is recommended:
- If the government has sold the capital assets by the end of the fiscal year, the governmental fund would report revenue in the operating statement (3699000, *Other*).
  - If the government has not sold the capital assets by the end of the fiscal year in which it was received, but it did succeed in selling during the availability period for revenue recognition early the following year, the government's fund balance sheet should report the capital assets as assets held for resale (G.L. account 193.70) and revenue would be reported in the governmental fund's operating statement (3699000, *Other*). Conversely, if the sale takes place the following year, but after close of the availability period, the donated capital assets would be reported only on the balance sheet as assets held for resale (G.L. account 193.70) and unearned revenue (G.L. account 257).
  - If the government was unable to sell the capital assets by the time the financial statements were issued, no asset or liability should be reported in governmental funds for donated capital assets for which there is no sale contract as of the date financial statements are issued. Instead, a receivable and revenue/unearned revenue would be recognized in the appropriate governmental fund only at the time the government finally entered into a sale contract.

3.3.4.120 In all above situation the donated assets would be reported on the government-wide statement of net position (capital asset held for resale) and the statement of activities (revenue).

Improvement/Repair/Maintenance Expenditures/Expenses

3.3.4.130 Routine repair and maintenance costs should be expensed as they are incurred. Major repairs should be capitalized if they result in betterments/improvements. The difficulty arises in the case of capital outlays that are partly replacements and partly betterments/improvements. To the extent that the project replaces the *old* part of a capital asset, outlays should not be capitalized (unless cost of the *old* part was removed from the cost of the asset); and to the extent that the project is betterment/improvement, outlays should be capitalized. The distribution of the total cost in such a case is a matter of managerial determination. When the distinction between replacement and betterment/improvement is not easily determinable, the government should expense the entire cost of the project.

3.3.4.140 When the cost of improvement is substantial or where there is a change in the estimated useful life of an asset, depreciation charges for future periods should be revised based on the new book value and the new estimated remaining useful life. No adjustment should be made to prior periods.

JOURNAL ENTRIES

3.3.4.150 The following journal entries are examples of how various types of capital asset transactions are recorded.

NOTE: Although the [GASB Statement 34](#) eliminated the general capital assets and the general long-term debt account groups, the local governments may still use the groups and related accounts for accounting purposes.

The entries are shown for both governmental and proprietary funds.

Funds	Governmental Funds Capital Asset Acquisition/Disposition		Proprietary Funds Capital Asset Acquisition/Disposition			
		DR	CR		DR	CR
Example No. 1: Record the cash purchase of a copy machine for \$15,000. The cost included taxes and set-up fees.						
<u>Purchasing Fund</u>	594PP60 Capital Outlay 111.10 Cash	15,000	15,000	186.XX Equipment 111.10 Cash	15,000	15,000
Add to capital assets inventory:	Equipment: copier \$15,000			Equipment: copier \$15,000		
<u>Worksheet adjustment for presentation in government-wide statements</u>	Equipment Expenditures – Capital Outlay	15,000	15,000	N/A		
Example No. 2: Record the purchase of a computer on a 5-year installment purchase contract or lease-purchase agreement. The cost included taxes. Set-up fees of \$200 were paid separately.						
<u>Purchasing Fund</u>	594PP60 Capital Outlay 594PP41 Capital Outlay 111.10 Cash 3915000 Proceeds from Capital Lease Installment Loan	25,000 200	5,200 20,000	186.XX Equipment 111.10 Cash 235.50 Current Leases and Installment Purchases Payable 263.50 Other Long-Term Liabilities – Leases and Installment Purchases	25,200	5,200 5,000 15,000
Add to capital assets inventory:	Equipment: computer \$25,200			Equipment: computer \$25,200		
Add to subsidiary ledger of long-term debt:	Capital Lease: \$20,000					
<u>Worksheet adjustment for presentation in government-wide statements</u>	Equipment Expenditures – Capital Outlay	25,200	25,200	N/A		

Funds	Governmental Funds Capital Asset Acquisition/Disposition			Proprietary Funds Capital Asset Acquisition/Disposition		
		DR	CR		DR	CR
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Proceeds from Capital Lease Installment Loan Leases and Installment Purchases Payable	20,000	20,000	N/A		
Example No. 3: Record the donation of a 10-acre tract of land with a fair market value of \$100,000. Land will be kept.*						
<u>Receiving Fund</u>	N/A			171.XX Land 3790000 Capital Contributions	100,000	100,000
Add to capital assets inventory:	Land \$100,000			Land \$100,000		
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Land Non-cash Donation	100,000	100,000	N/A		

\* This entry for governmental funds may vary depending on the government plan for those assets.

Funds	Governmental Funds Capital Asset Acquisition/Disposition			Proprietary Funds Capital Asset Acquisition/Disposition		
		DR	CR		DR	CR
Example No. 4: Record the purchase of a copy machine for \$15,000 cash less a trade-in allowance of \$1,500. The old machine cost \$5,000 with accumulated depreciation of \$4,000. Taxes and set-up costs are included.						
<u>Purchasing Fund</u>	594PP64 Capital Outlay 111.10 Cash 3951000 Proceeds from Trade-In of Capital Assets	15,000	13,500  1,500	186.9X Accumulated Depreciation 186.XX Equipment (new) 186.XX Equipment (old) 111.10 Cash	4,000 14,500	5,000 13,500
				(Note: This example follows the APB Opinion 29, <i>Accounting for Nonmonetary Transaction</i> . See Examples 6, 8 and 9 for recording a gain or loss.)		
Add to capital assets inventory:	Equipment: new copier \$15,000					
Remove from capital assets inventory:	Equipment: old copier \$5,000 Accumulated Depreciation \$4,000					
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Equipment (new) Accumulated Depreciation (old) Proceeds from Trade-In Equipment (old) Expenditures – Capital Outlay Gain on Disposal of Capital Assets  Note: The new capital asset should be recorded at what would have been its price without a trade-in (\$15,000).	15,000 4,000 1,500	5,000 15,000 500	N/A		

Funds	Governmental Funds Capital Asset Acquisition/Disposition		Proprietary Funds Capital Asset Acquisition/Disposition			
		DR	CR		DR	CR
Example No. 5: Record the purchase of a computer financed 90% with federal funding (HUD) and 10% local funding. The asset cost is \$20,000, including tax and set up costs.						
<u>Purchasing Fund</u>	594PP60 Capital Outlay 111.10 Cash	20,000		134.XX Due from Other Government 186.XX Equipment	18,000 20,000	
	111.10 Cash 3311420 Direct Federal Grants – HUD	18,000		3741420 Capital Contributions – Federal 111.10 Cash		18,000 20,000
			18,000			
Add to capital assets inventory:	Equipment: computer \$20,000			Equipment: computer \$20,000		
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Equipment Expenditures – Capital Outlay Expenditures – Capital Outlay	20,000		N/A		
			18,000			
			2,000			

Funds	Governmental Funds Capital Asset Acquisition/Disposition		Proprietary Funds Capital Asset Acquisition/Disposition			
		DR	CR		DR	CR
Example No. 6: Record the cost (\$50,000) of re-roofing the department. The original cost of roof components was \$15,000 (if proprietary fund accumulated depreciation of \$14,000). The project was financed from resources from the special revenue fund.						
<u>Purchasing Fund</u>	5942240 Capital Outlay 111.10 Cash	50,000	50,000	173.XX Buildings 173.9X Accumulated Depreciation 3730000 Gain (Loss) on Disposition of Capital Assets 173.XX Buildings 111.10 Cash	50,000 14,000 1,000	15,000 50,000
Add to capital assets inventory:	Buildings: new roof \$50,000					
Remove from capital assets inventory:	Buildings: old roof (\$15,000) Accumulated Depreciation (\$14,000)			Same		
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Buildings (new) Accumulated Depreciation (old) Loss (old) Buildings (old) Expenditures – Capital Outlay	50,000 14,000 1,000		N/A		15,000 50,000

Funds	Governmental Funds Capital Asset Acquisition/Disposition			Proprietary Funds Capital Asset Acquisition/Disposition		
		DR	CR		DR	CR
<p>Example No. 7: Record the construction of a new jail costing \$18,000,000. 80% of the project is funded by the Washington State Jail Commission and the remaining 20% were raised through the issuance of G.O. Bonds. The jail is 50% complete at year-end.</p>						
<u>Purchasing Fund</u>	(Capital Projects Fund) 134.XX Due from Other Governments 3340160 State Grant – Jail 111.10 Cash 3911000 Other Financing Sources - G.O. Bond Proceeds 5942360 Capital Outlay 111.10 Cash	7,200,000  3,600,000  9,000,000	 7,200,000  3,600,000 9,000,000	134.XX Due from Other Governments 3740160 Capital Contributions – State 111.10 Cash 251.12 G.O. Bonds Payable 189.XX Construction in Progress 111.10 Cash  Note: When the project is complete, a final entry is required: 173.XX Buildings 189.XX Construction in Progress	7,200,000  3,600,000  9,000,000  18,000,00	 7,200,000  3,600,000 9,000,000  18,000,00
Add to capital assets inventory:	Construction in Progress \$9,000,000			Construction in Progress \$9,000,000		
Add to subsidiary ledger of long-term debt:	G.O. Bond Payable \$3,600,000					
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Capital Assets – Construction in Progress Capital Outlay  Other Financing Sources – Bond Proceeds G.O. Bonds Payable	9,000,000  3,600,000	 9,000,000  3,600,000	N/A		

Funds	Governmental Funds Capital Asset Acquisition/Disposition		Proprietary Funds Capital Asset Acquisition/Disposition			
		DR	CR		DR	CR
	Note: When the project is complete, a final entry is required:			N/A		
	Buildings Construction in Progress	18,000,00	18,000,00			
Example No. 8: Record the sale of word processing equipment costing \$8,500 (if proprietary fund accumulated depreciation of \$6,000). The asset was sold for \$900.						
<u>Selling Fund</u>	111.10 Cash 3951000 Other Financing Sources – Proceeds from Sales of Capital Assets	900	900	111.10 Cash 3954000 Loss on Sale of Capital Assets 186.9X Accumulated Depreciation 186.XX Equipment	900 1,600 6,000	8,500
Remove from capital assets inventory:	Equipment (\$8,500) Accumulated Depreciation \$6,000			Equipment (\$8,500) Accumulated Depreciation \$6,000		
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Other Financing Sources – Proceeds from Sales of Capital Assets Loss on Sale of Capital Assets Accumulated Depreciation Equipment	900 1,600 6,000	8,500	N/A		

Funds	Governmental Funds Capital Asset Acquisition/Disposition		Proprietary Funds Capital Asset Acquisition/Disposition			
		DR	CR		DR	CR
Example No. 9: Record the write-off of a building, which was destroyed by fire. The building cost \$200,000 (if proprietary fund, accumulated depreciation was \$183,000). Insurance proceeds of \$180,000 were received.						
<u>Disposing Fund</u>	111.10 Cash 3952000 Other Financing Sources – Insurance Recoveries	180,000	180,000	111.10 Cash 173.9X Accumulated Depreciation  173.XX Buildings and Structures 3952000 Insurance Recoveries	180,000 183,000	200,000 163,000
Remove from capital assets inventory:	Building: (\$200,000) Accumulated Depreciation \$183,000			Same		
<u>Worksheet adjustment for presentation in the government-wide statements</u>	Other Financing Sources – Insurance Recoveries Accumulated Depreciation Buildings	17,000 183,000	200,000	N/A		

Funds	Governmental Funds Capital Asset Acquisition/Disposition		Proprietary Funds Capital Asset Acquisition/Disposition			
		DR	CR		DR	CR
Example No. 10: Record the transfer of a truck from the governmental fund to an Equipment Rental Fund. The truck cost \$10,000 and is two years old with an estimated life of five years. The truck was purchased on a three-year lease-purchase with \$4,800 in principal payments remaining.						
<u>Receiving Fund</u>	N/A			186.XX Equipment 3790000 Capital Contribution 235.50 Current Leases and Installment Purchases Payable 3790000 Capital Contribution	6,000 4,800	4,800 6,000
Transfer in capital assets inventory:  Remove from subsidiary ledger of long-term debt:	Accumulated Depreciation: truck \$4,000 Capital Assets: truck (\$10,000)  Capital Lease \$4,800			Capital Assets: truck \$6,000		
<u>Worksheet adjustment for presentation in the government-wide statements</u>	N/A – assuming that the internal service fund is reported under governmental activities			N/A		