State Accounting Office of Georgia
Fiscal Leadership for Georgia

Statewide Accounting Policy & Procedure

Accounting Manual Reference:	**Effective Date:** 07/01/2011
Section: Capital Assets	**Revision Date:** 06/30/2011
Sub-section: Construction in Progress	

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Policy Summary:
This policy provides guidance to all organizations included in the State of Georgia reporting entity for recording and reporting construction projects using the Construction in Progress (CIP) asset class as prescribed by Government Accounting Standards Board (GASB) Statement Nos. 34 and 54. The policy focuses on the accounting treatment of Capital Construction Projects (CCP) with respect to fund type, funding source, and managing organization. The policy also applies to intangible asset projects that qualify as CIP activities. Refer to the policy titled *Internally Generated Computer Software* for special rules on the capitalization criteria for internally generated intangible assets.

It is important to note that constructed assets require a reasonable system for identifying, capturing, and tracking cost. Each reporting organization with CIP activity is responsible for implementing an appropriate tracking process for accurately accounting for that activity.

Policy Requirements:
Management of each organization bears the responsibility for ensuring that proper accounting procedures are employed and for establishing effective internal controls to ensure compliance with this policy.

Accounting Requirements
Many capital projects extend over more than one financial reporting period and are still in progress at the end of the fiscal year. In such circumstances the recording and reporting of the construction in progress asset will depend on the fund incurring the costs.

Organizations managing Capital Construction Projects are responsible for recording the expenses/ expenditures and if applicable the asset, whether or not the asset will ultimately belong to them.

Governmental funds, including capital projects funds, record construction costs as expenditures at the fund level and capitalize projects that are incomplete at year-end under the CIP asset class in the governmental activities column of the government-wide statement of net assets.

Governmental fund entities with CCP funded with general obligation bond proceeds ***must report*** them in a capital project fund. SAO recommends that general obligation bond funded projects also be ***recorded*** in a capital project fund. Exceptions to this recommendation for ***recording*** CCP activity must be approved by SAO. Requests for approval should be submitted via email to SAO_Reporting@sao.ga.gov and must include business reasons for the exception. Non-general obligation bond funded projects are not required to be reported in a capital project fund but may be reported in such a fund if preferred.

Proprietary and fiduciary fund outlays for CCP are capitalized within the fund and are also reported in the government-wide statement of net assets. Proprietary and fiduciary funds operate on the accrual basis of accounting; therefore, construction project costs are accumulated in the CIP account until the project is completed.

Only those expenditures and ancillary costs that are directly attributable to the construction phase and that are necessary to place the asset into its intended location and use should be capitalized. Refer to the *Capital Assets – General* policy for comprehensive guidance on capitalizable costs. For assets constructed by outside contractors, the costs are based on contractual agreements and vendor invoices. However, if assets are constructed or substantially enhanced by labor supplied by governmental employees, a reasonable system for identifying and capturing costs, including direct internal labor, must be used. Costs to be captured include the cost of materials and labor, including the cost of attached fixtures; professional fees; construction insurance premiums; and related costs incurred during the construction period to place the constructed asset in service. All related construction expenditures will continue to accumulate in the construction in progress account until the asset is placed in service. Upon placement into service, the asset must be transferred to the proper capital asset classification account.

In the specific case of a building being constructed, furniture and/or equipment bought during the construction phase to furnish the building and used before the building is placed in service can be recorded directly in the equipment and furniture asset category. However if furniture and/or equipment are not used until the building is completed and placed in service, organizations have the option to record them as construction in progress. At the end of the project the construction in progress account should be zeroed out and two asset categories recognized: building and equipment/furniture.

Recognition and Measurement

Construction outlays reported in capital projects funds are recorded as capital expenditures because capital projects funds are governmental funds and therefore use the flow of current financial resources measurement focus and statutory or modified accrual basis of accounting. The construction in progress account is a capital asset account and therefore is not reported at the governmental fund level but only on the governmental activities column of the government-wide statements of net assets.

Capital assets constructed by proprietary or fiduciary funds should be recorded as capital assets in the individual funds making the acquisitions. Within these funds capital assets directly affect the statement of net assets. An expense is not recorded because, under the flow of economic resources measurement focus and the accrual basis of accounting, the funds are not economically affected when liquid assets (e.g., cash) are exchanged for capital assets.

The expected amount to be capitalized must meet established capitalization thresholds if CIP activity relates to a newly constructed asset or substantially extends the useful life of an existing capital asset. At the end of the project, the newly constructed asset is removed from the CIP asset classification and transferred to the appropriate asset account (building, infrastructure, etc.). Depreciation begins once the resulting asset is transferred into a permanent capital asset classification account and placed in service.

Basis of Accounting

Funds that operate on a statutory basis must convert their accounting activity to the modified accrual and/or accrual bases of accounting for the Comprehensive Annual Financial Report (CAFR). Proprietary and fiduciary funds that do not operate on a statutory basis use the accrual basis of accounting throughout the year.

- Statutory Basis for Budgetary Compliance Reporting
  Construction in progress outlays are recorded as expenditures on a statutory basis of accounting at the earlier of either the time the funds are encumbered (i.e., when purchase orders or other contractual obligations to procure goods or services have been executed) or the time the goods, services, rights, etc. have been received. Accruals are required at year-end for unencumbered goods and services received but not recorded. Also, a reclassification from encumbrance liability to accounts payable is required for any encumbered purchases that are received by year-end but not yet classified as accounts payable.

- Converting to Modified Accrual Basis for CAFR Reporting
  Any ending encumbrance liability balance related to CIP is eliminated under the modified accrual basis of accounting, and beginning fund balance is increased by the prior year encumbrance liability balance related to CIP. The offsetting change in the encumbrance liability is recorded as an expenditure to recognize the current year impact on expenditures for CIP activity. A decrease in the encumbrance liability results in an increase to expenditures, and an increase in the encumbrance liability results in a decrease to expenditures.

- Converting to Accrual Basis for CAFR Reporting
  Governmental fund activity must be adjusted to the full accrual basis of accounting for year-end government-wide reporting purposes. Construction in progress outlays that were reported as expenditures in the governmental funds under modified accrual basis of accounting must be capitalized if outlays exceed the capitalization threshold.

- Accrual Basis for Funds Not Reporting on a Statutory Basis
  Proprietary funds, fiduciary funds and component units which are maintained on the accrual basis of accounting must also recognize and report construction outlays in the construction in progress asset class until the project is completed.

Disclosure Requirements
GAAP requires the State to disclose, in the notes to the financial statements, the changes in the construction in progress asset class during the reporting period. This requirement includes disclosure of the beginning and ending balances of the CIP account, along with additions and deductions made during the year. Additionally, the estimated costs to complete construction projects must be disclosed.

General Accounting Procedures:
Identifying Transactions
At the inception of a CCP, organization management must decide how to fund and track the project. A CCP involves various financial transactions with numerous items being tracked and with each item potentially involving several expenses/expenditures or invoices. An organization can have multiple construction projects to track at the same time. To ensure a proper audit trail, a project identifier associated with construction expenses/expenditures should be used on all payment documents. Total expenditures for each construction project should be summed up to obtain the CIP balance to report. Monthly reconciliation between CCPs and the CIP expenses/expenditures account is strongly encouraged. Quarterly reconciliation is mandatory and should be performed in a timely manner.

As provided by Georgia law, the construction division of the Georgia State Finance and Investment Commission (GSFIC) has authority to manage construction projects for State reporting organizations.

Organizations that receive approval for a construction project to be managed by GSFIC should rely on GSFIC administration of the project. None of the construction activity prior to completion of the project should be recorded by the beneficiary organization. Upon completion of the project, the asset is transferred to the beneficiary organization and recorded in the appropriate class in accordance with capital assets policies. Refer to the policy titled *GSFIC Reimbursements for Bond Funded Construction Projects* for additional guidance on GSFIC managed projects.

Organizations that have CCPs that are managed and/or financed by GSFIC may obtain current quarterly information by accessing the following web link:

http://gsfic.georgia.gov/00/channel_modifieddate/0,2096,77323081_80872350,00.html

Organizations with CCPs that are not managed by GSFIC must rely on the information provided by their project accounting records. The responsibility for accuracy and documentation lies solely with the organization.

Accounting Transactions and Journal Entries

Following are journal entries that are required to reflect CCP activity in the different fund types. For, simplicity, assume that there is no encumbrance liability balance related to CCP at year-end. Under that assumption, no adjustments are required to convert from the statutory basis of accounting to the modified accrual basis. Refer to the *Capital Assets – General* policy for conversion entries related to year-end encumbrance balances.

CCP Outlays Recorded in a Governmental Fund

State organizations that receive approval for construction projects and record the transactions in a governmental fund should make the following entry at the fund level.

To record construction outlays:

Debit	$10,000	Construction in Progress (728xxx) or Expenditures (Various accounts)
Credit	$10,000	Cash (101xxx) or Accounts Payable (200xxx)

No accounting entries are made during the construction phase by organizations having their capital projects managed by GSFIC. The entry mentioned above is recorded only by the organization managing the project.

Government-wide Entries to Convert to the Accrual Basis for Government-wide Reporting

At year-end construction outlays exceeding the capitalization threshold are recorded as CIP in the governmental activities column of the government-wide statement of net assets. SAO uses the information provided by GSFIC or the organization managing the project and the year-end forms to make the adjusting entries.

To capitalize the asset:

Debit	$100,000	Construction in Progress (180xxx)
Credit	$100,000	Construction in Progress (728xxx) or Expenditures (Various accounts)

After completion of the project, the asset is moved from the construction in progress account to the appropriate asset class. The following entry is recorded in the governmental activities column of the government-wide statement of net assets.

To reclassify the constructed asset to the appropriate asset class:

Debit	$100,000	Building (171xxx or other appropriate asset class account)
Credit	$100,000	Construction in Progress (180xxx)

When the project is managed by GSFIC, once construction is complete, the asset is transferred to the beneficiary organization and the following entry must be recorded in the governmental activities column of the government-wide statement of net assets.

To remove CIP from GSFIC books:

Debit	$100,000	Transfers out (475001)
Credit	$100,000	Construction in Progress (180xxx)

To record the constructed asset in the beneficiary organization's books:

Debit	$100,000	Building (171xxx or other appropriate asset class account)
Credit	$100,000	Transfers In (471001)

It is important to note that if the beneficiary organization is a proprietary fund, the asset transferred is recorded as a capital contribution at the fund level; then at the entity-wide level, the capital contribution is reversed and a transfer is recorded. Refer to the *Capital Assets – Asset Transfers and Other Disposals* policy for comprehensive journal entries related to asset transfers.

<u>CCP Recorded in a Proprietary or Fiduciary Fund Using the Accrual Basis</u>
State organizations that receive approval for construction projects and record the transactions in a proprietary or fiduciary fund should make the following entries at the fund level.

To record construction outlays during the construction phase:

Debit	$100,000	Construction in Progress (180xxx)
Credit	$100,000	Cash (101xxx) or Accounts Payable (200xxx)

To record the constructed asset in the organization's books once the project is completed:

Debit	$100,000	Building (171xxx or other appropriate asset class account)
Credit	$100,000	Construction in Progress (180xxx)

Year-End Accounting Procedures
The SAO financial reporting group will request information about CIP as part of its year-end information package. All organizations included in the State of Georgia reporting entity that have CIP activity during the year must either provide audited disclosures that comply with this policy or complete the information for CIP on the Capital Assets and Construction in Progress forms. This information is required to ensure that appropriate accrual basis adjusting entries are recorded for the annual financial reports.

<u>Authority</u>:

- GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*
- GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*
- GASB Codification Section 1300, *Fund Accounting*

- GASB Codification Section 1400, *Reporting Capital Assets*
- OCGA 50-17-22 State Financing and Investment Commission
- Other SAO capital assets policies

Applicability:
Personnel at all organizations included in the State of Georgia reporting entity that have capital asset accounting and reporting responsibilities should be knowledgeable of this policy, including those responsible for maintaining capital asset inventory records.

Definitions:
Capital Construction Project **(CCP)** – The accounting record of a project dedicated to the acquisition or construction of a specific capital asset or asset group.

Construction in Progress **(CIP)** – A capital asset account reflecting the cost of construction work for projects not yet completed.

Capital Projects Fund **–** A fund used to account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including the acquisition or construction of capital facilities and other capital assets. Capital projects funds exclude those types of capital-related outflows financed by proprietary funds or for assets that will be held in trust for individuals, private organizations, or other governments [GASB 54].