PLANT FUND ACCOUNTING

There are two basic methods used to handle plant asset accounting: expense and capitalization. The expense method ignores the value of plant assets after purchase and is the most common method used by churches and smaller church schools. The capitalization method, on the other hand, is used in virtually all other levels of the denomination. The distinguishing feature of the capitalization method is that plant assets are recorded (and depreciation recognized) on the balance sheet. For non-profit accounting, the capitalization method also discloses the value of the plant assets (land, buildings, and equipment) separately from funds available for operating.

PLANT FUND & FUNCTIONS

The plant fund is used to account for plant (fixed) assets—land, buildings, and equipment—and funds set aside for their purchase, improvement, and/or replacement. Your statement of changes in net assets uses the terms capital additions or deductions to differentiate plant activity from operating activity (plant and capital are many times used interchangeably). Plant accounting consists of two components: Investment in Plant and Unexpended Plant.

Investment in Plant

Investment in Plant is only used to record the equity value of plant assets capitalized. This equity value is represented in an Investment in Plant balance separate from other equity balances representing expendable funds. The investment in plant must always equal the equity value of the plant assets (cost minus accumulated depreciation minus plant asset loans outstanding). To accomplish this requires a slight change in the way entries are made compared to commercial accounting. Follow the procedures in this chapter and you will save yourself a lot of problems with reconciliation.

Unexpended Plant

Unexpended plant is the other component of the plant fund. It holds the balance of <u>expendable funds</u> (i.e. cash & investments) allocated for capital activity. Because of the traditional separation of conference vs. association, and the political problems associated with the possession (and therefore control) of funds, unexpended plant functions may be accounted for in either or both the operating and plant funds. However, it is preferable to have all capital activity in a single place--the plant fund--if assets are capitalized. If all capital purchases are expensed (most churches and church schools), unexpended capital should be kept in the operating fund.

The unexpended plant may be sub-divided to distinguish between funds held for specific capital purposes. These sub-divisions are called functions. Since capital funds are commonly raised and/or held over a period of time, a different unexpended plant function should at least be set up for each major type of capital activity (e.g. land improvements, buildings, equipment, vehicles, etc.). The unexpended plant functions may be as specific as desired.

UNEXPENDED PLANT: Income

Unexpended plant functions are used to record income designated for land, building, or equipment purchases, improvements, and/or replacement. Capital income (donation or other) is receipted into an appropriate unexpended plant function. Income from the sale of plant assets should also be receipted into an unexpended plant function. Use your normal receipting procedure to post the income.

Plant Asset Income entries:	Debit	Credit
Donations	Cash/Bank	Unexp: Income
Sales income	Cash/Bank	Unexp: Income

Funding Transfers

Operating or other types of funds that are allocated for capital should be transferred to an unexpended plant function. This is called funding. There are two basic types of plant funding: acquisition and depreciation. Acquisition funding is "new" money being set aside for capital purchases, etc. Depreciation funding is operating funds set aside for the eventual replacement of plant assets.

Though it is recommended that full depreciation funding be practiced (i.e. transferring from operating to unexpended plant an amount equal to the total depreciation expense) there is presently no specific requirement to do so for conferences and academies. If depreciation is not fully funded then the distinction between acquisition and depreciation is not really meaningful. Also, since there is usually no distinction made in the unexpended plant concerning what portion of any balance was funded by depreciation or for acquisition it may not really make any difference anyway. In any case the funds are available for expenditure as the board sees fit (unless third-party donor restrictions apply of course).

Plant Funding by check:	Debit	Credit
Operating Fund	Depr/Acq Funding	Bank Account
Plant Fund	Cash/Bank	Unexp: Depr/Acq Funding

In cases where it is desired to keep the cash in the operating fund for investment or other reasons, the funding can be done by voucher. However, this method is not normally recommended since there is no assurance that funds will actually be available when needed by the plant fund.

Plant Funding by voucher:	Debit	Credit
Operating Fund	Depr/Acq Funding	Due to Unexp Plant
Plant Fund	Due from Operating	Unexp: Depr/Acq Funding

Capital Purchases

As mentioned previously, there are two basic methods of accounting for plant asset purchases (or additions): the expense method and the capitalization method.

Of the two, the expense method is the more simple. Assets purchased are recorded as an expense; period. No plant asset is recorded. This method is only suitable for asset purchases or improvements not considered significant enough in value to warrant maintaining a record of the asset even if the capitalization method is in use for other assets. The expense is usually charged to an operating function.

Cash payment entries for assets expensed:	Debit	Credit
Plant Asset Purchase	Oper: Purchase Exp.	Cash/Bank
Plant Asset Improv	Oper: Improv. Exp.	Cash/Bank

The capitalization method requires recording the plant asset therefore involving the plant fund. The purchase and the recording of the plant asset are two separate steps. We are only concerned with recording the purchase at this point. When cash payments are made, including down payments but excluding any plant loan payments (see Capital Loan section later in this chapter), they are recorded as a capital expense (addition) in a unexpended capital function of the plant fund.

Cash payment entries for assets capitalized:	Debit	Credit
Plant Asset Purchase	Unexp: Purchase Exp	Cash/Bank
Plant Asset Improv	Unexp: Improv. Exp	Cash/Bank

Capital Balance

Any balance remaining in the unexpended plant functions are available for capital purchases. If an unexpended plant function balance is negative, you have spent more than received and need to either generate additional income or have a transfer authorized from another unexpended plant function or operating fund to cover the overexpenditure. A negative unexpended function balance indicates the unauthorized (or at least not properly accounted for) expenditure of funds set aside for other purposes. Do not permit a negative function balance to remain.

INVESTMENT IN PLANT

In addition to recording the purchase expense, the capitalization method involves additional steps to account for plant assets after purchase. The presence of a fixed (or plant) asset section in the balance sheet indicates that the capitalization method is in use. In addition, the net investment in plant (asset cost minus accumulated depreciation minus outstanding capital loan principal) is recognized separately from the rest of the organization net asset balance (fund balance) which is expendable.

In commercial accounting the value (or investment) in plant assets is not kept separate from other net worth. However, the philosophy in non-profit accounting assumes that plant assets are not available for operating (i.e. you do not sell your building to raise funds to operate). Therefore, a distinction is made between expendable fund balances and that representing non-expendable plant assets. The Investment in Plant serves this purpose.

The most important rule you can follow to keep your Investment in Plant correct is: whenever you post to an asset, accumulated depreciation, or plant loan payable account always post the other side of the entry to the Investment in Plant function. <u>ALWAYS!</u> This requires a slight change in the way plant asset entries are recorded compared to commercial accounting. Follow the examples rather than your inclination and you will save a lot of problems with reconciliation.

Capital Additions

After recording an expenditure of funds as noted previously, the value of any asset considered significant enough to warrant maintaining a plant asset inventory record must be reflected in the Investment in Plant. Record the asset at its full value even if a loan is involved. Donated assets should be recorded at fair market value.

	Debit	Credit
Recording capital additions:	Plant Asset	Invest: Addition

Capital Loans

It is assumed that any plant asset purchase requiring a loan is significant and will be capitalized. The entries are slightly different if the asset is expensed such as would be the case with church and church school land and buildings which are capitalized on the conference books instead.

Since plant asset loans represent a third-party investment in your plant asset(s) it reduces your investment of the cost of purchase. The full cost of the asset is recognized in the preceding step (capital additions). You must now account for the third-party investment.

	Debit	Credit
New Plant Asset Loans:	Invest: New Loans	Loans Payable

This procedure is all that is necessary if the lending organization forwards the principal of the loan directly to the seller. If, however, you receive the loan principal in cash, you must also record the cash receipt into the unexpended plant function. Then when the asset is purchased, record the loan principal portion of the cost in the same account (the two entries will net out in the bank and unexpended function accounts resulting in the same effect as the direct disbursement from the lending organization to the seller). Use the normal capital purchase procedure to record your purchase cost in excess of the loan principal (i.e. down payment, etc.).

Loan Principal Cash entries:	Debit	Credit
Cash Received	Cash/Bank	Unexp: Misc. Activity
Cash Expended	Unexp: Msc Activity	Bank Account

Capital Loan Payments

Once you start making payments on a plant asset loan you must distinguish that portion of the payment used for principal reduction from that portion representing interest. Record the payment to the lending organization first.

Plant Loan Cash Payments:	Debit	Credit
Principal	Unexp: Principal Pmt	Bank Account
Interest	Unexp: Interest Pmt	Bank Account

Next, record the reduction of the loan payable (principal only) and the shift in investment in the asset from the lending organization to yours.

	Debit	Credit
Plant Loan Reduction:	Loan Payable	Invest: Loan Reduction

Depreciation

You need to reflect the declining value of any asset you have set up using the capitalization method. You do this by recording depreciation. Once the depreciation for the plant assets is determined, it is recorded and the reduction of the value of the asset is also recognized in your investment in plant.

	Debit	Credit
Recording depreciation:	Invest: Depr Expense	Accumulated Depr.

Capital Deductions

When you have recorded an asset using the capitalization method you will have to remove it when the asset is disposed of. This is referred to by the term capital deductions since it is the opposite of additions. There are two steps to consider when recording capital deductions: 1) recording any sale income received, and 2) removing the asset from your records.

Record all plant asset sales income as described earlier under the heading Capital Income. This step is the same for all plant assets (land, buildings, or equipment). If you did not receive income when you disposed of the asset, skip this step.

To remove plant assets set up using the capitalization method you must adjust your asset account and the investment in plant. The cost of the asset, and any accumulated depreciation, must be removed from the books. The difference between these (the book value) represents your investment in the asset and must also be removed from the Investment in Plant.

	Debit	Credit
Plant Asset Deductions:	Accumulated Depr.	Plant Asset
	Invest: Assets Sold (Net)	

RECONCILIATION

Each month you post equipment asset additions, depreciation, or deductions you should reconcile your plant (fixed) assets with your Investment in Equipment balance. At least once each year you should also reconcile your plant inventory records with the asset accounts in your ledger.

To reconcile your plant (fixed) assets with your Investment in Equipment balance, subtract any plant asset loans outstanding from the book value of your net plant assets (asset cost less accumulated depreciation) and compare it with the Investment in Plant balance. If they are not equal a mistake has been made. Review the entries made since the last time a reconciliation was performed to locate the error. Once corrected the figures will be equal.

To reconcile your plant assets inventory with the asset accounts in your ledger, add separately the cost, accumulated depreciation, and book amounts from your inventory. The total cost less total accumulated depreciation must equal the total book value. If they do not re-add the figures. They cannot possibly reconcile with the ledger accounts if they do not reconcile with themselves.

The total cost figure from your plant asset inventory records must equal the sum of the plant asset accounts (excluding accumulated depreciation). The total accumulated depreciation amount from the inventory records must equal the sum of the accumulated depreciation accounts in the ledger. The total plant asset inventory book value must equal the Investment in Plant balance. If any of these figures do not reconcile a mistake has been made. Locate and correct the mistake.

SUMMARY

The entries presented in this chapter are repeated here in summary form.

Expensed Plant Assets:	<u>Debit</u>	<u>Credit</u>
Purchase	Oper: Expense	Cash/Bank
Sale	Cash/Bank	Oper: Income

Capitalized Plant Assets:

Because there is a slight change in the way plant asset entries are recorded compared to commercial accounting, the most important rules to follow when recording capitalized assets are: <u>1) Always post to an unexpended plant</u> function to record plant fund cash/bank receipts or expenditures (due to and due from entries are treated like cash), and <u>2) Always post to the Investment in Plant</u> to record the value of assets (including additions, depreciation, and retirements) or any change in plant loans payable. The procedures outlined in this chapter follow these rules and you will save yourself a lot of reconciliation problems if you follow them.

	<u>Debit</u>	<u>Credit</u>
Income entries:		
Donations	Cash/Bank	Unexp: Income
Sales income	Cash/Bank	Unexp: Income
Plant Funding by check:		
Operating Fund	Depr/Acq Funding	Cash/Bank
Plant Fund	Bank Account	Unexp: Depr/Acq Funding
Plant Funding by voucher:		
Operating Fund	Depr/Acq. Funding	Due to Unexp. Plant
Plant Fund	Due from Operating	Unexp: Depr/Acq Funding
Cash payment entries (including down payments, excluding loan payments):		
Plant Asset Purchase	Unexp: Purchase Exp	Cash/Bank
Plant Asset Improv	Unexp: Improv Exp	Cash/Bank
Capital Additions (cost):	Plant Asset	Invest: Addition
New Plant Asset Loans:	Invest: New Loans	Loans Payable
Loan Principal Cash entries (if loan principal is received in cash):		
Cash Received	Cash/Bank	Unexp: Misc. Activity
Cash Expended	Unexp: Msc Activity	Bank Account
Plant Loan Cash Payments:		
Principal	Unexp: Principal Pmt	Bank Account
Interest	Unexp: Interest Pmt	Bank Account
Loan Principal Reduction:	Accounts Payable	Invest: Loan Reduction
Plant Asset Deductions:	Accumulated Depr.	Plant Asset
	Invest: Assets Sold (Net)	