

Manual of Accounting and Financial Reporting for Pennsylvania Local Educational Agencies (LEAs)

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Maintained by:
PA Office of the Budget
Office of Comptroller Operations
Central Agencies & School Finance Unit

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Chapter 1: Introduction

Introduction

The State Constitution declares "The General Assembly shall provide for the maintenance and support of a thorough and efficient system of public education to serve the needs of the Commonwealth." To carry out this mandate the General Assembly has established a public school system and authorized the **Pennsylvania Department of Education (PDE)** to administer school laws and assist LEAs in providing educational programming to Pennsylvanians.

The mission of the PDE is to assist the General Assembly, the Governor, the Secretary of Education and Pennsylvania educators in providing for the maintenance and support of a thorough and efficient system of education. This includes ensuring proper financial reporting.

Additional information on the PDE can be found at: www.education.pa.gov

The Office of Comptroller Operations (OCO) is part of the Office of the Budget of the Commonwealth of PA. The OCO works with the PDE in assisting the Secretary of Education and Governor in enforcing established policies and standards regulating the expenditure of public funds. Within the OCO is the Bureau of Accounting and Financial Management (BAFM), and within the BAFM is the Central Agencies & School Finance Unit (CA&SF Unit). School Finance is responsible for the collection, processing, and review of the AFR-Annual Financial Report (PDE forms 2056 and 2057). Other administrative functions include the maintenance of a uniform accounting manual and the Chart of Accounts and ensuring proper financial reporting in accordance with Sections 2-218 and 9-921A of Public School Code of 1949 (School Code), which states "...all financial accounting and reporting by Pennsylvania Local Educational Agencies (LEAs - school districts, charter schools, area vocational-technical schools/career technology centers and intermediate units) shall be in accordance with generally accepted accounting and reporting standards..." Information gathered from AFRs is used to calculate tuition rates and actual instructional expense, as well as, produce reports requested by the federal government.

Additional Information on the CA&SF Unit can be found at: www.education.pa.gov; under Teachers and Administrators/School Finances/Office of Comptroller Operations.

Purpose

The Office of Comptroller Operations (OCO) has compiled this manual as a financial reporting resource, as well as, to provide a uniform and standardized framework for reporting financial data to the state. It is essential for financial reporting to be consistent for LEAs. The manual captures and illustrates imperative accounting and financial reporting requirements of Pennsylvania public elementary and secondary school systems in accordance with recognized generally accepted accounting principles (GAAP) for governmental entities and state laws and regulations.

Additionally, the OCO maintains the Chart of Accounts for Pennsylvania LEAs which is provided in a separate manual. This manual includes an account code structure that is modeled after the current, *Financial Accounting for Local and State School Systems: 2014 Edition* (NCES 2015-347). U.S. Department of Education, National Center for Education Statistics, Washington, DC: U.S. Government Printing Office. The Chart of Accounts coincides with the guidance provided in this manual. We have established a standard account code structure that allows for the accumulation of program costs at the level of detail the school administration chooses. The Chart of Accounts is also located on PDEs web-site under Office of Comptroller as listed above.

History

The last major revision to this manual was in 2005 with an interim update issued on July 1, 2010 to reflect changes related to Governmental Accounting Standards Board (GASB) No. 54. Since 2005, there have been numerous changes to GASB Statements and the Annual Financial Report (AFR) requirements. These changes along with changing responsibilities of the CA&SFU and the increased availability of information on PDE's web-site has prompted this version of the manual which focuses more on general GASB rules and specific AFR reporting requirements.

Therefore, the primary changes reflected in this manual include:

- Changes to the Annual Financial Report (AFR) filing requirements as described in Sections 218 & 921-A of the School Code revised November 17, 2010. This change eliminated entity-wide financial statements within the AFR as well Notes and the management's discussion and analysis.
- Removal of the budget chapter.
- GASB Statement updates, with emphasis on those Statements impacting AFR filing. Most significantly:
 - GASB Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position
 - GASB Statement No. 65, Items Previously Reported as Assets and Liabilities

Organizations Instrumental in Local Educational Agency Financial Accounting & Reporting

Governmental Accounting Standards Board (GASB)

The GASB is the independent organization that establishes and improves standards of accounting and financial reporting for United States' state and local governments. The generally accepted accounting and reporting guidance included in this manual began with the National Council on Governmental Accounting, Statement No. 1, Governmental Accounting and Financial Reporting Principles, and were adopted by the GASB in 1984 in their first pronouncement, GASB Statement No. 1.

Accounting personnel should be familiar with the principles and statements issued by the GASB that are available in its publication titled Codification of Governmental Accounting and Financial Reporting Standards.

This publication and additional information on GASB can be found at: <http://www.gasb.org>

The National Center for Education Statistics, U.S. Department of Education (NCES)

The National Center for Education Statistics (NCES) is the primary federal entity for collecting and analyzing data related to education in the U.S. and other nations. The NCES is located within the U.S. Department of Education and the Institute of Education Sciences. The NCES fulfills a Congressional mandate to collect, collate, analyze, and report complete statistics on the condition of American education; conduct and publish reports; and review and report on education activities internationally.

The account code structure in this manual is modeled after the current Federal Accounting Handbook II, as revised, and promulgated by the NCES, U.S. Department of Education. A standard account code structure allows for the accumulation of program costs at the level of detail the school administration chooses, as well as provides for financial reporting in conformance with governmental accounting and financial reporting principles for all state and local governments, including public school systems.

Additional information about the NCES can be found at: <http://nces.ed.gov>

The Association of School Business Officials (ASBO) International

Founded in 1910, the ASBO International is a professional association of school business management professionals. They provide programs and services to promote the highest standards of school business management practices, professional growth, and the effective use of educational resources.

Additional information about ASBO International can be found at: <http://www.asbointl.org>

Pennsylvania Association of School Business Officials (PASBO)

The Pennsylvania Association of School Business Officials (PASBO) is a statewide association devoted to providing members with education, training, professional development and timely access to legislative and policy news. It's membership base covers school professionals working in finance, accounting, operations, facilities, transportation, food service, technology, communications, human resources, purchasing and safety services.

The PASBO accounting committee is one of the PASBO committees whose purpose is to review and comment upon all matters relevant to school or governmental accounting and to act in an advisory capacity to the PASBO board and executive director in accounting and related matters. As part of their responsibilities, the committee regularly reviews and provides responses to the GASB on Exposure Drafts.

Additional information on the PASBO can be found on the web at: <http://www.pasbo.org>

The Pennsylvania School Boards Association (PSBA)

The PSBA is a nonprofit statewide association of public school boards, pledged to the highest ideals of local leadership for the public schools of the Commonwealth. Since their foundation in 1895, they set out to create an efficient system of public education by maintaining legislative awareness and communication with members of local, state, and federal legislative bodies.

Additional information on the PSBA can be found at: <http://www.psba.org>

American Institute of Certified Public Accountants (AICPA)

Founded in 1887, the AICPA is the national, professional organization for all Certified Public Accountants. Its mission is to provide members with the resources, information, and leadership that enable them to provide valuable services in the highest professional manner to benefit the public, employers, and clients.

Additional information on the AICPA can be found at: <http://www.aicpa.org>

The Pennsylvania Institute of Certified Public Accountants (PICPA)

The PICPA is an active professional association of accounting professionals in Pennsylvania working together to better serve the public and to enhance the accounting profession. Founded in 1897, it is the second oldest and fifth largest state CPA organization in the United States. The mission of the PICPA is to further the well-being of its members, while upholding the public interest.

The PICPA offers a number of state conferences and workshops, member services and benefits.

Additional information on the PICPA can be found at: <http://www.picpa.org>

Government Finance Officers Association (GFOA)

The GFOA is the professional association of state/provincial and local finance officers in the United States and Canada, and has served the public finance profession since 1906. The association's members are dedicated to the sound management of government financial resources.

The association provides and administers a broad range of products, services, and programs in the major functional areas of government financial management, including accounting, auditing, and financial planning, along with many other areas.

The GFOA is the publisher of Governmental Accounting, Auditing and Financial Reporting (GAAFR). All schools should request this book if they don't have it.

Additional information on the GFOA can be found at: <http://www.gfoa.org>

Generally Accepted Accounting Principles (GAAP) and the Governmental Accounting Standards Board (GASB)

GAAP are accounting standards and practices that govern how an organization keeps information about its finance-related resources, obligations, and transactions and, ultimately, how it reports that data in financial statements.

In the United States, GAAP for state and local governments have developed separately of and differently from GAAP for private-sector companies. Private-sector GAAP initially was developed through various committees of the American Institute of Certified Public Accountants (AICPA). However, in the early 1970's that responsibility was transferred outside of the AICPA to the Financial Accounting Standards Board (FASB), a group that functions under the sponsorship of the Financial Accounting Foundation (FAF). GAAP for state and local governments was initially developed through various committees of Municipal Finance Officers Association, now known as the Government

Finance Officers Association (GFOA), an industry trade organization. Responsibility for setting GAAP for state and local governments was transferred from the last GFOA committee, the National Council on Governmental Accounting (NCGA), to the Governmental Accounting Standards Board (GASB) in 1984. The GASB, like the FASB, functions under the sponsorship of the FAF and is housed in the same facilities with the FAF and the FASB in Norwalk, Connecticut. The GASB establishes accounting and financial reporting standards for activities and transactions of state and local governmental entities and the FASB establishes standards for activities and transactions of all other entities.

Historical precedence is perhaps the strongest factor leading to the development of separate Boards to establish GAAP for private-sector and governmental organizations. However, there also are environmental factors leading to the development of two standards-setting structures. Private-sector standards setting developed in response to Securities and Exchange Commission (SEC) oversight of business accounting and financial reporting brought about by the 1929 stock market crash. State and local governments are largely exempt from SEC oversight. Instead, with states being sovereign bodies, state officials are responsible for the oversight of accounting and financial reporting for jurisdictions within their individual states. With federal pressure brought on the governmental community because of financial problems in the late 1970's and early 1980's, such as the financial distress of major cities such as New York, state officials worked in concert with the GFOA, which already had a standard-setting structure, that would be responsive to the unique financial environment in government.

What is that unique financial environment in government? It is explained in detail in GASB Concepts Statement No. 1, *Objectives of Financial Reporting*. Briefly, however, some of the strongest characteristics have to do with the involuntary nature of resource providers. For example: the budget as an expression of public policy and financial intent, as a method of providing control, and with the nature of the political process. Those governmental characteristics have led to GAAP for state and local governments that focus in large part on detailed information about how governments obtain and use their resources rather than, as is the focus in the private sector, on whether the current-period operations have resulted in a profit or loss. GASB Concepts Statement No. 1, however, introduced the concept of inter-period equity and the idea that governmental financial reporting should provide information on whether current-year revenues were sufficient to pay for current-year expenditures.

The Hierarchy of Generally Accepted Accounting Principles

The hierarchy of GAAP for governments was set forth by the AICPA literature adopted in 1992. In order for AICPA literature to remain authoritative and to address the issues associated with GASB Technical Bulletins and GASB Implementation Guides, the hierarchy was later reevaluated and condensed into two categories which became effective for reporting periods after June 15, 2015. Additional information is provided in GASB Statement No. 76.

GAAP hierarchy establishes the order of priority of pronouncements and other sources of accounting and financial reporting guidance that a governmental entity should apply. The sequential order of the hierarchy beginning with the greatest authority is as follows:

Category A - Officially established accounting principles—Governmental Accounting Standards Board (GASB) Statements

Category B - GASB Technical Bulletins; GASB Implementation Guides and literature of the AICPA cleared by the GASB

If the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP described above in categories A or B, a governmental entity should first consider accounting principles for similar transactions or other events within a source of authoritative GAAP described above and then may consider non-authoritative accounting literature from other sources (that does not conflict with or contradict authoritative GAAP), as discussed below:

Sources of non-authoritative accounting literature include GASB Concepts Statements; pronouncements and other literature of the Financial Accounting Standards Board, Federal Accounting Standards Advisory Board, International Public Sector Accounting Standards Board, and International Accounting Standards Board, and AICPA literature not cleared by the GASB; practices that are widely recognized and prevalent in state and local government; literature of other professional associations or regulatory agencies; and accounting textbooks, handbooks, and articles.

In evaluating the appropriateness of non-authoritative accounting literature, a governmental entity should consider the consistency of the literature with the GASB Concepts Statements, the relevance of the literature to particular circumstances, the specificity of the literature, and the general recognition of the issuer or author as an authority.

Reference: GASB Statement No. 76

Basic Governmental Accounting Principles

In 1979, the National Council on Governmental Accounting (NCGA) set forth basic principles of accounting and financial reporting in Statement 1, Governmental Accounting and Financial Reporting Principles. The principles established in Statement 1 are recognized as generally accepted accounting principles (GAAP) for governmental units by the American Institute of Certified Public Accountants (AICPA) and the Association of School Business Officials of the United States and Canada (ASBO).

GASB Codification Section 1100 provides a Summary Statement of Accounting Principles as outlined below. Adoption of the principles will (a) provide management with financial information that presents fairly and with full disclosure the financial position and results of financial operations; (b) provide reliable financial information as a basis for program evaluation and budgetary planning; (c) give the entity's financial statements greater credibility with four principal groups: the general public, investors, governmental units and educational and research organizations; whose interests and decisions are dependent upon the financial information produced by the entity's accounting system; and (d) enhance the comparability of financial reporting.

PRINCIPLE 1

Accounting and Reporting Capabilities

A governmental accounting system must make it possible both: (a) to present fairly and with full disclosure the funds and activities of the governmental unit in conformity with generally accepted accounting principles, and (b) to determine and demonstrate compliance with finance-related legal and contractual provisions.

Reference: GASB Codification Section 1200, NCGA-1

Pennsylvania LEAs:

LEAs annual financial reporting to the Pennsylvania Department of Education (PDE), Office of Comptroller Operations, and other external users will be in accordance with the principles described in this manual. These principles are based on generally accepted accounting principles (GAAP) for governmental entities. GAAP are uniform minimum standards of and guidelines for financial accounting and reporting.

Adherence to the principles described in this manual assures that financial reports of all LEAs, regardless of size or type, contain financial information based on the same measurement and classification criteria.

The LEAs accounting records must also be able to produce financial information that will meet legal and contractual compliance requirements. An example of this situation would be the reporting of tax revenues on a cash basis for basic instructional subsidy purposes and the recording of tax revenues for financial statement presentation purposes on the modified accrual basis of accounting.

PRINCIPLE 2

Fund Accounting Systems

Governmental accounting systems should be organized and operated on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein; which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. Fund financial statements should be used to report additional and detailed information about the primary government, including its blended component units. The focus of governmental and proprietary fund financial statements is on major funds.

Reference: GASB Codification Section 1300, NCGA-1

PRINCIPLE 3

Fund Types

In fund financial statements, governments should report governmental, proprietary, and fiduciary funds to the extent that they have activities that meet the criteria for using those funds.

- Government funds
 - The general fund
 - Special revue funds
 - Capital projects fund
 - Debt service funds
 - Permanent funds
- Proprietary funds
 - Enterprise funds
 - Internal service funds
- Fiduciary funds
 - Pension (and other employee benefit) trust funds
 - Investment trust funds
 - Private-purpose trust funds
 - Agency funds

Reference: GASB Codification Section 1300, NCGA-1

Pennsylvania LEAs:

The types of funds used in a school accounting system must be adapted to the needs of Pennsylvania LEAs. In addition to a general fund, certain funds are used in Pennsylvania to fulfill accounting requirements concerned with the School Code. For example school districts must maintain a separate cafeteria fund according to Section 504 of the School Code. More detail regarding specific fund types will be discussed in later chapters.

PRINCIPLE 4

Number of Funds

Governmental units should establish and maintain those funds required by law and sound financial administration. Only the minimum number of funds consistent with legal and operating requirements should be established because unnecessary funds result in inflexibility, undue complexity, and inefficient financial administration.

Reference: GASB Codification Section 1300, NCGA-1

PRINCIPLE 5

Reporting Capital Assets

A clear distinction should be made between general capital assets and capital assets of proprietary and fiduciary funds. Capital assets of proprietary funds should be reported in both the government-wide and fund financial statements. Capital assets of fiduciary funds (and similar component units) should be reported only in the statement of fiduciary net position. All other capital assets of the governmental unit are general capital assets. They should not be reported as assets in governmental funds but should be reported in the governmental activities column in the government-wide statement of net position.

Reference: GASB Codification Section 1400, NCGA-1

PRINCIPLE 6

Valuation of Capital Assets

Capital assets should be reported at historical cost. The cost of a capital asset should include ancillary charges necessary to place the asset into its intended location and condition for use. Donated capital assets should be reported at their acquisition value (an entry price) at the time of acquisition.

Reference: GASB Codification Section 1400, NCGA-1 (Note that the above stated is according to GASB Statement No. 72. As of February 2016, the updates have not been reflected in Codification.)

PRINCIPLE 7

Depreciation & Impairment of Capital Assets

Depreciation of a proprietary fund's capital assets should be recorded in the accounts of that fund. Depreciation is also recognized in those trust funds where expense, net income, and/or capital maintenance are measured.

Reference: GASB Codification Section 1400, NCGA-1

PRINCIPLE 8

Reporting Long-Term Liabilities

Because of the distinctive nature of fund financial statements and fund accounting requirements, some long-term liabilities should be reported in fund financial statements, while some should be reported only in the governmental activities column in the government-wide statement of net position. NCGA Statement 1, Paragraph 32, states that "a clear distinction should be made between ... *fund long-term liabilities* and *general long-term liabilities*."

- Long-term liabilities directly related to and expected to be paid from proprietary funds should be reported in the proprietary fund statement of net position and in the government-wide statement of net position.

- Long-term liabilities directly related to and expected to be paid from fiduciary funds should be reported in the statement of fiduciary net position.

All other un-matured general long-term liabilities of the governmental unit should not be reported as liabilities in governmental fund level statements but should be reported in the governmental activities column of the government-wide statement of net position.

Reference: GASB Codification Section 1500, NCGA-1

PRINCIPLE 9

Measurement Focus and Basis of Accounting in the Basic Financial Statements

- Government-Wide Financial Statements

The government-wide statement of net position and the statement of activities should be prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions should be recognized when the exchange takes place. Revenues, expenses, assets, and liabilities resulting from non-exchange transactions should be recognized in accordance with section n50, "non-exchange transactions."

- Fund Financial Statements

In fund financial statements, the modified accrual or accrual basis of accounting, as appropriate, should be used in measuring financial position and operating results.

Financial statements for governmental funds should be presented using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues should be recognized in the accounting period in which they become available and measurable. Expenditures should be recognized in the accounting period in which the fund liability is incurred, if measurable, except for un-matured interest on general long-term liabilities, which should be recognized when due.

Proprietary fund statements of net position and revenues, expenses, and changes in fund net position should be presented using the economic resources measurement focus and the accrual basis of accounting.

Financial statements of fiduciary funds should be reported using the economic resources measurement focus and the accrual basis of accounting. The recognition of certain liabilities of defined benefit pension plans and other postemployment benefit plans, is discussed in sections pe5, "pension plans—defined benefit," and po50, "postemployment benefit plans other than pension plans—defined benefit."

Transfers should be reported in the accounting period in which the inter-fund receivable and payable arise.

Reference: GASB Codification Section 1600, NCGA-1

PRINCIPLE 10

Budgeting and Budgetary Control

- An annual budget(s) should be adopted by every governmental unit.
- The accounting system should provide the basis for appropriate budgetary control.
- Budgetary comparisons should be presented for the general fund and for each major special revenue fund that has a legally adopted annual budget. Governments are encouraged to present such budgetary comparison information in schedules as a part of Required Supplementary Information (RSI). However, a government with significant budgetary perspective differences that result in the government's not being able to present budgetary comparisons for the general fund and each major special revenue fund is required to present budgetary comparison schedules as RSI based on the fund, organization, or program structure that the government uses for its legally adopted budget.

Reference: GASB Codification Section 1700, NCGA-1

Pennsylvania LEAs:

LEAs must, by law, adopt an annual budget for the general fund. LEAs should prepare an annual budget for every fund.

PRINCIPLE 11

Transfer, Revenue, Expenditure and Expense Account Classification

- At a minimum, the statement of activities should present:
 - Activities accounted for in governmental funds by function, as discussed in Section 1800, paragraph .133, to coincide with the level of detail required in the governmental fund statement of revenues, expenditures, and changes in fund balances
 - Activities accounted for in enterprise funds by different identifiable activities.
- Governmental fund revenues should be classified by fund and source. Expenditures should be classified by fund, function (or program), organization unit, activity, character, and principal classes of objects.
- Proprietary fund revenues should be reported by major sources, and expenses should be classified in essentially the same manner as those of similar business organizations, functions, or activities. Revenues and expenses should be distinguished as operating and non-operating.
- Proceeds of general long-term debt issues should be classified separately from revenues and expenditures in the governmental fund financial statements.

- Contributions to term and permanent endowments, contributions to permanent fund principal, other capital contributions, special and extraordinary items, and transfers between governmental and business-type activities should each be reported separately from, but in the same manner as, general revenues in the government-wide statement of activities. In the proprietary fund statement of revenues, expenses, and changes in fund net position, these items should be reported separately after non-operating revenues and expenses. Transfers should be classified separately from revenues and expenditures in the governmental fund statement of revenues, expenditures, and changes in fund balances. Special and extraordinary items should be reported separately after "other financing sources and uses" in the governmental fund statement of revenues, expenditures, and changes in fund balances.

Reference: GASB Codification Section 1800, NCGA-1

PRINCIPLE 12

Common Terminology and Classification

A common terminology and classification should be used consistently throughout the budget, the accounts, and the financial reports of each fund or activity.

Reference: GASB Codification Section 1800, NCGA-1

PRINCIPLE 13

Annual Financial Reports

- Appropriate interim financial statements and reports of financial position, operating results, and other pertinent information should be prepared to facilitate management control of financial operations, legislative oversight, and, where necessary or desired, for external reporting purposes.
- A comprehensive annual financial report should be prepared and published, covering all funds and activities of the primary government (including its blended component units) and providing an overview of all discretely presented component units of the reporting entity—including introductory section, management's discussion and analysis (MD&A), basic financial statements, required supplementary information other than MD&A, appropriate combining and individual fund statements, schedules, narrative explanations, and statistical section. The reporting entity is the primary government (including its blended component units) and all discretely presented component units presented in accordance with Section 2100, "Defining the Financial Reporting Entity."
- The minimum requirements for MD&A, basic financial statements, and required supplementary information other than MD&A are:
 - Management's discussion and analysis.
 - Basic financial statements. The basic financial statements should include:
 - Government-wide financial statements.
 - Fund financial statements.
 - Notes to the financial statements.

- Required supplementary information other than MD&A.
- As discussed in Section 2100, the financial reporting entity consists of (1) the primary government, (2) organizations for which the primary government is financially accountable and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's basic financial statements to be misleading or incomplete. The reporting entity's government-wide financial statements should display information about the reporting government as a whole, distinguishing between the total primary government and its discretely presented component units as well as between the primary government's governmental and business-type activities. The reporting entity's fund financial statements should present the primary government's (including its blended component units, which are, in substance, part of the primary government) major funds individually and non-major funds in the aggregate. Funds and component units that are fiduciary in nature should be reported only in the statements of fiduciary net position and changes in fiduciary net position.
- The nucleus of a financial reporting entity usually is a primary government. However, a governmental organization other than a primary government (such as a component unit, joint venture, jointly governed organization, or other stand-alone government) serves as the nucleus for its own reporting entity when it issues separate financial statements. For all of these entities, the provisions of Section 2100 should be applied in layers "from the bottom up." At each layer, the definition and display provisions should be applied before the layer is included in the financial statements of the next level of the reporting government.

Reference: GASB Codification Section 2200, NCGA-1

Pennsylvania LEAs:

LEAs are required to submit Annual Financial Reports (AFRs); Forms PDE-2056 (Intermediate Units) & PDE-2057 (school districts, charter schools, vocational-technical schools/career technology centers, and special program jointures) with the PDE through the OCO. The AFR must be filed in accordance with the provisions of Sections 218 & 921-A of the School Code as follows:

"...all financial accounting and reporting by LEAs shall be in accordance with generally accepted accounting and reporting standards, except that management discussion and analysis and related notes and the following financial statements shall not be required components of the annual financial report: entity-wide financial statements, including the statement of activities and the statement of net position; the reconciliation of the balance sheet - governmental funds to statement of net position; and the reconciliation of the statement of revenues, expenditures and changes in fund balances - governmental funds to statement of activities."

LEAs are required to complete additional schedules included as part of the AFR package. Annual Financial Reports are due to the OCO October 31st, following the close of the fiscal reporting period; July 1st through June 30th.

Chapter 2: Types of Local Educational Agencies and Summary of Funding

Types of LEAs

The term “Local Education Agency” (LEA) is used in this manual to refer to school districts, charter and cyber charter schools, area vocational-technical schools/career and technology centers, and intermediate units. The following describes such entities in more detail:

School Districts

School districts are considered to be political subdivisions with taxing authority. Depending on population, a school district can be in one of five classes, which include school districts of the first class, the first class A, the second class, the third class, and the fourth class. School districts in Pennsylvania receive their money from three separate sources: local monies (primarily through the collection of property taxes), state appropriations, and federal funds.

Article II of the Public School Code of 1949 (“School Code”) provides additional information on school districts.

Charter & Cyber Charter Schools

A **Charter School** is an independent public school established and operated under a charter approved by local school districts in which students are enrolled or attend (Section 1701-A of the School Code). Such schools, although classified as LEAs, are free of many state mandates, except for those pertaining to the health, safety, and civil rights of the state's children.

A **Cyber Charter School** is an independent public school established and operated under a charter and approved by the Department of Education. A cyber school uses the internet and other electronic means of technology to provide a significant portion of its curriculum and to deliver a significant portion of instruction to its students.

All students are eligible to attend a charter school at no charge to their families. Students residing in the chartering school district will receive first preference to attend the school. A charter school receives the majority of its funding from the school district in which the student resides (Section 1725-A of the School Code).

Transportation for Charter School Students

Section 1726-A of the School Code, specifies school district transportation responsibilities for resident students attending charter schools. If a charter school provides the transportation and receives funding from the school districts for this transportation service, the charter school should record this receipt to Revenue Account 6961, Transportation Services Provided other Pennsylvania LEAs.

Area Vocational-Technical Schools

Area vocational-technical schools (AVTS), also referred to as career and technology centers (CTC), are authorized by Section 1841 of the School Code.

School District Operated Area Vocational-Technical School

The State Board has approved several attendance areas comprised of a single school district to establish and operate an AVTS as an entity separate and distinct from the school district entity. In such cases, two general fund detailed expenditures and other financing uses sections of the Annual Financial Report must be filed - one for the AVTS entity, and one for the school district entity.

Vocational Education Costs

Costs will be classified as vocational education if the costs were incurred for courses of instruction approved by the Pennsylvania Department of Education (PDE) as shown on the Career and Technical Education System (CATS) approved program listing. Costs for courses of instruction not on the approved program listing are not classified as vocational education costs but are classified under the appropriate instructional sub-function.

- AVTS - Area Vocational-Technical School
- CTC - Career and Technology Center
- CATS - Career and Technical Education System
 - A system for collecting and reporting information about vocational education relating to a body of goals and objectives for vocational education.
- CIP CODE - Classification of Instructional Programs Code
 - Numeric codes developed by the Department of Education, Bureau of Vocational Education, for the classification of approved State Vocational Educational Instructional Programs.

Vocational Education Coding

LEAs offering PDE approved vocational education courses of instruction should report the costs for the courses by service area within the Instruction Sub-function for Vocational Education Programs on their Annual Financial Report.

The CATS approved program listing shows those courses approved and classified as vocational along with the Classification of Instruction Program Codes (CIP Codes). CIP Codes are numerical codes developed by the Department of Education, Bureau of Vocational Education, for classification of approved State Vocational Educational Instructional Programs.

The vocational instruction functions and sub-functions to which costs are to be reported are:

1300 - Vocational Education

1310 - Agricultural Education

1320 - Marketing and Distributive Education

- 1330 - Health Occupations Education
- 1340 - Home Economics Education
 - 1341 - Consumer and Homemaking Education
 - 1342 - Occupational Home Economics Education
- 1350 - Industrial Arts Education
- 1360 - Business Education
- 1370 - Technical Education
- 1380 - Trade and Industrial Education
- 1390 - Other Vocational Education Programs

*Home Economics Education is broken out to the dimension: Area of Responsibility

- AVTSs offering courses of instruction that are part of the normal vocational education curriculum of the AVTS should report the costs for the courses by service area within the Instruction Sub-function for Vocational Education Programs on their Annual Financial Report.
- AVTSs offering courses of instruction that are not part of the normal vocational education curriculum of the AVTS (e.g., remedial courses, full-day AVTSs offering a half-day of regular instruction) should report the costs for the courses in the Instruction Sub-function 1100 - Regular Programs on their Annual Financial Report.
- AVTSs administering PDE-approved vocational education satellites would report costs on their Annual Financial Report within the 1300 Vocational Education codes as outlined above.
- School districts offering courses of instruction that are part of a PDE-approved vocational education program (i.e. CATS, reported courses) should report the cost of these PDE-approved vocational education courses by service area within the 1300 Vocational Education codes as outlined above.
- School districts offering courses of instruction that have not been approved by PDE as vocational education courses should report the costs in the Instruction Sub-function 1100 - Regular Programs on their Annual Financial Report. Only PDE-approved vocational courses are reported as vocational costs within Function 1300. The CATS approved program listing shows those courses approved and classified as vocational.
- School districts sending students to an AVTS or a PDE-approved AVTS satellite should report the costs incurred in sub-function - Other Vocational Education Programs, and in object code 564 - Tuition to Area Vocational Technical Schools on their Annual Financial Report.

Adult Vocational Programs

An AVTS or school district offering courses of instruction to students that are classified as adults by law and/or regulation should report the cost for the courses by service area within the Instructional sub-function for Adult Education Programs on their Annual Financial Report. The sub-function, service area and areas of responsibility to which costs are to be reported are:

- 1600 - Adult Education Programs
- 1610 - Adult Vocational Education
- 1690 - Other Adult Education Programs
- 1691 - Instructional Services
- 1692 - Tutor Training

- Only those courses of instruction that are Adult Vocational Education courses should be charged to account code 1610. All other courses offered to adults should be charged to account code 1690.
- Tuition charged to adults should be credited to revenue account 6943 - Adult Education Tuition.

Intermediate Units

Intermediate units (IUs) were created by the Pennsylvania Legislature under Act 102 of 1970 Section 901A of the School Code to provide services to school districts. IUs are governed by a board of directors whose membership comes from representatives from their member school district board of directors.

Act 102 suggests that IU services include curriculum development and instructional improvement, research and planning, instructional materials, continuing professional education, pupil personnel, management services and state and federal agency liaison. However, IUs are not restricted from providing any service requested by their local school districts. Intermediate units have two purposes: to provide quality education services and to save tax money by providing cooperative services that cost each participant less than had they been provided independently. By combining resources, the IU can offer services that each school district, individually, could not conduct as economically or effectively.

IUs, unlike school districts, are not empowered to levy taxes. Revenue is received from a variety of sources: state and federal grants, and fees for services provided to other local education agencies, local governments and individuals. Funding for the IU programs of service (those suggested in Act 102) is provided by either subsidy withholding from school districts by PDE or by direct payment to the IU from the school districts. IUs have the option to charge their member school districts only for services that each district requests. When this option is exercised, an IU invoices the school districts that elect to receive the service. If a district elects not to receive the service, that district is not charged a cost for that particular service.

Intermediate units may operate programs that are funded by state, federal or local contracts. They may operate these programs either at the request (or mandate) of state, federal or local agencies or by submitting proposals in response to a Request For Proposals (RFPs). They also may enter into contracts with school districts, other intermediate units, and / or other governmental entities (i.e., counties, state or federal agencies, etc.) to provide services on a fee-for-service basis.

- Consortiums or Joint Purchasing Boards

Many intermediate units (IUs) have formed consortiums or joint purchasing boards for their member districts. The purpose of such arrangements is to provide an opportunity for school districts to jointly purchase materials, supplies, equipment and services, and to take advantage of the price savings associated with bulk purchasing.

LEA Revenue and Funding Sources

LEAs receive revenue from a variety of local, state, and federal sources. These sources are used to provide instruction and adjunct support services consistent with Article III of Pennsylvania's Constitution's which requires the "the General Assembly shall provide for the maintenance and support of a thorough and efficient system of public education to serve the needs of the Commonwealth." Revenues are derived from the following sources:

Local Funding

Revenue from local sources is the amount of money produced within the boundaries of the LEA and available to the LEA for its use. It includes tax revenues and other intergovernmental revenues collected by another governmental unit, local tax collector or agent of the LEA (net of collection fees). Shared revenues are revenues levied and/or collected by another governmental unit, and shared with the LEA in proportion to the amount collected on behalf of the LEA. Local source revenues also include investment income, student activity revenues, rental receipts, and tuition received from other LEAs or patrons. The Public School Code of 1949 as amended, and the Local Tax Enabling Act of 1965 as amended, empower school districts with the authority to levy and collect such taxes for the purposes of providing public education.

State Funding

The state funding streams include two types of funding: subsidies and grants. Subsidies are payments to schools based various student counts, local wealth, or formulas determined by legislation. Grants are funding streams that are competitive and may require the schools to complete applications and demonstrate a need for the funds. This revenue includes items such as: basic instructional and operational subsidies, specific educational program subsidies, non-educational program subsidies, state reimbursements for school employee benefits, nonpublic program funding, and vocational training.

The Office of Comptroller Operations (OCO) distributes state subsidy payments on behalf of the Pennsylvania Department of Education. State grant-funding, on the other hand, may be disbursed by the OCO or may be disbursed by another Commonwealth agency such as the Department of Health or the Department of Agriculture. It is the responsibility of the school to be aware of what grant funds are available for distribution.

The following is a summary of some of the major sources of state funding and may not be applicable to all LEAs:

Basic Education Funding

The largest education subsidy program that the Commonwealth administers is the Basic Education Funding subsidy. The Basic Education Funding is distributed to all of the Commonwealth’s public school districts. The formula is complex, and provides a level of financial support to ensure that a minimum program of education is provided at each public school district. The Pennsylvania Department of Education provides each school district, via the Financial Accounting Information System (FAI), with form PDE-2548, Report of Basic Education Funding that lists all of the components of the formula.

The Basic Education Subsidy is distributed to schools in a total of six (6) payments. The first five (5) payments are estimates; each of the five (5) estimates equal approximately 15 percent of the school’s entitlement and are paid on the last Thursday of August, October, December, February and April. The final payment is calculated by determining the actual entitlement due and subtracting out the first five (5) payments. The final payment is paid on June 1st.

The Basic Education Funding subsidy is also utilized as a vehicle for recovering funds that schools owe the Commonwealth. This recovery is referred to as deductions on the PDE-2548 Form. Situations in which a school might owe the Commonwealth funds include: overpayment of current or prior-year subsidies, Auditor General audit resolution, tuition recovery for students attending Approved Private Schools, Private Residential Rehabilitative Institutions, etc.; and school district costs for their participation in Intermediate Unit operated programs.

Sample of Basic Education Funding revenue entries are:

Cash	\$100,000.00	
Basic Education Revenue		\$100,000.00

To record the August receipt of Basic Education Funding Subsidy.

Cash	\$490,000.00	
IU Operating Expenditure	\$ 10,000.00	
Basic Education Revenue		\$500,000.00

To record the December receipt of Basic Education Funding Subsidy and recognize the IU Operating expenditure that was deducted in December.

Pupil Transportation

The Commonwealth is required by *Section 2543* of the School Code to reimburse LEAs for transportation of children between home and school. The Commonwealth funds LEAs for a portion of the cost of transporting public, non-public, and charter school children. It is important that schools keep thorough records relating to the transportation costs.

Social Security Contributions

Pursuant to *Section 8329 of Part 24*, the Pennsylvania Consolidated Statutes, LEAs are reimbursed for a percentage, not to be less than one-half of the employers’ share of the social security tax per employee.

Public School Employees' Retirement Contributions

The Commonwealth reimburses LEAs (school districts, intermediate units and area vocational-technical schools) for a portion of the employers' share of contributions to the Public School Employees' Retirement System (PSERS). This reimbursement is received by schools on a quarterly basis, and more specifically, five (5) days prior to the requirement that the schools make payment to PSERS. The payments are made in accordance with Section 8535 of Part 24 of the Pennsylvania Consolidated Statutes.

Special Education

Special Education programs are provided for exceptional children. The term "exceptional" includes both disabled and intellectually gifted children. School districts are required to provide special education classes for all school-aged students residing in their district. The funding formula for the school district operated special education programs is based on a factor multiplied by the average daily membership. There is also funding available for schools that experience extraordinary costs associated with special education programs, for intermediate units, and for the costs associated with the Cordero lawsuit. The Special Education subsidy formula payments are established by Section 2509.5 of the School Code.

Vocational Education

Funding is provided to support vocational education programs at both the school district and vocational-technical school level. Current law provides for a proportionate reduction in secondary vocational education program funding if the amounts appropriated is less than the total subsidy payments earned by all schools in the state.

The Vocational Education Subsidy is distributed to schools in a total of six (6) payments. The first five (5) payments are estimates and are calculated by multiplying each school's entitlement by 15 percent. These payments are issued on the last Thursday of August, October, December, February and April. The final payment is calculated by subtracting the total of the initial five (5) payments from the total of each school's entitlement. The final payment is made on June 1st. The Vocational Education subsidy formula payments are established by Section 2502.8 of the School Code.

Authority Rentals and Sinking Funds

When a school district undertakes a major construction project and seeks reimbursement from the Commonwealth, a process known as PlanCon is initiated. PlanCon is an acronym for Planning and Construction Workbook.

The Division of School Facilities in the Pennsylvania Department of Education reviews proposed school building projects including their plans and specifications, enrollments, building utilization and building condition. The Division also calculates state reimbursement for qualified school construction projects, and reviews and approves the financing for reimbursable projects. They are also responsible for approving reimbursement for charter school facility leases.

Unipay Cycle for State Subsidy Payments

The Unipay is an accumulation of state payments due to a school and processed once in a given month. Unipay's are received on the last Thursday of each month.

Federal Funding

Federal funding available to schools can come from a number of sources. Some of the federal funding sources are subsidies while others are competitive grants that require completion of applications.

Federal revenues have a Catalog of Federal Domestic Assistance (CFDA) number attached to each program and could be received from the federal government, state government, local government or other interim sources. When an LEA does not have a method for determining the prorated share of federal, state, and other sources of revenue in a commingled grant, the distributing agency should provide this information to each recipient. Questions concerning federal program funding should be directed to the program office in the respective granting agency.

The OCO is responsible for processing many federal grants and subsidy payments to public schools, non-public institutions, private institutions, institutions of higher education, charter schools, child and adult care centers, and food and nutrition sponsors.

The Pennsylvania Department of Education's web page www.education.pa.gov provides comprehensive information on grants, both federal and state. There are links provided to other related issues on this page.

Miscellaneous

A LEA may collect a variety of other revenues such as fines, fees, and charges. Since it is not practical to measure a number of these revenues, GASB's Codification, Section 1600.113 recommends that some miscellaneous revenues should be accounted for on a cash basis unless the measurable and available criteria can be satisfied. Miscellaneous revenues should be accounted for in the general fund. However, LEAs use an enterprise fund when a fee is charged to users in exchange for a service, i.e. cafeteria lunches.

Pass-Through Grants

GASB Codification N.50 addresses accounting for pass-through grants which are defined as grants and other financial assistance received by a governmental entity that is to be transferred or spent on behalf of a secondary recipient.

All cash pass-through grants received by a governmental entity (referred to as a recipient government) should be reported in its financial statements. As a general rule, cash pass-through grants should be recognized as revenue and expenditures or expenses in the funds of the primary government and in the government-wide financial statements. In those infrequent cases in which a recipient government serves only as a cash conduit, the grant should be reported in an agency fund. A recipient government serves only as a cash conduit if it merely transmits grantor-supplied monies without having administrative or direct financial involvement in the program. A recipient government has administrative involvement if, for example, it (a) monitors secondary recipients for compliance with program-specific requirements, (b) determines eligible secondary recipients or projects, even if using grantor-established criteria, or (c) has the ability to exercise discretion in how the funds are allocated. A recipient government has direct financial involvement if, for example, it finances some direct program costs because of a grantor-imposed matching requirement or is liable for disallowed costs. Please refer to the GASB Codification Section 1600.112 for additional information regarding expenditure driven grants.

Many grants are known as “expenditure-driven.” They are recognized when (1) qualifying expenditures are incurred and (2) other requirements are met, such as matching and maintenance of effort requirements (“MOE”). Grants are very specific as to the expending of the funds and each school is held accountable for the correct usage of the money. When grants and entitlements are received from another government, but the available and/or measurable criteria have not been met, the amount received should be recorded as “deferred inflows.” If no funds have been received and the available and measurable criteria have not been met, then no entry should be made. Do not use a special revenue fund to record grants and entitlements, unless the program specifically requires you to do so.

It is important to note that not all money passed to another entity is pass-through money. For example, transportation services purchased from another school or tuition paid to another school would not be considered pass-through money. These expenditures should be coded to the appropriate account established in the Chart of Accounts. Likewise, if you serve merely as a fiscal agent for money received, the expenditure should **not** be recorded; as defined in GASB Statement No. 24.

Particular notice must be taken when forming a consortium to disburse federal grant monies. The recipient government will book the total amount of the grant and code the disbursed amounts to #2990 – Pass-Thru Funds object 899. The secondary recipient will record the revenue to revenue account 6830 – Federal Revenue received from other Pennsylvania Public Schools or revenue 6821 – State Revenue received from other Pennsylvania Schools. The secondary recipient should record the expenditures in the appropriate sub-function / service area and funding source. These are federal expenditures and should be reported as such on the Annual Financial Report and Schedule of Expenditures of Federal Awards.

More information on pass-through grant accounting can be found in Accounting Bulletin #1998-01, Accounting for Pass-Through Grants and Other Shared, State and Federal Grants, which is available on the School Finance Section of PDE’s website.

Chapter 3: Overview of Fund Accounting

The Government Environment

As a local subdivision of the Commonwealth of Pennsylvania, LEAs, as well as other types of local governments, operate under a unique financial environment. These governments are financed in a variety of ways different from the private-sector; thus, requiring a different focus in accounting and financial reporting.

Most government services are financed through taxes and intergovernmental revenues. Taxation is used to finance government services when there has been a public policy decision that individual citizens should not be asked to pay for a given service based upon their use of that service. Intergovernmental revenues are often utilized by a larger government to finance local government services taking advantage of their broader tax base to raise revenues. These revenues are considered “nonexchange revenues” because there is no direct relationship between what an individual is asked to pay and the cost of the services received by that individual. When a service is largely funded through nonexchange revenues, it can be called a “governmental-type activity.”

When a service provided by a government receives a significant portion of its funding through user charges, it can be referred to as a “business-type activity.” These activities are similar to those found in the private sector. Traditionally, the type of financial information desired for governmental-type activities has not been the same as for business-type activities. Accordingly, governments report their business-type activities in a separate fund category. Also, the focus of financial reporting for business-type activities is quite different from the focus of financial reporting for governmental-type activities. Governments often hold or manage financial resources in an agent or fiduciary capacity. In this situation, the government operates in a trustee capacity or as an agent.

Another unique aspect to governmental finance is the need to ensure compliance to the numerous restrictions placed on specific resources utilized by governments. For example, management must only spend money with the approval of the Board of Directors. Federal grants are restricted to specific uses. Also, bond proceeds must only be expended for specific projects identified in the actual indenture. Governmental accounting and financial reporting have been adapted to demonstrate compliance with these legal requirements.

Each of the diverse situations described above and the necessity of legal compliance prevent a government from summarizing and reporting all financial transactions and balances in one category, as done with private business. Instead, a government is required to use “fund accounting” to report financial activity. Thus, from an accounting and financial management viewpoint, a governmental unit is a combination of separate accounting entities known as “funds.”

Fund Accounting

Fund accounting was developed as a governmental accounting standard in response to a demand for greater financial accountability on the part of state and local governments. As a result, a state or local government is not considered to be a single entity for accounting and financial reporting purposes, but rather a collection of separate funds. A fund is an accounting entity with a self-balancing set of accounts. Each fund has a separate trial balance, balance sheet, revenues and expenditures/expenses. A fund's purpose is to carry on a specific activity or certain objective and should be established to adhere to legal requirements, a specific project or goal, and to achieve good management.

GASB Codification Section 1100.104 states that governmental units should establish and maintain those funds required by law and that only the minimum number of funds consistent with legal and operating requirements should be established to avoid inflexibility, undue complexity, and inefficiency in financial administration.

Fund accounting does not require physical separation of cash and investments. The LEAs total cash and investment balance may be invested or deposited as one.

Government-Wide and Fund Financial Statements

GAAP requires governments to provide basic financial statements that include government-wide and fund financial statements. The government-wide statements should display information about the reporting government as a whole, except for its fiduciary activities. The statements should include separate columns for the governmental and business-type activities of the primary government as well as for its component units. Government-wide financial statements should be prepared using the economic resources measurement focus and the accrual basis of accounting.

GAAP requires that the government-wide financial statements be accompanied by separate sets of fund financial statements for governmental funds, proprietary funds, and fiduciary funds. The financial statements for proprietary funds and fiduciary funds use the same measurement focus and basis of accounting used for government-wide financial reporting. Because governmental funds have a different measurement focus, governmental fund financial statements must present reconciliation statements to explain differences between the data reported in the governmental funds and the data reported for the corresponding governmental activities in the government-wide financial statements.

Categories and Types of Funds

Three categories of funds are used in governmental accounting. There are a number of “fund types” within each of the three categories. Below is a summary of the three categories and the different fund types used by LEAs. Each fund category is also discussed in greater detail in later chapters.

Reference: GASB Codification Section 1300, NCGA-1

Governmental Funds

Governmental funds are the funds through which most LEA functions are typically financed. The focus is for reporting the sources, uses and balances of current financial resources. Expendable assets are used to pay for current liabilities. The difference between assets and liabilities is fund balance.

The financial statements required for governmental funds are a balance sheet and a statement of revenues, expenditures, and changes in fund balances. Financial statements for governmental funds should be presented using the *current financial resources measurement focus* and the *modified accrual basis of accounting*.

The following fund types are used to account for a government's governmental-type activities.

General Fund

The general fund should be used to account for and report all financial resources unless there is a legal or other compelling reason to use another fund type.

Special Revenue Funds

Special revenue funds account for and report the proceeds of specific revenue sources that are limited to specific expenditures. These revenue sources must provide a "substantial" amount of the funding accounted for in a special revenue fund. The standard further limits the use of this fund to expenditures that are not related to capital outlay or debt service.

Capital Projects Funds

Capital projects funds account for and report financial resources that are restricted, committed, or assigned to expenditures for capital outlays. Types of expenditures made from this fund include the acquisition of capital facilities and other capital assets.

Debt Service Funds

Debt service funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditures for principal and interest. This fund should also be used to accumulate the resources to make future debt service payments.

Permanent Funds

Permanent funds should be used to account for and report resources that are restricted to the extent that only earnings, and not principal, may be used to benefit the reporting government.

Proprietary Funds

Proprietary fund reporting focuses on business-type activities for the determination of operating income, changes in net position, and cash flows. Required financial statements for proprietary funds are a statement of net position; a statement of revenues, expenses, and changes in fund net position; and a statement of cash flows. Proprietary fund statements of net position and revenues, expenses, and changes in fund net position should be presented using the *economic resources measurement focus* and *the accrual basis of accounting*. The proprietary fund category includes enterprise and internal service funds.

Enterprise Funds

Enterprise funds may be used to report any activity for which a fee is charged to external users for goods or services. These funds are used to report operations that are financed and operated in a manner similar to private businesses.

Internal Service Funds

Internal service funds may be used to report any activity that provides goods or services to other funds, departments, or agencies of the primary government and its component units, or to other governments, on a cost-reimbursement basis. Internal service funds should be used only if the reporting government is the predominant participant in the activity. Otherwise, the activity should be reported as an enterprise fund.

Fiduciary Funds

Fiduciary funds should be used to report assets held in a trustee or agency capacity for others and therefore cannot be used to support the government's own programs.

Required financial statements for fiduciary funds are the statement of fiduciary net position and the statement of changes in fiduciary net position. Financial statements of fiduciary funds should be reported using the *economic resources measurement focus* and the *accrual basis of accounting*. The fiduciary fund category includes pension (and other employee benefit) trust funds, investment trust funds, private-purpose trust funds, and agency funds.

Pension Trust Funds

Pension trust funds should be used to report resources that are required to be held in trust for the members and beneficiaries of defined benefit pension plans, defined contribution plans, other postemployment benefit plans, or other employee benefit plans.

Investment Trust Funds

Investment trust funds should be used to report the external portion of investment pools reported as required by GASB Statement No. 31, Paragraph 18.

Private Purpose Trust Funds

Private purpose trust funds should be used to report arrangements for bequests and other arrangements where the use of principal and earnings is restricted and the beneficiaries are outside the government.

Agency Funds

Agency funds should be used to report resources held by the reporting government in a purely custodial capacity. Agency funds have no equity balances (assets equal liabilities).

Note: The use of trust funds is only appropriate when resources are legally restricted. The Government Finance Officers Association (GFOA) recommends that trust funds only be used in cases where there is a written trust agreement with a party outside of the government.

Measurement Focus

The “measurement focus” determines: (1) which assets and which liabilities are included on a government’s balance sheet, and (2) whether an operating statement presents information on the flow of financial resources (revenues and expenditures) or information on the flow of economic resources (revenues and expenses).

For example, governmental funds use a “flow of current financial resources” measurement focus. The operating statement of a governmental fund answers the question, “Are there more or less resources that can be spent in the near future as a result of events and transactions of the period?” Increases in spendable resources are reported in the operating statement as “revenues” or “other financing sources.” Decreases in spendable resources are reported as “expenditures” or “other financing uses.”

The operating statement of a proprietary fund is designed to answer the question “Is the fund better or worse off economically as a result of events and transactions of the period?” Events and transactions that improve the economic position of a proprietary fund are reported as “revenues” or “gains” in the operating statement. Those that diminish the economic position of a proprietary fund are reported as “expenses” or “losses.”

Measurement Focus

	Governmental Funds	Proprietary & Fiduciary Funds
Measurement Focus	Flow of current financial resources	Flow of economic resources
Fundamental Question	More or less resources to spend in the near future	Better or worse off economically
Terminology for Increases	Revenues/Other Financing Sources	Revenues/Gains
Terminology for Decreases	Expenditures/Other Financing Uses	Expenses/Losses

Practical effects of the difference of measurement focus between governmental and proprietary funds.

Transaction	Governmental Funds	Proprietary & Fiduciary Funds
Does the fund report the receipt of proceeds from long-term borrowings in the operating statement?	Yes	No
Does the fund report capital outlay in the operating statement?	Yes	No
Does the fund report the repayment of the principal of debt in the operating statement?	Yes	No
Does the fund report a charge for consumption of capital assets (i.e., depreciation)?	No	Yes
Does the fund defer and amortize disbursements over the benefiting period?	No*	Yes

**Exceptions are prepaid items and inventories accounted for using the “consumption” method.*

Basis of Accounting

According to GASB Codification Section 1600.101 the basis of accounting refers to the timing of *when* transactions are recognized in the accounts and reported in the financial statements. The basis of accounting is used to determine when an accounting entry should be made. Different funds use different bases of accounting, in accordance with governmental accounting standards. The three recognized bases of accounting are:

Basis of Accounting

	Accrual Basis	Modified Accrual Basis	Cash Basis *
Timing of Revenue Recognition	When earned, or an inflow is reasonably certain to be collected	When measurable and available **	When received in cash
Timing of Expenditure/Expense Recognition	When the cost is incurred	When the expenditure is incurred, if measurable. Interest on debt is recognized when it is due. Claims, judgments and compensated absences are recognized in the year they are liquidated from expendable available resources	When paid in cash

* NCGA Statement 1 concludes that this is not an appropriate basis of accounting and reporting for governmental organizations.

** “**Measurable**” means revenues subject to reasonable estimation. “**Available**” means revenues are subject to collection within the current period or after the end of the period, but in time to pay liabilities outstanding at the end of the current period.

Revenues and other governmental fund financial resource increments (for example, bond issue proceeds) are recognized in the accounting period in which they become susceptible to accrual—that is, when they become both measurable and available to finance expenditures of the fiscal period. Application of the "susceptibility to accrual" criterion requires judgment, consideration of the materiality of the item in question, and due regard for the practicality of accrual, as well as consistency in application. The length of time used to define available for purposes of revenue recognition in the governmental fund financial statements should be disclosed in the summary of significant accounting policies.

Cash and Accrual Bases

Under the cash basis of accounting, revenues and transfers in are not recognized until cash is received, and expenditures or expenses (as appropriate) and transfers out are recognized only when cash is disbursed. Under the accrual basis of accounting, most transactions are recognized when they occur, regardless of when cash is received or disbursed. Items not practicably measurable until cash is received or disbursed are accounted for at that time using either basis of accounting, as may be items whose measurement would be approximately the same under either basis or that are immaterial.

Accrual Basis Reporting in Government-wide Financial Statements

The statement of net position and the statement of activities should be prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions should be recognized when the exchange takes place. Revenues, expenses, gains, losses, assets, and liabilities resulting from nonexchange transactions should be recognized in accordance with the requirements of GASB Codification Section N50.

Modified Accrual Basis in Governmental Fund Statements

The major differences in applying the accrual concept in governmental fund accounting, as opposed to that used in government-wide financial statements and proprietary and fiduciary fund statements, relate to differences in the environment and in the accounting measurement objectives. These modifications and adaptations for the practical and appropriate implementation of the accrual concept in governmental fund accounting are best referred to as the "modified accrual basis" and should be applied in all governmental funds accounting and reporting.

Measurement Focus and Basis of Accounting by Fund

FUND CATEGORY	FUND TYPE	DEFINITION	MEASUREMENT FOCUS	BASIS OF ACCOUNTING
Governmental	General	To account for all governmental resources except those required to be accounted for elsewhere	Current financial resources flow (revenues and expenditures)	Modified Accrual
Governmental	Special Revenue	To account for the proceeds of specific revenue sources that are limited to specific expenditures; These revenue sources must provide a "substantial" amount of the funding	Current financial resources flow (revenues and expenditures)	Modified Accrual
Governmental	Capital Projects	To account for financial resources that is limited to expenditures for capital outlays	Current financial resources flow (revenues and expenditures)	Modified Accrual
Governmental	Debt Service	To accumulate, account for and report financial resources used for debt service payments	Current financial resources flow (revenues and expenditures)	Modified Accrual
Governmental	Permanent	To report resources that are legally restricted to the extent that only earnings and not principal may be used for the benefit of the government	Current financial resources flow (revenues and expenditures)	Modified Accrual
Proprietary	Enterprise	To account for operations financed and operated similar to businesses-services rendered to general public on a fee basis	Economic resources flow (capital maintenance) (revenues and expenses)	Accrual
Proprietary	Internal Service	To account for the financing of goods or services provided by one department or unit to another department or to other governmental units on a cost reimbursement basis	Economic resources flow (capital maintenance) (revenues and expenses)	Accrual
Fiduciary	Trust	To account for assets held by a governmental unit in a trustee capacity	Economic resources flow	Accrual
Fiduciary	Agency	To account for assets held by a governmental unit in a purely custodial capacity	Economic resources flow	Accrual

Recognition of Nonexchange Transactions

GASB Codification Section N50 establishes accounting and financial reporting standards for nonexchange transactions involving financial or capital resources (for example, most taxes, grants and private donations). The principal issue addressed in the statement is the *timing of recognition* of nonexchange transactions – that is, *when* (in which fiscal year) should they be recognized in the financial statements.

In an **exchange** transaction, each party receives and gives up essentially equal values. Revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions should be recognized when the exchange takes place. However, in a **nonexchange** transaction a government gives (or receives) value without directly receiving (or giving) equal value in return.

There are two kinds of stipulations on the use of resources; timing requirements and purpose restrictions for nonexchange transactions. **Time requirements** may be imposed that specify (1) the period when resources are required to be used or when use may begin or (2) that the resources are required to be maintained intact until a specified date or event has occurred. For revenue recognition to occur on the modified accrual basis, all applicable eligibility requirements must be met **and** the resources must be available and measurable. **Purpose restrictions** specify the purpose for which resources are required to be used. They should not affect when nonexchange transactions are recognized. However, if a government receives resources with purpose, restrictions should report resulting net assets, equity, or fund balance as restricted.

There are four (4) classes of nonexchange transactions:

1. *Derived tax revenues* resulting from assessments imposed on exchange transactions (for example, income taxes and other assessments on earnings or consumption).
2. *Imposed nonexchange revenues* result from assessments imposed on nongovernmental entities, including individuals, other than assessments on exchange transactions (for example, property taxes and fines).
3. *Government-mandated nonexchange transactions*, which occur when a government at one level provides resources to a government at another level and requires the recipient to use the resources for a specific purpose (for example, federal programs that state or local governments are mandated to perform).
4. *Voluntary nonexchange transactions*, which result from legislative or contractual agreements, other than exchanges, entered into willingly by the parties to the agreement (for example, certain grants and private donations).

Basis of Accounting for Nonexchange Transactions

All standards in GASB Section N50 apply whether the accrual basis or the modified accrual basis of accounting is required, except for the revenue recognition standards. (When the modified accrual basis of accounting is used for governmental funds in the fund financial statements, the requirements of this section for the recognition of expenses should be interpreted as requirements for the recognition of expenditures).

On either basis of accounting, recognition of nonexchange transactions in the financial statements is required unless the transactions are not measurable (reasonably estimable) or are not probable of collection. Transactions that are not recognizable because they are not measurable should be disclosed.

GASB Section N50 contains many examples on the application of accrual accounting to nonexchange transactions. The following chart from Section N50 summarizes the four classes of nonexchange transactions and the timing of recognition required for each class.

Classes and Timing of Recognition of Nonexchange Transactions

CLASS	RECOGNITION
<p>Derived Tax Revenues</p> <p>Examples: sales taxes, personal and corporate income taxes, motor fuel taxes, and similar taxes on earnings or consumption</p>	<p>Assets</p> <p>Period when <i>underlying exchange has occurred</i> or when resources are received, whichever is first.</p> <p>Deferred inflows of resources</p> <p>When modified accrual accounting is used, resources that are not “available.”</p> <p>Revenues</p> <p>Period when <i>underlying exchange has occurred</i>. (Report advance receipts as deferred revenues.) When modified accrual accounting is used, resources <i>also</i> should be “available.”</p>
<p>Imposed Nonexchange Revenues</p> <p>Examples: property taxes, most fines and forfeitures</p>	<p>Assets</p> <p>Period when an enforceable legal claim has arisen or when resources are received, whichever is first.</p> <p>Deferred inflows of resources</p> <p>When resources are received or recognized as receivable before (a) the period for which property taxes are levied or (b) the period when resources are required to be used or when use is first permitted for all other imposed nonexchange revenues in which enabling legislation includes time requirements. When modified accrual accounting is used, resources that are not “available.”</p> <p>Revenues</p> <p>Period when resources are required to be used or first period that use is permitted (for example, for property taxes, the period for which levied). When modified accrual accounting is used, resources should be “available.” (For property taxes, apply Section P70)</p>
<p>Government-Mandated Nonexchange Transactions</p> <p>Examples: federal government mandates on state and local governments</p>	<p>Recipients:</p> <p>Assets</p> <p>Period when all eligibility requirements have been met.</p> <p>Liabilities</p> <p>Receipt of resources before eligibility requirements are met, excluding time requirements.</p> <p>Deferred inflows of resources</p> <p>Receipt of resources before time requirements are met, but after all other eligibility requirements have been met. When modified accrual accounting is used for revenue recognition, resources that are not “available.”</p>
<p>Voluntary Nonexchange Transactions</p> <p>Examples: certain grants and entitlements, most donations</p>	<p>Revenues</p> <p>Period when all eligibility requirements have been met. However, when a provider precludes the sale, disbursement, or consumption of resources for a specified number of years, until a specified event has occurred, or permanently (for example, permanent and term endowments), report revenues when the resources are received and report resulting net position or fund balance as restricted. When modified accrual accounting is used for revenue recognition, resources also should be “available.”</p> <p>Providers:</p> <p>Assets</p> <p>Payment of resources before eligibility requirements are met, excluding time requirements.</p> <p>Liabilities</p> <p>Period when <i>all eligibility requirements have been met</i>.</p> <p>Deferred outflows of resources</p> <p>Payment of resources before time requirements are met, but after all other eligibility requirements have been met.</p> <p>Expenses or expenditures</p> <p>Period when all eligibility requirements have been met. However, when a provider precludes the sale, disbursement, or consumption of resources for a specified number of years, until a specified event has occurred, or permanently (for example, permanent and term endowments), report expenses or expenditures when the resources are paid.</p>

Interfund Activity

Interfund Activity is defined as transactions within and among the three fund categories (governmental, proprietary, and fiduciary) and are classified as revenue expenditure/ expense within the individual funds, but not to the LEA overall. GASB Codification 1800.102 divides the transactions into reciprocal and nonreciprocal activity.

Reciprocal Interfund Activity

Reciprocal interfund activity describes situations involving the exchange of equal or almost equal value between funds. It is the internal counterpart to exchange and exchange-like transactions. There are different types of reciprocal interfund activity: interfund loans and interfund services provided and used. *Interfund loans* — amounts provided with a requirement for repayment. Interfund loans should be reported as interfund receivables in lender funds and interfund payables in borrower funds. This activity should not be reported as other financing sources or uses in the fund financial statements. If repayment is not expected within a reasonable time, the interfund balances should be reduced and the amount that is not expected to be repaid should be reported as a transfer from the fund that made the loan to the fund that received the loan.

Interfund Services Provided and Used (Quasi-external Transactions)

Interfund activity includes sales and purchases of goods and services between funds for a price approximating their external exchange value. Interfund services provided and used should be reported as revenues in seller funds and expenditures or expenses in purchaser funds. Unpaid amounts should be reported as interfund receivables and payables in the fund balance sheets or fund statements of net position. The quasi-external transaction is tantamount to the existence of a buyer-seller relationship. For example, charges for utilities or data processing provided by one fund to another fund, as if the provider of the utilities or data processing were in the business of providing such products or services.

The enterprise fund bills the general fund \$5,000 for services rendered and is unpaid, the quasi-external transactions would be recorded as follows:

Example:

General Fund

Expenditures	\$ 5,000	
Due To Other Funds – Enterprise Fund		\$ 5,000

Enterprise Fund

Due from Other Funds – General Fund	\$ 5,000	
Revenues		\$ 5,000

Nonreciprocal Interfund Activity

Nonreciprocal interfund activity describes situations that do not involve the exchange of equal or almost equal value between funds. It is the internal counterpart to nonexchange transactions. It includes:

Interfund Transfers

Interfund transfers are flows of assets (such as cash or goods) without equivalent flows of assets in return and without a requirement for repayment. This category includes payments in lieu of taxes that are not payments for, and are not reasonably equivalent in value to, services provided. In governmental funds, transfers should be reported as other financing uses in the funds making transfers and as other financing sources in the funds receiving transfers. In proprietary funds, transfers should be reported after non-operating revenues and expenses as discussed in GASB Codification Section P80 paragraphs .115 and .116.

Interfund Reimbursements

Interfund Reimbursements are repayments from the funds responsible for particular expenditures or expenses to the funds that initially paid for them. Interfund reimbursements are reported as an expenditure/expense in the fund ultimately responsible and as a reduction of expenditure/expense in the fund being reimbursed. Interfund reimbursements are not to be confused with interfund transfers, revenues, advances, or loans.

Example:

- When the general fund is the reimbursed fund – reimbursement occurs in the same year. Record the initial payment as an expenditure in the general fund. No entry is made in the reimbursing fund. When the reimbursing fund reimburses the general fund, the general fund reduces its expenditures by the amount received. The reimbursing fund then recognizes the expenditure or expense.

The general fund pays a utility bill of \$20,000 for the cafeteria fund. The initial payment is recorded in the general fund as:

General Fund

Expenditures – Utilities	\$ 20,000	
Cash		\$ 20,000

Cafeteria Fund

No Entry

When the cafeteria fund *reimburses* the general fund, the general fund reverses its original entry:

General Fund

Cash	\$ 20,000	
Expenditures – Utilities		\$ 20,000

Cafeteria Fund

Expenditures – Utilities	\$ 20,000	
Cash		\$ 20,000

- Same as above, except the general fund is not reimbursed until the following year:

End of Year, general fund not yet reimbursed by cafeteria fund:

General Fund

Due from other funds	\$ 20,000	
Expenditures – Utilities		\$ 20,000

Cafeteria Fund

Expenditures – Utilities	\$ 20,000	
Due to Other Funds		\$ 20,000

- Cafeteria fund reimburses general fund in the following year:

General Fund

Cash	\$ 20,000	
Due from other funds		\$ 20,000

Cafeteria Fund

Due to other funds	\$ 20,000	
Cash		\$ 20,000

Due To/Due From

Other balances owed between funds, whether resulting from quasi-external transactions or interfund reimbursement transactions, are reported as follows: ‘due from other funds’ for the receivable and ‘due to other funds’ for the payable.

Due to Other Funds is a liability account that reflects amounts owed to another fund for goods sold or services rendered. These amounts include only short-term obligations on open accounts, not interfund loans.

Due from Other Funds is an asset account used to indicate amounts owed from a particular fund by another fund for goods sold or services rendered. This account includes only short-term obligations on open accounts, not interfund loans.

Chapter 4

Governmental Fund Overview

Nature and Purpose

Governmental fund reporting focuses primarily on the sources, uses, and balances of current financial resources and often have a budgetary orientation. The governmental fund category includes the general fund, special revenue funds, capital projects funds, debt service funds, and permanent funds.

Governmental funds are, in essence, accounting segregations of financial resources. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used; current liabilities are assigned to the fund from which they are to be paid.

Number of Funds

General Fund: A Government will report only one general fund; however, for practical purposes it may be convenient to maintain separate and distinct components of the general fund, but all components must be combined for reporting purposes. The Government may choose to maintain federal program expenditures separate from its general operations. Although separate components may be maintained, each component is subject to board control and the laws and regulations governing general fund operations.

Other Funds: Some governmental units often need several funds of a single type, such as special revenue or capital projects funds. On the other hand, many governmental units do not need funds of all types at any given time.

Basis of Accounting and Measurement Focus

Financial statements for governmental funds should be presented using the current financial resources measurement focus and the modified accrual basis of accounting. The governmental fund measurement focus is on the determination of financial position and changes in financial position (sources, uses, and balances of financial resources).

Governmental Fund Financial Statements

Balance Sheet

Governmental funds contain only “current” assets and “current” liabilities.

- Assets – Current assets are expected to be received within one-year from the balance sheet date.

Governmental funds report cash, and assets that convert to cash in due course – receivables, investments, and assets acquired with the intent of resale. Governments also may report supplies inventories and prepayments as assets in governmental funds. Governmental funds do not report assets used in operations.

A clear distinction should be made between general capital assets and capital assets of proprietary and fiduciary funds. Capital assets of proprietary funds should be reported in both the government-wide and fund financial statements. Capital assets of fiduciary funds (and similar component units) should be reported only in the statement of fiduciary net position. All other capital assets of the governmental unit are general capital assets. They should not be reported as assets in governmental funds but should be reported in the governmental activities column in the government-wide statement of net position.

- Deferred Outflows of Resources – A deferred outflow of resources is a consumption of net assets by the government that is applicable to a future reporting period.

Note: GASB Statement No. 63 established financial reporting of Deferred Outflows/Inflows of Resources and states that recognition of deferred outflows/inflows of resources should be limited to those instances identified by the GASB in authoritative pronouncements procedures. GASB Statement No. 65 identifies those items previously reported as assets and liabilities which should be reported as deferred outflows/inflows.

For example, items previously reported as deferred revenues (assets recorded in governmental fund financial statements where the revenue is not available) are reported as a deferred inflow of resources until such time as the revenue becomes available.

- Liabilities – Current liabilities are expected to be paid within one year from the balance sheet date. Consistent with the flow of current financial resources measurement focus required for governmental fund financial statements, governmental financial reporting standards include criteria for distinguishing the portions of liabilities incurred by the government that should be reported as:
 - Governmental fund liabilities (claims against current financial resources)
 - General long-term liabilities of the government

Governments, in general, are normally expected to liquidate liabilities with expendable available financial resources to the extent that the liabilities mature (come due for payment) each period. For all types of expenditures to which this criterion applies, the criterion for modified accrual recognition is whether and to what extent the liability has matured independent of the method and timing of resource accumulation.

Governmental fund liabilities and expenditures for debt service on general long-term debt, including capital leases, generally should be recognized when due—that is, to the extent that portions of the debt mature during the reporting period.

- Deferred Inflows of Resources - A deferred inflow of resources is an acquisition of net assets by the government that is applicable to a future reporting period.
- Fund Balance - The equity for governmental funds is known as a “fund balance.” The calculation for fund equity may be reduced to a mathematical equation written as:

$$\text{Assets} + \text{Deferred Outflows of Resources} = \text{Liabilities} + \text{Deferred Inflows of Resources} + \text{Fund Balance}$$

The fund balance of the general fund is of significance because it is the primary fund through which most functions are financed and which includes state aid and local taxes.

Governmental fund balances do not always represent cash in the bank or funds available for expenditures. They report up to five different components of fund balance, presented from most constraining to least constraining. Accordingly, it is necessary to determine the constraints on how resources can be spent and the resources of constraints to classify what portions of the gross fund balance pertain to:

- 0810 Non-spendable Fund Balance
Amounts that cannot be spent because they are either in a non-spendable form, or are in spendable form, but are legally or contractually required to be maintained in tact such as inventory, or principal of a permanent fund.
- 0820 Restricted Fund Balance
Amounts constrained to be used for a specific purpose as per external parties or legislation.
- 0830 Committed Fund Balance
Amounts constrained to be used for a specific purpose as per government's highest level of decision making authority such as the school board, board of directors, board of trustees, etc.
Note: Board Resolution required. Constraint can also be removed or changed by an equal level action.
- 0840 Assigned Fund Balance
Amounts intended to be used for a specific purpose as per a committee or individual authorized by the governing body. These amounts are not restricted or committed.
- 0850 Unassigned Fund Balance
A residual classification for the general fund representing the amount that has not been assigned to other funds, and that has not been restricted, committed, or assigned to specific purposes within the general fund. Amounts are available for any purpose within the general fund only. Other governmental funds, by their nature would automatically require that funds be classified as non-spendable, restricted, committed or assigned. In the event that a fund, other than the general fund has expenditures that exceed revenues, the unassigned fund balance category may be used to report a negative ending fund balance only.

Reference: GASB Statement No. 54

Statement of Revenues, Expenditures, and Changes in Fund Balance

Perhaps the most distinctive and significant aspect of governmental fund accounting is that the operations measurement focus is on sources, uses, and balances of fund financial resources. In this context, the term **revenues** mean increases in (sources of) fund financial resources other than from interfund transfers and the debt issue proceeds and redemptions of demand bonds; and the term **expenditures** mean decreases in (uses of) fund financial resources other than through interfund transfers and expirations of demand bond takeout agreements. Revenue and expenditure accounts thus reflect the changes in the financial condition of a governmental fund that occur during a given time period except those arising from transfers and debt transactions.

- Revenues – Revenues represent increases in current financial resources. Revenues are recognized in the accounting period in which they become susceptible to accrual – that is when they become both measurable and available to finance expenditures of the fiscal period. "Available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Application of the "susceptibility to accrual" criterion requires judgment, consideration of the materiality of the item in question, and due regard for the practicality of accrual, as well as consistency in application. The length of time used to define available for purposes of revenue recognition in the governmental fund financial statements should be disclosed in the summary of significant accounting policies.
- Expenditures – The measurement focus of governmental fund financial statements is on expenditures—decreases in net financial resources—rather than expenses. Most expenditures and transfers out are measurable and should be reported when the related liability is incurred.

Modified Accrual Recognition of Liabilities and Expenditures

GASB Codification Section 1600.116 requires that a government accrue a governmental fund liability and expenditure for most expenditures and transfers in the period in which the government incurs the liability (**general rule**). Section 1600.119 further states that in the absence of an explicit requirement to do otherwise (**exception to the general rule**) a government should accrue a governmental fund liability and expenditure in the period in which the government incurs the liability. Governmental fund liabilities and expenditures that should be accrued include liabilities that, once incurred, normally are paid in a timely manner and in full from current financial resources

Exceptions to the General Rule

- Long-term debt

The major exception to the general rule of expenditure accrual, stated in paragraph .116, relates to unmatured principal and interest on general long-term debt, which includes special assessment debt for which the government is obligated in some manner. Governmental fund liabilities and expenditures for debt service on general long-term debt, including capital leases, generally should be recognized *when due*—that is, to the extent that portions of the debt mature during the reporting period.

- Other Long-term liabilities

Governmental fund liabilities and expenditures for claims and judgments, compensated absences, termination benefits, landfill closure, and post-closure care costs, and receipts of goods and services for pollution remediation should be recognized to the extent the liabilities are "normally expected to be liquidated with expendable available financial resources." Governments, in general, are normally expected to liquidate liabilities with expendable available financial resources to the extent that the liabilities *mature* (come due for payment) each period.

- Other expenditure recognition alternatives

Other alternative expenditure recognition methods in governmental fund accounting, usually of a relatively minor nature, include:

- Inventory items (for example, materials and supplies) may be considered expenditures either when purchased (purchases method) or when used (consumption method), but significant amounts of inventory should be reported in the balance sheet.
 - Expenditures for insurance and similar services extending over more than one accounting period need not be allocated between or among accounting periods, but may be accounted for as expenditures of the period of acquisition.
- Other Financing Sources (Uses) – Includes items such as the cash received when bonds are issued and debt service payments as well as transfers between funds. Due to the fact that these resource flows are not revenues or expenditures, they are shown separately to assist the reader of the statement in assessing the balance between ongoing revenues and expenditures related to the basic operations of the government.
- Special and Extraordinary Items – Special items are either unusual or infrequent and are within the control of the government. Extraordinary items are increases or decreases in fund balance that are both (a) unusual in nature and (b) infrequent in occurrence and are seldom in control of the government. Extraordinary items, as their name implies, do not appear in the financial statements very often.
- Changes in Fund Balance – Revenues minus expenditures plus or minus total other financing sources (uses) plus or minus extraordinary and special items equals fund balance. This amount is added to the fund balances as of the beginning of the fiscal year (generally the same amount reported as the ending fund balance for the previous year) to arrive at the ending fund balance amounts. These must match the total fund balances reported in the balance sheet.

Types of Governmental Funds

General Fund

Nature and Purpose

A general fund is used to account for all financial resources, except for those resources that may be accounted for in a different fund for nonspecific or legal reasons. A government must have and may only maintain one general fund.

This fund typically has a greater number and variety of revenue sources than other funds and its resources finance a wide range of activities. It is established at the inception of the LEA and continues to exist throughout the life of the school system.

The general fund is financed from local, state, and federal sources. These revenues are generally used for financing the current, ordinary, normal, and recurring operations of the LEA such as programs of instruction for the students, maintenance, data processing, printing, and pupil transportation.

Revenues

General fund revenues are recognized when measurable and available. Many general fund revenues are measurable, such as taxes, grants, and fees. Since accounting standards do not specify a time frame for all revenues to be classified as “available,” judgment must be used in determining when to recognize an item as revenue. Materiality as well as consistency in revenue transactions from year to year must be considered in this determination.

Pennsylvania LEAs:

*Determining when revenues are available has caused some confusion for LEAs in the past. “Available” has been interpreted as one year, 90 days, 60 days, as well as other time frames. Codification Section P70 provides some guidance when recording property taxes and states that amounts collected within 60 days after the year-end which are used to finance current-period expenditures be recorded as available. **Unfortunately, this guidance only applies to property taxes.***

Expenditures

Expenditures are decreases in fund financial resources. Some examples of general fund expenditures are current operations and repayment of principal and interest on long-term debt. Interfund transfers are not classified as expenditures, but instead are reported as “other financing uses.” Depreciation and amortization are not expenditures within the general fund. Expenditures are generally accrued when incurred if the transaction results in a reduction of the general fund’s current financial resources. However, expenditures for long-term debt, principal, and related interest are recognized when they are due. Do not record an expenditure if there is not a reduction in the fund’s current financial resources. For example, an LEA may estimate a liability for compensated absences, but if the actual payments to employees are expected to be made after the current fiscal year, the expenditure would not be reported in the general fund at year-end. Expenditures are classified by function and object in accordance with the Chart of Accounts. The major classifications of expenditures are:

- Instruction
- Support Services
- Non-instructional Services
- Facilities Acquisition, Construction, and Improvement

Other Financing Sources/Uses

When long-term debt is issued and the proceeds are available to the general fund, the proceeds should be recorded as part of “other financing sources.” These proceeds should not be reported under the general fund’s operating revenues. Although bond proceeds are reported in the general fund, the long-term debt is reported in the non-current liabilities section on the government-wide statement of net position, not the general fund.

If short-term debt is issued by the general fund, i.e. debt to be paid off in one year or less, the debt liability is recorded in the general fund because the payment of the debt will require current resources.

Specific Revenue Examples

Property Taxes

GASB Codification Section P70 addresses the application of the Modified Accrual Basis of Accounting to Property Taxes.

Current Recognition

When a property tax assessment is made, it is to finance the budget of a particular period, and the revenue produced from any property tax assessment should be recognized in the fiscal period for which it was levied, provided the "available" criteria are met. Available means collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Such time thereafter **shall not exceed 60 days**. Governments should disclose in their summary of significant accounting policies the length of time used to define available for purposes of revenue recognition in the governmental fund financial statements. If, because of unusual circumstances, the facts justify a period greater than 60 days, the governmental unit should disclose the period being used and the facts that justify it.

Examples:

Current Recognition (Measurable & Available)

- Property Taxes Levied

\$400,000 is levied in property taxes during the current year. There is a history of 7.5% (\$30,000 in this case) being uncollectible.

Taxes Receivable	\$400,000	
Revenue – Current R/E Taxes		\$370,000
Estimated Uncollectible Taxes		\$30,000

- Collections & Write-offs

Current collections -- \$350,000 is collected in property taxes during the year and \$20,000 is uncollectible.

Cash	\$350,000	
Estimated Uncollectible Taxes	\$ 20,000	
Taxes Receivable		\$370,000

- Revenue deferred for amount of taxes that do not meet the revenue recognition definition of available at end of fiscal period (60 days).

\$4,000 receivable will not be collected until 90 days after the fiscal year-end.

Revenues – Current R/E Taxes	\$4,000	
Deferred Inflow		\$4,000

Receivable Recognition

Governments should recognize assets from imposed non-exchange revenue transactions in the period when an enforceable legal claim to the assets arises or when the resources are received, whichever occurs first. For property (ad valorem) taxes, the date when an enforceable legal claim to taxable property arises generally is specified in the enabling legislation. Many governments refer to this date as the "lien date," even though a lien is not formally placed on the property at that date. Some governments, however, use a different term, such as the "assessment date." (For some governments, the enforceable legal claim does not arise until the period after the period for which the taxes are levied. Those governments should recognize property taxes receivable in the same period that revenues are recognized in accordance with GASB Codification Section N50, *paragraph .115.*)

Examples:

Receivable Recognition - Taxes Levied (Measurable but not available)

- Property taxes levied:

Taxes Receivable	\$400,000	
Estimated Uncollectible		\$ 30,000
Deferred Inflow		\$370,000

- Collections:

Cash	\$350,000	
Taxes Receivable		\$350,000
Deferred Inflow	\$350,000	
Revenue – Current R/E Taxes		\$350,000

Remember:

Recognize taxes receivable to be collected within 60 days as revenue; defer the remaining balance.

Uncollectible Taxes

Property taxes receivable that is susceptible to accrual should be recognized in the accounts, reduced by an allowance for uncollectible taxes receivable.

Recognition of Deferred Inflows of Resources

When property taxes receivable are recognized, or when property taxes are collected in advance of the period for which they are levied, they should be recorded as deferred inflow of resources and recognized as revenue in the period for which they are levied, subject to the "available" criterion.

Disclosure

Details of the governmental unit's property tax calendar, including lien dates, levy dates, due dates, and collection dates, should be disclosed in the notes to the financial statements.

Tax Discounts

An LEA may offer tax discounts to taxpayers who pay before a specified date. An allowance of such discounts may be established at the levy date. Discounts actually taken should be charged against this allowance

Examples:

- To record the property tax levy, estimated net revenues, uncollectible, and discounts:

Property Taxes Receivable	\$1,000,000	
Allowance for Uncollectible Taxes		\$100,000
Allowance for Discount on Taxes		\$7,000
Property Tax Revenues		\$893,000

- As discounts are taken, the following entry would be made to record the collection of property taxes and discounts taken:

Cash	\$495,000	
Allowance for Discount on Taxes	\$5,000	
Property Taxes Receivable		\$500,000

Delinquent Property Taxes

Taxes not paid by the due date on the bill are delinquent. The amount of taxes remaining in "taxes receivable – current year" should be transferred to "taxes receivable – delinquent." If you maintain separate "allowance for uncollectible taxes" by year, then this account should also be transferred from a current account, to a delinquent account.

Delinquent taxes are usually subject to penalties and interest charges. The cash collection of interest and penalties is similar to the collection of the property taxes.

Taxes Paid In Protest

All taxes paid in protest should be recorded in the general fund of the LEA.

The Chart of Accounts provides a balance sheet account – Taxes Held in Escrow to recognize taxes paid under protest. This account is a liability account and is used for the following purposes.

- Credit (increase) this account with the amount of taxes collected under protest.
- Debit (decrease) this account with the amounts involved when cases under protest are settled.

The credit balance in this account represents at any time the amount of taxes held in escrow for which disposition remains unsettled.

Protested taxes are recorded as a credit (increase) to the appropriate tax revenue account and a debit (decrease) to the taxes held in escrow liability account when the case is resolved in favor of the school district. If the case is resolved in favor of the taxpayer, the protested taxes are recorded as a debit (decrease) to account – Taxes Held in Escrow and an offsetting credit to account – Cash.

Further, if the case is resolved in favor of the school district in a year subsequent to the year of tax, the credit entry should be recorded to tax revenue account – Delinquent Taxes.

Protested taxes recorded in account – Taxes Held in Escrow are not recognized as tax revenue by the district, and therefore, do not become a part of the district’s fund balance.

Examples:

- Taxes due are paid in full amount

Full amount of tax due \$1,200 for Fiscal Year 2x1-x2 were paid under protest on 10/31/10. School district was notified by the tax collector that the taxes were paid with a written protest in accordance with 72 Purdon’s, Section 5020–518.1.

Cash	\$1,200.00	
Taxes Held in Escrow		\$300.00
Current Real Estate Taxes		\$900.00

- Interest paid on escrow account

Interest: 152 days x .000164383 x \$300.00 = \$7.50

Cash	\$7.50	
Taxes Held in Escrow		\$7.50

- Court Settlement Occurred before 07/01/X2

The court ruled on 03/31/X2 to return 10% of the tax plus 6% interest to the taxpayer.

Interest: 152 days x .000164383 x \$120.00 = \$3.00

Taxes Held in Escrow	\$ 303.00	
Current Real Estate Taxes *		\$180.00
Cash		\$123.00

*Tax Account – Delinquent Real Estate Taxes would be used here if the court settlement occurred on or after 07/01/X2.

Liquid Fuel Tax Refunds

Liquid Fuel Taxes are paid when the school purchases fuel and are refunded to the school based on calendar year, not fiscal year, purchases. To properly record this transaction, you should record the anticipated liquid fuel tax refund when fuel is purchased, rather than when the refund is received.

Special Revenue Funds

Nature and Purpose

Special revenue funds are used to account for and report the proceeds of revenue sources that are legally restricted for specific purposes than debt service or capital projects. The revenue source(s) must comprise a substantial portion of the inflows reported in the fund. Schools should discontinue reporting activities as a special revenue fund if these criteria are no longer met. Special revenue funds differ from enterprise funds in that the services delivered by a special revenue fund are not financed by user charges.

Pennsylvania LEAs:

LEAs are not permitted to establish special revenue funds not listed in this chapter unless authorized by the Office of Comptroller Operations. Special revenue funds may not be established to account for monies for future health care cost increases, technology expenditures or other uses not specified in this chapter.

Special Revenue Funds Available for Use by All LEAs:

- Public Purpose (expendable) – Trust Fund - Fund #27
This fund type maintains the principal and earnings of a trust that benefits the school. The principal and earnings of this fund may be spent.
- Other Comptroller Approved Special Revenue Fund – Fund #28
Accounts for activities recognized by the Office of Comptroller Operations as meeting the criteria for a special revenue fund but that are not defined in this chapter. Requests to establish a comptroller approved fund should be sent to ra-schlfin@pa.gov
- Athletic Fund – Fund #29
Athletic funds are set up in accordance with Section 511 of the School Code. LEAs are permitted to establish athletic funds as a special revenue fund only if they meet the revenue and expenditure criteria, i.e. the expenditures are limited only for athletic purposes and the revenue source (gate receipts) must comprise a substantial portion (defined as 50% or more in Accounting Bulletin 2010-02) of the inflow of this fund. If the criteria are not met, all athletic activities must be accounted for in the general fund of the school. If the criteria are met then **all** athletic expenditures must be accounted for in this fund.

Special Revenue Funds Available for Use by Intermediate Units

- Special Education Fund – Fund #23
This fund should be used to account for regular IU operated special education programs performed on behalf of LEAs as authorized by Section 2590.1(d) of the School Code.
- Special Education Transportation Fund – Fund #24
Accounts for financial resources received and utilized for the transportation of exceptional children in accordance with Section 2509.1 (d) (2) of the School Code.

- Institutionalized Children Program – Fund #25
This fund should be used to account for institutionalized children programs operated on behalf of LEAs. This fund was previously known as the Special Education Mandated Program.
- Early Intervention Program – Fund #26
Established to comply with Early Intervention Programs and accounts for monies to be used for handicapped children of preschool age.
- Other legally restricted resources, including state and federal grants and subsidies, are to be accounted for in the general fund. Examples of restricted resources accounted for in the general fund for the intermediate unit would be federal and nonpublic funds. An example for a school district or area vocational-technical school would be federal funds.

Capital Projects Funds

Nature and Purpose

Capital projects funds are used to account for and report financial resources 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. Capital outlays financed from general obligation bond proceeds should be accounted for through a capital projects fund (*GASB Codification 1300.106*). The fund's purpose is to track funding and expenditures for the project/asset. Neither the asset nor the long-term debt is recorded in this fund. Capital projects funds are used when projects are financed partially or wholly by bond issues, intergovernmental revenues, fund transfers or major private donations. They are also useful for projects financed by current revenues from more than one fund or extending longer than a year.

The disposition of surpluses and deficits at the close of a project is a legal as well as an accounting issue. Usually, if debt is outstanding, any remaining assets are transferred to the debt service fund to retire the debt. If debt is not outstanding, assets are normally returned to the fund or funds that originally provided the resources, e.g. general fund.

Note: Bond proceeds are not permitted to be a revenue source for the capital reserve funds #31 & #32. Projects funded by bond proceeds should be accounted for in fund 39.

Pennsylvania LEAs:

Capital Reserve Funds – Funds #31 & #32 are unique to Pennsylvania LEAs. Although categorized as capital projects funds, the statutory limitations must be followed when establishing and maintaining these funds.

- **Capital Reserve Fund (Sections 690 and 1850.1 of the School Code) - Fund #31**
Section 690 of the School Code authorizes **school districts** to create a capital reserve fund to account for moneys resulting from the levy of a special tax.

- A school district may create a capital reserve fund and reserve money to be spent, as outlined in this section, during a period not to exceed five years from the date when the first payment was made into the fund. The fund is established for a specific purpose as listed below, and requires a board-adopted resolution.
- Section 690 allows capital reserve funds to be used for constructing a school building project or projects under a long-term project program approved by the Pennsylvania Department of Education. It includes the costs of acquiring sites for school buildings, constructing new school buildings, and providing needed additions or alterations to existing buildings.
- Receipts of this type of capital reserve fund come from a special tax assessment, which is levied by the school board in accordance with this section of the School Code. The section details millage limits (cannot exceed 3 mil in one year) and time frames.
- If for any reason the project for which the capital reserve fund was established fails to materialize, the moneys accumulated in the fund shall be transferred to the general fund in equal amounts spread over a period of five years.
- No other transfers out of this fund are allowable for any purpose.
- Section 1850.1 of the School Code authorizes area vocational-technical schools to create a capital reserve fund under the provisions of Section 1850.4.
- An AVTS may create a capital reserve fund to accumulate money to be spent, as outlined in this section, during a period not to exceed five years from the date when the first payment was made into the fund.
- The money in this capital reserve fund may be utilized only for the purchase of equipment or facilities maintenance.
- Receipts for this type of capital reserve fund come from transfers of appropriations remaining in the general fund in the current or prior fiscal years.
- Any interest earnings on investments must remain within the capital reserve fund.
- Transfers out of this fund are not allowable.

Accounting Bulletin 2003-01 provides additional information regarding Fund 31.

- **Capital Reserve Fund (Section 1431-36 of the Municipal Code) - Fund #32**

- Authorized by P.L. 145, Act of April 30, 1943, Section 1431-36 (referred to as section 1432) of the Municipal Code. Capital Reserve Fund, Section 1432, information is reported on the Annual Financial Report (PDE-2057) and the General Fund Budget (PDE-2028) as fund 32.
- The money in this capital reserve fund may be spent only on capital improvements; replacement of, addition to and improvement to public works; deferred maintenance and for the replacement of school buses.
- Receipts for this type of capital reserve fund come from transfers during the fiscal year from appropriations in the general fund that have surplus money.
- Receipts may also come from surplus money in the general fund at the end of the fiscal year.
- Any interest earnings on investments must remain within the capital reserve fund
- Transfers out of this fund are not allowable for any purpose.

- The Pennsylvania Department of Education has determined that new construction and the debt service associated with these projects may also be accounted for in this type of capital reserve fund.

Accounting Bulletins 2003-01 and 2007-01 provide additional information regarding Fund 32.

- **Capital Projects Fund – Fund #39**

This fund will be utilized to report the total of all capital project fund activity not specifically associated with Funds 31 or 32 above. Financial data of this fund was reported as Fund 30 prior to the implementation of GASB Statement No. 54.

Debt Service Funds

Nature and Purpose

Debt service funds are used to account and accumulate resources for the payment of general long-term debt principal and interest. Debt service funds should be used to report resources if legally mandated. Financial resources that are being accumulated for principal and interest maturing in future years also should be reported in debt service. A debt service fund is used to account for accumulations of resources. Without such accumulations, it is common to account for debt service in the general fund.

Pennsylvania LEAs:

Section 8221 (a) of the Pennsylvania Local Government Unit Debt Act addresses the applicability of debt service funds (sinking funds) to municipalities (school districts), and the number of debt service funds (sinking funds) required to be maintained for bonds and notes outstanding other than tax anticipation notes and other than notes issued under section 8109 All outstanding bonds or notes, other than the exceptions noted, must have a corresponding debt service fund (sinking fund) established.

Note: The debt service fund does not report long-term debt obligations. Long-term debt obligations are reported as government-wide type transactions at the LEA level. The debt service fund services the debt of the governmental funds. Debt service relating to the proprietary funds is reported within the appropriate proprietary fund, not the debt service fund.

Accounts and Transactions

- Revenues and Other Financing Sources

The primary sources of funds in the debt service fund are transfers from the general fund and interest earnings on investments. Other financing sources represent revenues in the debt service fund.

- Transfers

Transfers from other governmental funds to the debt service fund are made to pay long-term debt. The fund making the transfer debits an interfund transfers-out account (Other Financing Uses), and the debt service fund records an interfund transfers-in (Other Financing Sources).

- Expenditures and Other Financing Uses

Accounting for debt service fund expenditures is similar to that for the General and special revenue funds. The exception to this is that un-matured principal and accrued interest on general obligation long-term debt need not be recognized as an expenditure until due to be paid. Thus, accrual of principal and/or interest during the fiscal year is not required but is recorded as an expenditure when the payment is due.

As principal payments are made, the debt service fund recognizes expenditure and the corresponding long-term debt obligation recorded in the entity wide statements is reduced.

Permanent Funds

Nature and Purpose

Permanent funds should be used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support your school's programs, i.e., for the benefit of your school or its citizenry. Do **not** include resources that require your school to use the principal or earnings for the benefit of individuals, private organization or other government as a permanent fund type. These resources must be accounted for as private-purpose trust funds, which are fiduciary funds **not** governmental funds.

An example of a permanent fund is a donation by a private citizen that allows for the earnings on the donation to be used for band activities.

Permanent Funds Available for Use by All LEAs:

- Permanent Fund – Fund #90

Permanent funds do not include "private" purpose trust funds, which are available only to individuals, private organizations and other governments.

Chapter 5: Proprietary Funds

Proprietary Fund Overview

Nature and Purpose

Proprietary fund reporting focuses on the determination of operating income, changes in net assets (or cost recovery), financial position, and cash flows.

Basis of Accounting and Measurement Focus

Proprietary fund statements of net position and statement of revenues, expenses, and changes in fund net position should be presented using the economic resources measurement focus and the accrual basis of accounting. The generally accepted accounting principles applicable in this fund category are similar to those applicable to business in the private sector. The measurement focus is on determination of net income, financial position, and cash flows. Proprietary funds are concerned with the flow of economic resources as opposed to the focus on the flow of current financial resources found in governmental funds. If advance payments are received, the revenue is deferred until the service is provided.

Based on the provisions of GASB Codification Section P80, paragraph .102, proprietary funds should be reported based on all applicable GASB pronouncements (including all NCGA Statements and Interpretations currently in effect).

Proprietary Fund Financial Statements

Statement of Net Position

- Assets - Current & noncurrent assets are reported in the statement of net position. A clear distinction should be made between general capital assets and capital assets of proprietary and fiduciary funds.
 - Capital Assets
Capital assets of proprietary funds (enterprise and internal service) should be reported in the government-wide statement of net position and in the proprietary fund statement of net position. Capital assets of proprietary funds should be capitalized and reported as discussed in paragraphs GASB Codification Section 1400.102–.111.
- Deferred Outflows of Resources – A deferred outflow of resources is a consumption of net assets by the government that is applicable to a future reporting period.
- Liabilities – Current and noncurrent liabilities are reported in the statement of net position. Long-term liabilities directly related to and expected to be paid from proprietary funds should be reported in the proprietary fund statement of net position. These are specific fund liabilities, even though the full faith and credit of the governmental unit may be pledged as further assurance that the liabilities will be paid.
- Deferred Inflows of Resources – A deferred inflow of resources is an acquisition of net assets by the government that is applicable to a future reporting period.

- Net Position – Net positions should distinguish between net investment in capital assets, restricted (separately reporting expendable and nonexpendable components), and unrestricted.

Statement of Revenues, Expenses and Changes in Fund Net Position

- Operating Revenues, and Expenses – The proprietary fund statement of revenues, expenses, and changes in fund net position should distinguish between operating and nonoperating revenues and expenses. A policy should be established that defines operating revenues and expenses that is appropriate to the nature of the activity being reported. The policy should be disclosed in the summary of significant accounting policies, and used it consistently from period to period.
- Nonoperating Revenues & Expenses – Nonoperating revenues and expenses should be reported after operating income.
- Other – Capital contributions and additions to permanent and term endowments, special and extraordinary items, and transfers should be reported separately after nonoperating revenues and expenses. Revenue recognition for capital contributions, additions to permanent and term endowments, and all other nonexchange revenues should be based on the requirements of GASB Codification Section N50.
- Change in Net Position – Reports beginning net position, change in net position, and ending net position.

Statement of Cash Flows

A statement of cash flows should be presented for proprietary funds based on the provisions of GASB Codification Section 2450. The direct method of presenting cash flows from operating activities (including a reconciliation of operating cash flows to operating income) should be used.

A statement of cash flows should explain the change during the period in cash and cash equivalents regardless of whether there are restrictions on their use. The statement should use a descriptive term such as cash or cash and cash equivalents rather than the term funds, which has several different meanings in governmental accounting. The total amounts of cash and cash equivalents at the beginning and end of the period shown in the statement of cash flows should be easily traceable to similarly titled line items or subtotals shown in the statements of financial position as of those dates.

Types of Proprietary Funds

Enterprise Funds

Nature and Purpose

Enterprise funds may be used to account for operations where the intent of the governmental entity is to recover the costs of providing goods and services to the LEA's student population and staff primarily through user charges. The costs to be recovered are the *expenses* of the operation, including depreciation. This does not mean, however, that all of the expenses of the operation must be paid by the users for an enterprise fund to be appropriate. Enterprise funds are required to be used when specific circumstances require it, as described in the GASB Codification Section 1300.109

Enterprise Funds Available for Use by LEAs

- Food Service / Cafeteria Operations – Fund # 51

The food service fund is the primary enterprise fund operated by Pennsylvania LEAs. This fund provides goods and services to the students on a continuing basis and is financed through user charges.

Pennsylvania LEAs:

Section 504 of the School Code establishes the criteria for the establishment and maintenance of a food service fund by school districts. This fund should be used to account for all revenues and expenses pertaining to cafeteria operations.

Section 504 requires that prices will not materially exceed the cost of operation and that any funds remaining from operations must be used 'only for the improvement or maintenance of the cafeteria and may not be used for other purposes.'

Any assistance given the cafeteria operations by the general fund must be recorded as a transfer to the food service fund and all revenues and expenses of the cafeteria must then be recorded in the food service fund itself.

Charter schools are permitted to account for food service type activities in the general fund if the cafeteria operations do not meet the GASB criteria for proprietary fund reporting.

- **Revenues**

Food service fund revenues are recognized in the period in which they are earned. User charges are normally received when the service is performed and thus recorded as received. If advanced payments are received the revenue is deferred until the service is provided. Subsidy payments are received based on services provided, thus the revenue is recognized along with a corresponding receivable. When the cash is received, the receivable is adjusted accordingly.

Examples:

Sales in the cafeteria for the month were \$30,000.00.

Cash	\$30,000.00	
Price Reduction For Reduced Priced Meals	\$ 2,000.00	
Daily Sales Reimbursable Programs		\$29,000.00
Daily Sales Non-reimbursable		\$ 3,000.00

The state will subsidize \$1,000.00 for milk, lunch and breakfast programs, while the federal subsidy for the same program will be \$9,000.00 for the month.

State Subsidies Receivable	\$1,000.00	
Federal Subsidies Receivable	\$9,000.00	
State Subsidy For Lunch Programs		\$1,000.00
Federal Subsidy For Lunch Programs		\$9,000.00

- **Expenses**

Food service fund expenses are recognized in the period in which they are incurred. Inventories of materials and supplies are recognized as expenses when they are consumed.

- **Debt**

Bonds, notes and other long-term liabilities should be reported in the enterprise fund if they were issued for enterprise fund purposes and are expected to be paid with enterprise funds. The debt may be considered a “general obligation” of the LEA, but if the expected source of repayment is the enterprise fund, then the debt should be reported in the fund itself. Long-term debt is used often to make capital asset purchases.

General obligation bonds are considered to be full faith and credit bonds. If they will be repaid from the earnings of the food service fund, then the proceeds should be recorded as a liability of the food service fund. If, however, the principal and the interest are to be paid from general fund revenues and taxes of the school district, then the entries to record the issuance of the general obligation bonds are recorded in the general fund.

- **Federally Donated Commodities**

Inventory of federally donated commodities must be reported at year-end. The suggested way to report the commodities that are on hand at year-end is a debit to inventory and an offsetting credit to deferred inflow. The reason for the offsetting credit to a deferred inflow account is that the title of the federal donated commodities does not pass to the school district until the commodities are used.

Donated commodities should be recorded at their fair market value. The fair value of the commodities used during the year is reported in the operating statement as an expense with a like amount reported as intergovernmental revenue. The following example is meant to aid in the reporting of federally donated commodities.

Examples:

The federal government donated 50 pounds of butter at a fair market value (FMV) of \$150.00.

Food Service Fund

Inventory – Federally Donated	\$150.00	
Deferred Inflow		\$150.00

Assume that it is decided that 10 pounds of butter with a FMV of \$30.00 had been used in servicing the food service program.

Food Service Fund

Food Service Expense	\$30.00	
Inventory – Federally Donated		\$30.00

Deferred Inflow	\$30.00	
Revenue		\$30.00

- Child Care Operations – Fund #52
Activities that provide custodial care and childcare services to children so parents can participate in education, training activities, accept or maintain employment or receive needed protective services. These operations are not part of the instructional program.
- Other Enterprise Funds – Fund #58
This fund should be used for enterprise activities that cannot be specifically accounted for in Funds 51 & 52, are reported in the Other Enterprise Fund #58.

Internal Service Funds

Nature and Purpose

The GASB Codification, Section 1300.110 states that internal service funds may be used to account for the financing of goods or services provided by one department or agency to other departments or agencies of the governmental unit and its component units, or to other governments, on a cost-reimbursement basis. When it is advantageous to centralize the provision of goods or services, LEAs may use an internal service fund to account for such provision to other funds of the LEA. Services accounted for in internal service funds are tangible, and it is possible to determine the extent to which they benefit individual funds or LEAs. Typical services reported in internal service funds include printing and duplicating, data processing services, central purchasing and risk financing (Self Insurance).

Internal service funds are reimbursed for the costs of services by the fund or LEA to which they are provided. Such reimbursements are accounted for as quasi-external transactions. Accordingly, they are treated as operating revenues of the internal service fund and as current operating expenditures or operating expenses of the reimbursing fund.

Charges to other departments and agencies for internal service fund services are intended only to recoup the total cost of such services. Internal service funds are not designed to produce any significant profit in the long run.

The use of internal service funds are not required by GAAP. Once a decision is made to account for a particular service as an internal service fund; however, it should be followed consistently from year-to-year. Governmental fund type and proprietary fund type accounting produce significantly different financial statements. Therefore, fund classifications must be consistently applied from year to year if there is to be a significant potential for meaningful financial statement comparative analysis.

Number of Funds

The main purpose of internal service funds is to identify and allocate costs related to the provision of specific goods and services within the LEA. Therefore, it is important that costs related to separate activities be accounted for separately. Accordingly, separate individual Internal Service Funds normally are established for each different type of activity. This segregation is essential to determine the total cost of providing a service, and assure that the resources generated by one service are not improperly utilized for another. Activity for all the internal service funds are combined at year-end and reported under one internal service fund category.

Internal Service Fund Available for Use by LEAs

- *Internal Service Fund – Fund #60*

This fund accounts for the operation of LEA functions that provide goods or services to other LEA funds, other LEAs or to other governmental units, on a cost reimbursable basis. Some examples of internal service funds could include those used for central warehousing and purchasing, central data processing, and central printing and duplicating.

Note: Act 94 of 2011 outlines certain conditions related to joint purchases of Pennsylvania school districts.

Accounting Issues Unique to Internal Service Funds

Three issues arise with proper accounting and financial reporting for internal service funds. These issues are:

- *Duplication of Expenses / Expenditures within The Financial Reporting Entity*

Most transactions between internal service funds and other funds are quasi-external transactions. Consequently, the funds receiving goods or services report an expense or expenditure for payment to the internal service fund. The internal service fund reports revenue received, as well as an expense for producing the goods or service.

Internal service fund activities should be eliminated when preparing the government-wide statement of activities to avoid duplication of expenses and revenues. This is accomplished by adjusting the activities of the fund to create a break-even balance. Any residual balances are reported in the governmental activities column on the statement of activities if the internal service fund's activities benefited the governmental funds. If the activities benefited the business funds of the school, then the residual amounts would be accounted for in the business type activities column on the government-wide statement of activities.

- Surpluses And Deficits Within The Internal Service Fund

Internal service funds are used to account for services provided on a *cost-reimbursement* basis (i.e., without profit or loss). Therefore, surpluses or deficits in the internal service fund may be an indication that other funds were not charged properly for the goods or services they received.

The cost-reimbursement basis applies to the operations of the fund over time. If internal service funds consistently report significant deficits or surpluses, however, charges made to other funds must be reassessed. If it is determined that the charges made to other funds are more or less than is needed to recover cost over a reasonable period, then the excess or deficiency should be charged back to the participating fund or LEA. It is not appropriate to report a material deficit in an internal service fund without the intent and ability to recover that amount through future charges over a reasonable period. Often internal service funds charge for asset use in excess of historical cost depreciation to ensure that adequate funds will be available to purchase replacement assets. This recovery of the replacement cost of fixed assets is not a violation of the cost allocation principle because the resulting surpluses are only temporary. They will disappear when the higher priced assets are acquired.

- Risk Financing Activities

Risk management is the process of managing an organization's activities to minimize the adverse effects of certain types of losses. The main elements of risk management are risk control (to minimize the losses that strike an organization) and risk financing (to obtain finances to provide for or restore the economic damages of those losses). Risk financing techniques include risk retention (sometimes referred to as self-insurance), risk transfer to and from an insurer (either a commercial insurance company or a public entity risk pool), and risk transfer to a noninsured.

GASB Codification Section C50 establishes the accounting and financial standards for risk financing and self-insurance related activities for state and local governments. If an LEA wishes to account for all of its risk financing activities in a single fund, it is recommended that the internal service fund be used. However, GASB also permits the use of the general fund for such purposes. Charges to other funds by the internal service fund are to be treated as *quasi-external* transactions, i.e., expenses / expenditures by the paying fund(s) and as revenue by the internal service fund.

- Participation in Public Entity Risk Pools

A public entity risk pool is defined by the GASB Codification Section Po20 as a cooperative group of governmental entities joining together to finance an exposure, liability or risk. Risk may include property and liability, workers' compensation or employee health care. A pool could be a stand-alone entity or it could be included as part of a larger governmental entity that acts as the pool's sponsor.

Some pool risk arrangements entail a transfer of risk and others do not. GASB Statement No. 10, Po20.112 defines four types of public entity risk pools:

- A risk sharing pool is an arrangement by which governments pool risk and share in the cost of losses;
- An insurance-purchasing pool is an arrangement by which governments pool funds or resources to purchase commercial insurance products. This arrangement is also called a risk-purchasing group.
- A banking pool is an arrangement by which monies are made available for pool members in the event of loss on a loan basis; and
- A claims-servicing or account pool is an arrangement by which a pool manages separate accounts for each pool member from which the losses of that member are paid.

A pool could serve only one of these functions. Pools that act only as banking or claims-servicing pools do not represent transfer of risk.

All public entity risk pools should account for their activities in an enterprise fund regardless of whether there is a transfer or pooling (sharing) of risk. As discussed in Section P80, public entity risk pools and other entities that use proprietary (enterprise) fund accounting and reporting should apply all applicable GASB pronouncements (including all NCGA Statements and Interpretations currently in effect) as well as certain Financial Accounting Standards Board and Accounting Principles Board pronouncements.

Chapter 6: Fiduciary Funds

Fiduciary Fund Overview

Nature and Purpose

Fiduciary funds should be used to report assets held in a trustee or agency capacity for others and therefore cannot be used to support the government's own programs. The fiduciary fund category includes pension (and other employee benefit) trust funds, investment trust funds, private-purpose trust funds, and agency funds. The three types of trust funds should be used to report resources held and administered by the reporting government when it is acting in a fiduciary capacity for individuals, private organizations, or other governments. These funds are distinguished from agency funds generally by the existence of a trust agreement that affects the degree of management involvement and the length of time that the resources are held.

Number of Funds

LEAs can have multiple trust and agency funds that are combined for AFR reporting purposes. Separate agency funds are used for individual agency relationships. Specifically, activity funds are addressed in Section 511 of the School Code. Implied in Paragraph (d) of this Section is that the funds of each school, class, organization, club, society, or group thereof is to be maintained as a separate fund.

Basis of Accounting and Measurement Focus

Financial statements of fiduciary funds should be reported using the economic resources measurement focus and the accrual basis of accounting. Fiduciary fund reporting focuses on net position and changes in net position.

Agency funds, a fiduciary fund type, use the accrual basis of accounting to report assets and liabilities. Agency funds have no measurement focus since they only report assets and liabilities and do not report operating statements.

Fiduciary Fund Financial Statements

The Statement of Fiduciary Net Position

- Assets - Current and noncurrent assets are reported in the statement of fiduciary net position. Capital assets of fiduciary funds (and similar component units) should be reported only in the statement of fiduciary net position.
- Deferred Outflows of Resources – A deferred outflow of resources is a consumption of net assets by the government that is applicable to a future reporting period.

- Liabilities – Current and noncurrent liabilities are reported in the statement of net position. Long-term liabilities directly related to and expected to be paid from fiduciary funds should be reported in the fiduciary fund statement of net position. These are specific fund liabilities, even though the full faith and credit of the governmental unit may be pledged as further assurance that the liabilities will be paid.
- Deferred Inflows of Resources – A deferred inflow of resources is an acquisition of net assets by the government that is applicable to a future reporting period.
- Net Position – Net Positions should distinguish between net investment in capital assets, restricted (separately reporting expendable and nonexpendable components), and unrestricted net position.

The Statement of Changes in Fiduciary Net Position

The statement of changes should include information about the additions to, deductions from, and net increase (or decrease) for the year in net position. The statement should provide information about significant year-to-year changes in net position.

This statement is applicable for each fiduciary fund except for agency funds. This statement is not applicable for agency funds because their assets equal their liabilities and thus they do not have residual net position.

Types of Fiduciary Funds

Trust Funds

Nature and Purpose

Trust funds exist where the LEA acts as a trustee for assets placed in its care. The use of a trust fund should be limited to situations where the use of resources is legally restricted by parties outside of the LEA (e.g., formal trust agreement with the donor).

Trust Funds Available for Use by LEAs

- Private-Purpose Trust Funds – Fund #71
This fund is used to report escheat property and all trust agreements under which principle and interest benefit individuals, private organizations or other governments. Do not use a private purpose trust fund to account for monies that are available to support school programs. See the note below for information on accounting for trusts that benefit the school operations. If your LEA has an activity that benefits both your school and a private party, you should classify the trust fund according to the predominant beneficiary, rather than in two (2) separate funds. Use a Special Revenue Fund if your LEA is the predominant beneficiary and reserve the “private purpose” portion. Use the private-purpose fund if the “private purposes” has the predominate use of resources in the fund.
- Investment Trust Funds – Fund #72
This fund is used to report the external portion of investment pools sponsored by your school.

- Pension Trust Funds – Fund #73

This fund is used to report pension trust and other employee benefit trusts that are required to be held in trust for members and beneficiaries of defined benefit pension plans, defined contribution plans, and other post-employment and employee benefit plans. The recognition of certain liabilities of defined benefit pension plans and other postemployment benefit plans is discussed in GASB Codification Sections Pe5, "Pension Plans—Defined Benefit," and Po50, "Postemployment Benefit Plans Other Than Pension Plans—Defined Benefit."

NOTE: For information regarding accounting for trust funds that benefit the school or are used to support school purposes, refer to the governmental funds chapter of this manual under the topics of Public Purpose Trust Funds #27 and Permanent Trust Funds #90.

Agency Funds

Nature and Purpose

Agency funds should be used to report resources held by the reporting government in a purely custodial capacity. They typically involve only the receipt, temporary investment, and remittance of fiduciary resources to individuals, private organizations, or other governments. Based on the provisions of GASB Statement No. 63, fund assets should equal liabilities in the statement of net position. However, they should not be reported on the statement of changes in net position. No fund equity is reported in Agency Funds.

The primary use of agency funds for LEAs are for student activity funds. They are used to account for school activities such as various clubs (i.e., drama, Spanish, etc.) and class funds (i.e., the class of 20XX). While both agency funds and trust funds are classified as fiduciary fund types, the degree of management for trust funds is much higher than for agency funds. Agency funds normally only involve the receipt, temporary investment and remittance of assets to the rightful owners.

Agency Funds Available for Use by LEAs

- Activity Funds - Fund #81

Students often retain control of funds obtained from sources (i.e., special fund-raising activities) other than the LEA's budget. For example, a trip to Spain for the Spanish Club may be funded through sub sales, car washes and similar fund-raising efforts. The school's principal is typically responsible for overseeing the administration of such student activity funds. Therefore, a separate designation for activity funds is provided in the Chart of Accounts. Activity funds are accounted for in the 80 series of account numbers. The major fund designation of 80 can be subdivided into sub-accounts (i.e., 81, 82, etc.) to accommodate the LEA's specific requirements for the various activities (e.g., science club, student council, etc.).

- Other Agency Fund – Fund # 89

This fund is used to report all other fiduciary funds that fit the agency fund description.

NOTE: Agency fund grants received as a pass-through. In those infrequent cases in which a recipient government serves only as a cash conduit, the grant should be reported in an agency fund. A recipient government serves only as a cash conduit if it merely transmits grantor-supplied moneys without having administrative or direct financial involvement in the program. GASB Codification Section N50.128 addresses this more specifically.

Specific issues regarding activity funds

- Sales Tax

When a public school purchases taxable property such as candles, magazines, etc. for resale to raise funds, the public school must pay the applicable sales tax at the time of purchase, or collect the sales tax from the customer when the item is resold. If sales tax is paid to the vendor when purchasing the taxable item, the school can reimburse itself by adding the amount of tax paid to the charge to customers when the item is resold.

If the school organization operates a school store, sells pictures, class rings, and/or yearbooks, or sells property or services to the public, the school has the option to claim tax-exempt status. Sales would be required to obtain a permit for collection and remission of the tax, and remit the amount directly to the Department of Revenue.

Specific questions related to sales tax should be directed to the Pennsylvania Department of Revenue.

- Organizations Not Part of the School

Funds that belong to outside organizations such as booster clubs, PTAs, and PTOs should not be accounted for as agency funds. These types of funds do not belong to the school and should not be accounted for in the school's accounting records. These groups should operate independently from the school. The school's board must adopt a policy regarding the accounting of monies from outside organizations.

- Unexpended Senior Class Funds

Each school board should establish a policy to transfer unused/uncommitted funds to a Student Body Activity account or similarly named account. In 1989, a Common Pleas Court ruling determined that ownership of money leftover in student activity funds following the graduation of each senior high school class is vested in the LEA, and the funds must be used to further a school-related purpose pursuant to the Section 511 of the School Code. Maintaining the funds for future activities such as class reunions, are not a legitimate use of the funds. The graduating class should designate how the remaining funds are to be spent for school related purposes or the board policy will dictate the usage of the funds.

Examples:

The senior class earns \$1,500.00 by sponsoring car washes. The car wash facilities and supplies were donated by various service dealers.

Cash	\$1,500.00
Due To Class of 20XX	\$1,500.00

The senior class receives accrued interest on class funds they had invested.

Cash	\$200.00	
Interest Receivable		\$200.00

The senior class estimates \$2,300.00 on a senior trip before graduation. Class sponsor withdrew \$2,300.00 to pay the anticipated expenses (a member of the high school faculty acts as the class sponsor) by recording the cash advance to the class sponsor.

Due To Class of 20XX	\$2,300.00	
Cash		\$2,300.00

Documented expenses after-the-fact amount to \$2,200.00, and the class sponsor returns \$100.00.

Cash	\$ 100.00	
Due To Class of 20XX		\$ 100.00

\$1,800.00 in unused funds is remaining in the senior graduating class fund at graduation. According to board policy, this balance becomes the property of the LEA. The trial balance of the senior class at graduation is:

Agency Fund – Senior Class (to close out fund for senior class)

Due To Student Council	\$1,800.00	
Cash		\$1,800.00

Student Council Account (to record donation from the senior class)

10-0101 Cash	\$1,800.00	
10-6920 Contributions And Donations		\$1,800.00

Chapter 7: Investments, Inventory, and Capital Assets

CASH AND INVESTMENTS

Cash (including cash equivalents) and investments represent some of the largest assets on an LEA's balance sheet. The investment of excess LEA funds should be made with judgment, care, prudence, discretion, and with diligent management.

Cash Equivalents

Cash equivalents are short-term highly liquid (readily convertible to known amounts of cash) investments that are so near to their maturity that they present an insignificant risk of change in value resulting from changes in interest rates. Generally, only investments with original maturities of three months and less qualify under this definition. Items commonly considered as cash equivalents are Treasury bills, commercial paper and money market funds. Investments that qualify as cash equivalents are not all required to be treated as cash equivalents. An LEA should establish a policy concerning short-term highly liquid investments (that satisfy the definition), which are to be treated as a cash equivalent. An LEA must disclose its policy for cash equivalents in notes to the financial statements. Any change in that policy represents a change in accounting principle that shall be affected by restating financial statements for earlier years presented for comparative purposes.

Investments

Investments are defined as securities and other assets acquired primarily for the purpose of obtaining income or profit. Interest-bearing deposits (including certificates of deposits) with financial institutions should be treated as deposits, not as investments.

A *security* is a transferable financial instrument that evidences ownership or creditor status. Securities that are often held by or pledged to LEAs generally include U.S. Treasury bills, notes and bonds, federal agency and instrumentality obligations, direct obligations of the State of Pennsylvania or its agencies, commercial paper, negotiable certificates of deposit, fully collateralized repurchase agreements, and prime domestic bankers' acceptances.

Accounting Bulletin 1998-02 - Reporting Standards for Investment Gains and Losses provides further guidance for Pennsylvania LEAs on this topic.

Valuation of Investments

GASB Codification Section I50 states that governmental entities, including governmental external investment pools, should report the majority of investments (Refer to Section I50 for exceptions) at fair value in their basic statements. Fair value (as described in GASB Statement No. 72) is the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. Fair Value may be measured using a market approach, cost approach or income approach. Valuation techniques should maximize the use of observable inputs and minimize the use of unobservable inputs. If there is a quoted price in an active market for an identical asset, a government should use that quoted price without adjustment to measure at fair value. If this is not available, quoted prices for similar assets in active markets, quoted prices for identical assets in markets that are not active, or inputs other than quoted prices that are observable should be utilized. Other observable inputs include interest rates and yield curves observable at commonly quoted intervals, implied volatilities, or credit spreads. Unobservable inputs should only be used when no observable inputs are available.

Pennsylvania LEAs:

LEAs should report investments at fair value in the balance sheet. All investment income, including changes in the fair value of investments, should be recognized as revenue in the statement of revenues, expenditures, and changes in fund balances (or other statement of activities). When identified separately as an element of investment income, the change in the fair value of investments should be captioned net increase (decrease) in the fair value of investments. Realized gains and losses should not be displayed separately from the net increase (decrease) in the fair value of investments in the financial statements.

Authorized Types of Investments for Pennsylvania School Districts:

Section 440.1(c) of the School Code authorizes the types of investments school districts may have:

- United States Treasury bills.
- Short-term obligations of the United States Government or its agencies or instrumentalities. Short-term obligations usually refer to investments of less than 13 months.
- Deposits in savings accounts or time deposits or share accounts of institutions insured by The Federal Deposit Insurance Corporation (FDIC), or The Federal Savings and Loan Insurance Corporation, or The National Credit Union Share Insurance Fund to the extent that such accounts are so insured, and for any amounts above maximum, provided that approved collateral as provided by law therefore shall be pledged by the depository.
- Obligations of the United States of America or any of its agencies or instrumentalities backed by the full faith and credit of the United States of America, the Commonwealth of Pennsylvania or any of its agencies or instrumentalities. Full faith and credit means the obligation is backed by the government's ability to levy taxes to repay debt. These investments include any bonds issued by the Commonwealth of Pennsylvania or any municipality or school district carrying the backing of the taxation powers of the governmental unit issuing the debt. Some investments of the federal government do not have full faith and credit backing. Fannie-Mae (FNMA) and Freddy-Mach (FNMC) bonds do not. Ginnie-Mae (GNMA) bonds do have full faith and credit backing.

- Shares of an investment company registered under the Investment Company Act of 1940 whose shares are registered under the Securities Act of 1933 provided that the following are met:
 - Only investments of that company are in the authorized investments for school district funds listed in the categories above, and repurchase agreements fully collateralized by such investments.
 - The investment company is managed so as to maintain its shares as a constant net asset value in accordance with 17 CFR 270 2a-7 (relating to money market funds).
 - The investment company is rated in the highest category by a nationally recognized rating agency.

This classification includes pooled investments such as the Pennsylvania School District Liquid Asset Fund, Pennsylvania Local Government Investment Trust and the Pennsylvania State Treasurer's Invest Program.

Any purchase or sale of investments shall be made by the treasurer of the school district on a resolution adopted by the board of school directors.

INVENTORY

Governmental accounting generally requires that amounts spent to purchase goods be recorded as expenditures at the time of the purchase. An exception to this general rule is made for inventory. Inventory items (for example, materials and supplies) may be considered expenditures either when purchased (purchases method) or when used (consumption method), but significant amounts of inventory should be reported in the balance sheet.

Consumption Method

Purchase transactions are first recorded in the inventory account under the consumption method. As inventory is actually used, an entry to recognize the expenditure is posted to the appropriate accounts. This method must be used for entity-wide financial statements and is required for proprietary funds. Inventory may also be recorded as expenditure when it is purchased (purchase method) rather than when it is consumed. This method must be used for entity-wide statements.

Purchase Method

The purchase method recognizes expenditures for inventory when supplies are purchased. An inventory account and a fund balance reserve must be established at the end of the year.

Reference: GASB Codification 1600.127.

Examples:

\$75,000 worth of Inventory purchased. At year-end, it is determined that \$60,000 of the supplies was used during the year.

Purchase Method (at the time of purchase)

Expenditures	\$75,000	
Cash		\$75,000

Purchase Method at year-end (entry is made only if inventory balances are significant)

Inventory	\$15,000	
Fund Balance – Nonspendable		\$15,000

Consumption Method at the time of purchase

Inventory	\$75,000	
Cash		\$75,000

Consumption Method at year-end (supplies actually used)

Expenditures	\$60,000	
Inventory		\$60,000

Capital Assets

GASB Codification Section 1400 defines capital assets as land, improvements to land, easements, buildings, building improvements, vehicles, machinery, equipment, works of art, and historical treasures, infrastructure, as well as, all other tangible or intangible assets that will be used in operations and have initial useful lives extending beyond a single reporting period. Assets acquired for the purpose of sale or investment, do not qualify as capital assets, regardless of their form, because they are not used in operations.

LEAs generally account for their capital assets based on asset class: land and land improvements such as pavements, gutters, fences, and walking bridges; buildings and building improvements; machinery and equipment; construction in progress and intangibles. A capital asset generally is classified as equipment rather than as a building improvement if it retains its original shape, appearance and character with use and is an independent unit that does not lose its identity through fabrication or incorporation into a different or more complex unit or structure. An item generally is accounted for as a building improvement rather than as an operating expenditure or expense if it extends the useful life of the building beyond its original life expectancy or significantly increases its value.

Infrastructure Tangible Assets

Infrastructure assets are long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets. LEAs generally do not have a significant number of infrastructure assets, although they may have assets of a similar nature that are land improvements such as roads and bridges that are part of a campus, rather than part of the public domain. Water and sewer systems are also infrastructure items that are reportable by an LEA if the LEA must maintain them. Other examples of infrastructure assets include tunnels, drainage systems, water and sewer systems, dams, and lighting systems. Buildings, except those that are an ancillary part of a network of infrastructure assets, should not be considered infrastructure assets for purposes of this section.

Intangible Assets

Intangible Assets are assets that possess all of the following characteristics (exceptions to this definition noted in GASB Codification 1400.121):

Physical Substance

An intangible asset lacks physical substance. An asset may be contained in or on an item with physical substance. For example, a compact disc in the case of computer software. An asset also may be closely associated with another item that has physical substance, for example, the underlying land in the case of a right-of-way easement. These modes of containment and associated items should not be considered when determining whether or not an asset lacks physical substance.

Nonfinancial in Nature

An intangible asset is nonfinancial in nature. In the context of this section, an asset with a nonfinancial nature is one that is not in a monetary form similar to cash and investment securities, and it represents neither a claim or right to assets in a monetary form similar to receivables, nor a prepayment for goods or services.

Useful Life

An intangible asset has an Initial useful life that extends beyond a single reporting period.

Accounting for Capital Assets

GASB Codification Section 1400 addresses the general principles of accounting for capital assets of governmental funds, proprietary funds, and fiduciary funds.

General Capital Assets

General capital assets are capital assets of the government that are not specifically related to activities reported in proprietary or fiduciary funds. General capital assets are associated with and generally arise from governmental activities. Most often, they result from the expenditure of governmental fund financial resources. The purchase of capital assets in governmental funds are accounted for and reported as expenditures in the fund that pays for the asset in the year of purchase. They should not be reported as assets in governmental funds but should be reported in the governmental activities column in the government-wide statement of net position.

Donated Capital Assets in Governmental Funds

The proper treatment of donated capital assets depends on the plans for those assets. If the intention is to retain the assets, they are recorded directly in the government-wide statement of net position, with no effect on the governmental funds. If, however, the intention is to sell the donated assets, the transaction should be recorded in one of three ways:

- If the assets are sold by the end of the fiscal year, report revenue in the operating statement.
- If the assets are sold after June 30, but before the financial statements are issued, report the fixed assets on the fund's balance sheet as "assets held for resale" and report revenue on the operating statement.
- If the assets were not sold before the issuance of the financial statements, the assets should be reported only in the statement of net position. When they are sold, the LEA would report the sale.

Capital Assets in Proprietary Fund Financial Statements

Capital assets of proprietary funds (enterprise and internal service) should be capitalized and reported in the government-wide statement of net position and in the proprietary fund statement of net position. More specifically, food service fund capital assets are recorded in the fund's asset account and reported in the fund's statement of net position as capital assets. No expenditure is recorded in the fund's accounts or reported in the fund's operating statement when the purchase is made.

Capital Assets in Fiduciary Fund Financial Statements

Capital assets of fiduciary funds and component units that are fiduciary in nature should be capitalized and reported in the statement of fiduciary net position.

Valuation of Capital Assets

Capital assets should be reported at *historical cost*. The cost of a capital asset should include ancillary charges necessary to place the asset into its intended location for use (e.g., freight and transportation charges, site preparation costs and professional fees). Capital assets of proprietary funds should include interest expense incurred during construction. Interest expense should not be included in capital asset valuation for governmental funds this expense is presented as a line item on the statement of activities.

Donated capital assets should be reported at their *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.

Capitalizing Assets and Infrastructure

Each LEA school board should establish a formal written policy for the capitalization of capital assets and infrastructure. This school's capitalization policy should list the assets or asset groups to be managed and the estimated useful lives of each asset or asset system or group. The policy should address whether the threshold for capitalizing asset purchases is to be based on individual equipment items or on systems / categories or groups of assets. For example, individual pieces of computer hardware may fall below a capitalization threshold, but when purchased together as a system they may exceed the threshold. The board policy should list a monetary threshold for capitalization of assets. The board may establish differing monetary, capitalization thresholds for each asset, asset group / class or system. The capitalization threshold refers to the dollar value threshold at which purchases of assets will be capitalized in the financial records of the governmental entity (i.e., within the proprietary funds, fiduciary funds, and government-wide financial statements) rather than recorded as an expense at the time of purchase (except in the governmental funds, where they remain as an expenditure).

The LEA's capitalization policy should be consistently applied each year in making decisions concerning the capitalization and expensing of capital asset purchases.

Note: Sometimes, LEAs raise the minimum dollar value for capitalizing assets. Subsequent changes in an LEA's capitalization threshold generally are accounted for retroactively by removing previously capitalized assets that do not meet the revised capitalization threshold from the capital asset records. For example, if an LEA decides to raise its capitalization threshold from \$500 to \$1,000, all assets valued between \$500 and \$1,000 should be removed from the school's capital asset records for financial reporting purposes.

Depreciation of Capital Assets

Depreciation is a method of spreading the loss in value of a capital asset over several periods and is necessary to measure net income and capital maintenance. Capital assets should be depreciated over their estimated useful lives unless they are inexhaustible, are intangible assets with indefinite useful lives, or are infrastructure assets using the *modified* approach. Inexhaustible assets such as land and land improvements should not be depreciated. Depreciation should be reported in the government-wide statement of activities, proprietary fund statement of revenues, expenses, and changes in fund net position, and the statement of changes in fiduciary net position.

Depreciation Methods

GASB Codification Section 1400.113 states that “depreciation expense should be measured by allocating the net cost of depreciable assets (historical cost less estimated salvage value) over their estimated useful lives in a systematic and rational manner.”

Depreciation May Be Calculated for:

- A class of assets (for example, infrastructure, buildings and improvements, vehicles, machinery, and equipment);
- A network of assets – All assets that provide a particular type of service for a government. For example, a network of infrastructure assets may be a dam composed of a concrete dam, a concrete spillway and a series of locks.
- A subsystem of a network – All assets that make up a similar portion or segment of a network of assets. For example, all the roads of a government could be considered a network of infrastructure assets. Interstate highways, state highways and rural roads could each be considered a subsystem of that network.

Individual assets

Although GASB requires governmental entities to depreciate capital assets, (other than inexhaustible assets) the statement does not prescribe a method. As a result, depreciation methods are a management decision. In addition to composite or group methods, any established depreciation method may be used (e.g., straight-line, sum-of-the-years' digits, or double-declining balance).

The use of the straight-line method is virtually universal in the public sector. Annual depreciation using the straight-line method is determined by taking actual cost, subtracting estimated salvage value, and dividing by the number of years that the asset is expected to be used. Accumulated depreciation for an asset is the annual depreciation times the number of years the asset was actually used.

Examples:

Assume that a capital asset costs \$11,000.00 and is expected to be used for ten (10) years with an estimated salvage value of \$1,000.00.

Annual depreciation is \$1,000.00, which is determined by taking the actual cost of \$11,000.00, subtracting the estimated salvage value of \$1,000.00, and then dividing by the estimated life of ten (10) years. $(\$11,000 - \$1,000)/10$.

Accumulated depreciation at the end of five (5) years, for example, is \$5,000.00. This is determined by multiplying annual depreciation of \$1,000.00 by five (5) years.

In accounting, depreciation of capital assets is usually determined at the close of each fiscal period. Once a method of depreciation is placed into use by a school entity, it should be consistently and systematically applied.

Modified Approach to Depreciation of Infrastructure Assets

Infrastructure assets that are part of a network or subsystem of a network (hereafter, eligible infrastructure assets) are not required to be depreciated as long as two requirements are met:

First, the government manages the eligible infrastructure assets using an asset management system that has an up-to-date inventory of eligible infrastructure assets, perform condition assessments of the eligible infrastructure assets and summarize the results using a measurement scale, and estimate each year the annual amount to maintain and preserve the eligible infrastructure assets at the condition level established and disclosed by the government.

Second, the government documents the eligible infrastructure assets are being preserved approximately at (or above) a condition level established and disclosed by the government.

Determining what constitutes adequate documentary evidence to meet the second requirement for using the modified approach requires professional judgment because of variations among governments' asset management systems and condition assessment methods. These factors also may vary within governments for different eligible infrastructure assets. However, governments should document that complete condition assessments of eligible infrastructure assets are performed in a consistent manner at least every three years. The results of the three most recent complete condition assessments provide reasonable assurance that the eligible infrastructure assets are being preserved approximately at (or above) the condition level established and disclosed by the government.

If eligible infrastructure assets meet the requirements above and are not depreciated, all expenditures made for those assets (except for additions and improvements) should be expensed in the period incurred. Additions and improvements to eligible infrastructure assets should be capitalized.

Impairments of Assets and Insurance Recoveries

Pursuant to GASB Codification Section 1400.161-.177, Governmental entities including school districts, are required to report the financial effects of capital impairments when the service utility of a capital asset has permanently declined significantly and unexpectedly. Though, such events are generally rare. In brief, the codification explains a standardized definition of a capital asset impairment (i.e., "a significant, unexpected decline in the service utility of a capital asset" that is deemed to be permanent); definitive guidance that impaired capital assets no longer being used should be reported at the lower of carrying value or fair value; a variety of measurement options for impaired capital assets that are still being used and how such losses should be reported in the financial statements; and guidelines for reporting insurance recoveries.

Leases

Authoritative guidance on leases can be found in the GASB's Codification, Section L20. Subject to the accounting and financial reporting distinctions of governmental funds, the criteria of FASB Statement No. 13, Accounting for Leases should be the guidelines for accounting and financial reporting for lease agreements, except for operating leases with scheduled rent increases. FASB Statement No. 13 should be consulted for specific guidance concerning detailed criteria referenced in this section. There are two (2) types of leases, "Capital" and "Operating."

Capital Leases

A capital lease is one that transfers the benefits and risks of ownership of the leased asset to the lessee. Capital leases are in substance an acquisition of a capital asset. This happens if **any one** of the following conditions is met:

- The lease transfers ownership of the property to the lessee by the end of the lease term.
- The lease contains a bargain purchase option.
- The lease term is equal to seventy-five percent or more of the estimated life of the leased property.
- The present value of the minimum lease payments exceeds 90 percent of the fair value of the leased asset at the start of the lease.

The lessee shall record a capital lease as an asset and an obligation at an amount equal to the present value at the beginning of the lease term of minimum lease payments during the lease term, excluding that portion of the payments representing executor costs such as insurance, maintenance, and taxes to be paid by the lessor, together with any profit thereon.

With capital leases, periodic payments (usually monthly) are made for principal and interest. The present value of the minimum lease payments should be reported on a modified accrual basis as both an other financing source and expenditure in the governmental fund's operating statement, even though no financial resources were actually received or disbursed by the fund. The lease down payment and subsequent principal and interest payments are reported as expenditures. For proprietary and fiduciary funds, the lease should be reported on the accrual basis as a capital asset balanced by a long-term liability.

Authority lease obligations are capital leases since ownership is vested in the LEA or LEAs (if a joint agreement) at the end of the lease term. The accounting for authority lease obligations is similar to capital leases. The authority obligation is the principal amount outstanding. If the outstanding principal amount is not known, the discounted present value of payments to be made in future years to an authority in accordance with the current schedule from the present to the fulfillment of the agreement should be used. The discount factor to be used should be known interest rate on the authority obligation.

Note: When the risks and benefits of ownership are not transferred to the LEA, the lease is considered an operating lease and the accounting consists of recording the rental payments without any recognition of the asset or related liability. Operating leases of a material amount must be disclosed in the notes to the financial statements.

Chapter 8: Debt

Debt Overview

Governmental entities borrow money on a short-term basis either to meet operating cash needs or in anticipation of long-term borrowing at later dates. LEAs usually borrow money on a long-term basis to finance capital acquisitions or construction or infrastructure improvements. Borrowing may also occur for the initial funding of a risk-retention program, the payment of a claim or judgment, or the financing of an accumulated operating deficit.

Short-term debt obligations and long-term debt obligations are defined (based on the initial maturity of the obligation) as follows:

Short-Term Obligations

Short-term obligations are loans, negotiable notes, time-bearing warrants, or leases with duration of 12 months or less, regardless of whether they extend beyond the fiscal year. Using the current financial resources measurement focus, short-term debt should be reflected in the balance sheet of the governmental fund that must repay the debt. The presentation of the liability on the balance sheet of a governmental fund implies that the debt is current and will require the use of current financial resources. Bond anticipation notes may be classified as long-term debt if the criteria of GASB Codification Section 2200 paragraphs .180 and .189 are met.

Long-term Obligations

Long-term obligations are loans, negotiable notes, time-bearing warrants, bonds, or leases with a duration of more than 12 months. Noncurrent obligations that will be repaid from revenues generated by proprietary funds should be recorded in the related proprietary fund, whereas noncurrent obligations to be repaid from governmental funds should be reported only on the government-wide statement of net assets.

General Long-Term Debt

General long-term debt is the unmatured principal debt that is secured by the general credit and full revenue powers; that is, full faith and credit, of the governmental entity. It is not a debt that is specific to a certain fund. Debt specific to a fund is a fund liability backed by the revenue power of the fund.

Debt Types

Debt instruments have different characteristics, terms and legal authority. Some various forms of debt are discussed below.

Bonds

General Obligation Bonds

General obligation bonds are direct debt instruments issued by a government that are secured by the government's taxing power.

Revenue Bonds

Revenue bonds are issued to acquire, purchase, construct, or improve major capital facilities. The revenue generated by the facility or the activity supporting the facility is pledged as security for the repayment of the debt.

- **Conduit Debt Obligations**

The term conduit debt obligations refers to certain limited-obligation revenue bonds, certificates of participation, or similar debt instruments issued by a state or local governmental entity for the express purpose of providing capital financing for a specific third party that is not a part of the issuer's financial reporting entity. Although conduit debt obligations bear the name of the governmental issuer, the issuer has no obligation for such debt beyond the resources provided by a lease or loan with the third party on whose behalf they are issued. GASB Codification Section C65 provides more information on conduit debt obligations.

Demand Bonds

Demand Bonds contain a provision permitting holders, at their discretion, to redeem the bonds at any time during its life. The demand provision is referred to as a “put” and due on-demand. Demand bonds may have variable interest rates with rates adjusted daily, weekly, or monthly. The bonds may have maturity periods of up to 30 years, and sometimes longer. The demand provisions require the issuer to repurchase the bonds upon notice from the bondholder. The repurchase price would be equal to the principal plus any accrued interest.

Reference: GASB Codification Section D30

Anticipation Notes

Tax and Revenue Anticipation Notes (TANS and TRANS)

TANS and TRANS are often issued to pay current operating expenditures prior to the receipt of the revenues. The proceeds from the revenue sources are pledged as security for the notes.

Bond Anticipation Notes (BANS)

BANS are notes with various maturities, which are issued with the anticipation of future bond sales. These are usually issued when a government is waiting for better interest rates or when it has additional projects, which would require financing through bond issuance. The Government must intend to refinance the BANS with long-term bonds, and the intent to refinance must be substantiated by either post-balance sheet issuance of long-term bonds or an execution of an acceptable financing agreement. BANS are reported as another financing source, rather than a liability of the fund that received the proceeds, if it can be demonstrated that repayment of the BANS will not require the use of current financial resources within 12 months of the reporting date because other debt was used to replace the BANS prior to the issuance of the financial statements or a qualifying financing agreement was in place that ensures financing for a period that extends at least 12 month beyond the reporting date.

Capital Leases

Capital Leases are in substance a capital asset and are considered to be debt financing. More information on capital and operating leases can be found in the capital asset chapter.

Pennsylvania LEAs:

Pennsylvania State Public School Building Authority Issue (SPSBA) was created to construct, improve, maintain, equip, and lease public school building projects. It gives LEAs the option of combining borrowed funds with one (1) or more other LEA borrowings or individual debt issuance utilizing the LEA's own credit strength. Under either option, a district leases the project to the SPSBA, and the SPSBA sub-leases the project back to the LEA. In exchange for the bond proceeds, the district makes lease rental payments that consist of the debt service payments and an administrative fee.

The Local Government Unit Debt Act (the "Debt Act") provides the framework for the issuance of debt by Pennsylvania Local Education Agencies (LEAs). The Department of Community and Economic Development (DCED) is named as the enforcement agency within the Commonwealth of Pennsylvania for the approval of debt. Please check DCED's website for details: <http://www.newpa.com/>.

Miscellaneous items regarding BONDS

Debt Service

Debt service is the cash that is required to make principal and interest payments for a given time frame. Normally bond issuers are required to pay a stated rate of interest on a bond in regular intervals (current interest bonds).

Deep Discount Debt

Deep discount debt is a bond that is selling at a discount from par value and has a coupon rate significantly less than prevailing rates. The principle and interest are paid in one lump sum on the bond's maturity date instead of making a series of regular payments. An example of deep-discount debt is a zero-coupon bond. Zero-coupon bonds are deep-discount bonds issued with a stated interest rate of zero percent. Proceeds received at issuance are far less than the face amount of the bonds. The difference represents the "interest" the investor will receive at maturity. There is no regular interest payments associated with zero-coupon bonds. Instead, interest on the debt is incorporated into the bond's inflated face value (such as U.S. Savings Bonds or Capital Appreciation Bonds).

Although debt is usually reported at face value, deep-discount debt should be reported instead at the amount of the proceeds initially received by the government. Only the initial proceeds of deep discount debt are treated as principal; accretion on the debt is treated as accrued interest payable.

Debt Issuance Costs

Debt issuance costs are those costs related to the issuance of general obligation bonds. They can include items such as bond insurance, rating fees, financial advisory / underwriting fees, solicitor and bond counsel fees, printing costs, and agent fees.

Debt issuance costs, except any portion related to prepaid insurance costs, should be recognized as an expense in the period incurred. Prepaid insurance costs should be reported as an asset and recognized as an expense in a systematic and rational manner over the duration of the related debt.

Premiums and Discounts

Premiums and discounts associated with debt are shown separately and amortized over the life of the loan using the effective interest method and are reported as an asset / liability on the fund's balance sheet. When debt is issued at a discount, the proceeds received are more than the face value. Discounts are shown as reduction of proceeds, which is recorded as an "other financing source." When debt is issued at a premium, the proceeds are less than the face value. Premiums may be recorded as an addition to bond proceeds, or they may be recorded in the fund in which the debt service payments will be recorded.

Reference: GASB Statement No. 65

Call Provisions

The call provision is the earliest date at which the issuer can repay an outstanding bond prior to maturity. Shorter call dates are more difficult to market since they benefit the issuer in terms of refunding opportunities. Other factors such as current market conditions and the size of the financing also affect the call provision.

Debt Refunding

A refunding involves the issuance of new debt whose proceeds are used to repay previously issued ("old") debt. The new debt proceeds may be used to repay the old debt immediately (current refunding); or the new debt proceeds may be placed with an escrow agent and invested until they are used to pay principal and interest on the old debt at a future time (advance refunding). Debt may be advanced refunded to take advantage of lower interest rates, extend maturity dates, revise payment schedules or remove / modify restrictions contained in the old debt agreements.

Current Refunding

The Government will borrow funds sufficient to pay off the existing bonds and to pay the costs of issuing the refunding bonds in a current refunding. This type of refunding can only occur if the call date for the bond issue has already passed or if it will occur within 90 days of the issuance of the refunding bonds.

Advance Refunding

Most advance refunded bonds result in the defeasance of debt. Defeasance of debt can be either legal or in substance. A legal defeasance occurs when debt is legally satisfied based on certain provisions in the debt instrument even though the debt is not actually paid.

In-substance defeasance occurs when debt is considered defeased for accounting and financial reporting purposes. When debt is defeased, it is no longer reported as a liability on the face of the financial statements; only the new debt is reported as a liability. In order to satisfy the requirements of an in-substance defeasance, the following conditions must exist:

- The escrow must be an irrevocable trust.
- Escrow resources can only be used exclusively to service the principal and interest payment requirements.
- The likelihood of the Government being required to make any additional future payments on this issue is remote.
- The assets in the escrow account must be risk-free as to the amount, timing and collection of interest and principal. Examples of such assets are: U.S. government securities and U.S. government- backed securities.
- The timing of principal and interest collections on investments in the escrow account must coincide in timing and amount with the scheduled principal and interest payments on the refunded debt.

When the above requirements are met, the outstanding principal balances associated with the refunded bonds are removed from the Government's Debt Account, borrowing base, and debt limit calculation. The new debt is recorded in the statement of net assets and the proceeds from the new borrowing are recorded as another financing source -proceeds from refunded bonds. The subsequent payment to the escrow agent is then recorded as another financing use -debt service-refunded bonds.

Accounting for Debt Issues

When a government issues bonds it is reported on the financial statements as of the closing date. The appropriate accounting for debt issuances depends on the type of fund that issues the debt.

Governmental Funds

In governmental funds the proceeds from the issuance of debt are recorded in the fund that is authorized to receive the cash and are recognized as an "other financing source," not as revenue. If the debt is classified as current, the fund receiving the money will also record the liability.

A government may choose to or be required to use a debt service fund for repayment of debt. *Debt service funds* are used to account and accumulate resources for the payment of general long-term debt principal and interest. Debt service funds should be used to report resources if legally mandated. Financial resources that are being accumulated for principal and interest maturing in future years also should be reported in debt service funds.

Debt service expenditures are recognized when payments are due, not when the liability occurs. Normally, interest is not accrued and expenditures are recognized when payment is made. However, Government's may recognize a July obligation at June 30th if the previous fiscal year's budget provided for the expenditure.

Proprietary Funds

Proceeds from issuance of debt in proprietary funds are recorded as a long-term liability of the fund as "bonds payable." Bonds payable is reported at the principal balance, net of any unamortized premium or discount.

Debt Service expenses are recognized when incurred. Principal payments on a proprietary fund's debt obligation are recorded as a debit to the liability account, while interest payments are charged as an expense of the fund.

Reporting Debt

The face amount of debt, underwriter's discount, original issue discount and premium, and cost of issuance must all be separately recorded in the accounting records. It is not appropriate to record only the net amount of cash received. If there is accrued interest earned and payable from date of issuance to date of sale of the debt, it is recorded in the fund that will be making the debt service payments. This interest is normally used to offset some portion of the first interest payment.

Specific Debt Issuance Examples

Examples:

Issuance of Bond at a discount:

Face Amount \$10,000; Original Issue Discount: \$500; issuance costs \$500 (\$100 prepaid insurance).

- GOVERNMENTAL FUNDS

Cash	\$9,000	
Bond Issue Expenditures	\$ 400	
Other Financing Uses – Original Issue Discount	\$ 500	
Prepaid Insurance	\$ 100	
Other Financing Sources – Bond Proceeds		\$10,000

- PROPRIETARY FUNDS

Cash	\$9,000	
Expense - Bond Issue costs	\$ 400	
Original Issue Discount	\$ 500	
Prepaid Insurance	\$ 100	
Bonds Payable		\$10,000

Issuance of Bond at a premium

The following entries would be made if the bonds were issued at a \$500 premium rather than a discount:

- GOVERNMENTAL FUNDS

Cash	\$10,000	
Bond Issue Expenditures	\$ 400	
Prepaid Insurance	\$ 100	
Other Financing Sources – Bond Proceeds		\$10,000
Other Financing Sources – Bond Premium		\$ 500

- PROPRIETARY FUNDS

Cash	\$10,000	
Expense - Bond Issue Costs	\$ 400	
Prepaid Insurance	\$ 100	
Bonds Payable		\$10,000
Other Financing Sources – Bond Premium		\$ 500

Chapter 9: Financial Reporting for Pennsylvania Local Educational Agencies (LEAs)

FINANCIAL REPORTING OBJECTIVES

The GASB sets forth six characteristics which accounting data must possess in order to be considered of value to users. These characteristics are briefly summarized as follows:

Understandability

Information should be presented as simply as possible. To be publicly accountable, a government should issue financial reports that can be understood by those that may not have a detailed knowledge of accounting principles. Reports should include explanations and interpretations that help users understand the information provided.

Reliability

The information presented should be verifiable and free from bias and should faithfully represent what it purports to represent. Information must be comprehensible and should not be misleading. Reliability is affected by the degree of estimation in the measurement process and by uncertainties inherent in what is being measured. A properly explained estimate provides more meaningful information than no estimate at all.

Relevance

Relevance encompasses many of the objectives of financial reporting. For example, if the information provided in a financial report is not timely or reliable, it is not relevant. Information can, however, meet all other objectives and still not be relevant. To be relevant, there must be a close logical relationship between the information provided and the purpose for which it is needed. Information is relevant if it is capable of making a difference in a user's assessment of a problem, condition or event.

Timeliness

To optimize value to users, financial reports must be issued promptly after the close of the related accounting cycle. Clearly, financial reports issued one (1) month after the close of the accounting cycle will be much more valuable to users than reports issued twelve months after the close of the same accounting period.

Consistency

Financial reports should be consistent over time; that is, there is a presumption that once an accounting principle or reporting method is adopted, it will be used for all similar transactions and events. This concept extends to areas such as valuation methods, basis of accounting and determination of the financial reporting entity. If accounting principles or methods have changed or if the financial reporting entity has changed, the nature and reason for the change as well as the effect of the change should be disclosed.

Comparability

Financial reports should be comparable. This does not imply that all schools perform the same functions. Comparability implies that differences between financial reports should be due to substantive differences in the underlying transactions or the governmental structure rather than due to selection of different alternatives for accounting procedures and practices.

Reference: GASB Concepts Statement No. 1, Paragraphs 62-68

Defining the Financial Reporting Entity

Financial reporting has historically emphasized transactional substance over legal form. That is to say that preparer of financial statements cannot be satisfied with including in their reports only those organizations and activities that are legally defined as being a part of the government being examined. Instead, the preparer of the report must go beyond the legal definition of the entity to include all organizations and activities that may be legally separate but are still a substantive part of the government at hand.

Specific guidelines on defining the financial reporting entity can be found in the GASB Codification Section 2100. That guidance will be briefly summarized in the paragraphs that follow.

Primary Government

The core or nucleus of the financial reporting entity is the “primary government.” All state governments and general-purpose local governments are considered to be primary governments. In addition, special-purpose governments, which include Pennsylvania LEAs, are considered to be primary governments if they meet **all** of the following criteria:

- The members of the governing body are chosen in a general election;
- The government functions as a separate legal entity; and
- The government is fiscally independent.

A government is considered to function as a separate legal entity if it enjoys the corporate rights typically associated with separate legal status. Examples of such rights include the ability to have its own legal name, the ability to sue or be sued in its own name, and the ability to own property in its own name. If an entity is *not* legally separate, it is considered to be an integral part of whichever government does exercise those powers.

A government is considered fiscally independent when it is not subject to outside interference with regard to such matters as creating a budget, setting taxes, and fees, or issuing bonded debt. Broadly imposed limitations such as; a prohibition of all school districts of a certain class within a state from issuing bonded debt, or the requirement by state governments that all schools have a balanced budget, do not meet the qualification for disallowance of fiscal independence.

It follows then that only school districts qualify as primary governments under the guidelines identified above. However, other governmental organizations such as joint ventures, jointly owned organizations, or other stand-alone organizations do form the nucleus of a financial reporting organization and must prepare financial reports. LEAs that do not meet the definition of a primary government, but which do qualify as financial reporting entities and must therefore issue financial reports include area vocational-technical schools (AVTSs), charter schools and intermediate units.

Note: The Commonwealth of Pennsylvania is not the primary government of any LEA.

Component Units

GASB Codification Section 2100.119 defines component units as legally separate organizations for which the elected officials of the primary government are financially accountable. In addition, component units can be other organizations for which the nature and significance of their relationship with a primary government are such that exclusion would cause the reporting entity's financial statements to be misleading.

The financial reporting entity includes both the primary government and all of its "component units." Component units are legally separate entities that meet *any one* of the following three (3) tests:

Test 1: The primary government appoints the voting majority of the board of the potential component unit; *and*

- Is able to impose its will on the potential component unit and/or
- Is in a relationship of financial benefit or burden with the potential component unit.

Test 2: The potential component unit is fiscally dependent upon the primary government and presents a financial benefit/burden

Test 3: The financial statements would be misleading if data from the potential component unit were not included.

It is important to note that an entity can be the component unit of only one (1) primary government. However, situations may arise when a given entity meets the criteria for inclusion as a component unit of more than one (1) primary government. For example, the state could appoint a school board and partially finance its operations (Test 1), while the school board also may be fiscally dependent upon the county (Test 2). Should such a situation arise, a decision must be made to include the school district as a component unit of one (1) or the other primary governments.

It must be reiterated here that only legally separate entities can properly be defined as "component units." The conclusion must not be drawn, however, that financial data from entities that are not "legally separate" should be excluded from the financial statements of other governments. Indeed, entities that are not legally separate are automatically included as a part of whatever government exercises legal powers on their behalf.

Financial statements of the reporting entity should provide an overview of the entity, yet allow users to distinguish between the primary government and its component units. Because of the closeness of their relationships with the primary government, some component units should be blended as though they are part of the primary government. However, most component units should be discretely presented.

Reference: GASB Codification 2100.142

Pennsylvania LEAs:

The case with an AVTS is not as immediately obvious when applying the criteria set forth above, but upon close scrutiny, the reason for independence is clear. Since it is generally the case that primary governments (school districts) appoint the board of directors that oversee the operations of the AVTS, part of the criteria of Test 1 is met. However, because the primary government does not have the direct ability to modify the AVTS budget, does not have direct control over AVTS personnel, and is not legally entitled to the AVTS resources, Test 1 is not met in its entirety. Test 2 is not met because an AVTS is generally dependent on several school districts for support. Further, Test 3 is not met because school districts disclose funds paid to AVTS entities on the annual financial report. There are, however, a few exceptions to this rule; some school districts operate a vo-tech school and have a controlling interest on the Joint Operating Committee.

Joint Ventures

Defined

GASB Codification Section J50 defines a joint venture as a legal entity or organization that results from a contractual arrangement and that is owned, operated, or governed by two or more participants as a separate and specific activity subject to joint control. GASB indicates that an arrangement should possess all of the following characteristics to be classified as a “joint venture:”

Contractual Entity

A joint venture must be an organization or legal entity that results from a contractual arrangement.

Separate Status

A joint venture must be owned, operated, or governed by two or more participants as a separate and specific activity.

Joint Control

A joint venture must be subject to joint control in which no single participant has the ability to unilaterally control the joint venture’s financial or operating policies; and On-going Financial Relationship.

A joint venture must involve either an ongoing financial interest or an ongoing financial responsibility on the part of participating governments.

An ongoing financial interest can be either direct (e.g., a right to the joint venture’s surpluses) or indirect (e.g., the ability to cause the joint venture to undertake desired projects). Ongoing financial responsibility can take the form of being “obligated in some manner” for the joint venture’s debt. Financial responsibility also arises when a joint venture’s continued existence depends upon a government’s continuing participation.

Once it has been determined that an arrangement qualifies as a “joint venture,” it must be further classified into one of two categories.

Joint Ventures with Equity Interest

An equity interest is an explicit claim to joint venture resources that can be measured based on the terms of the joint venture agreement. (For this purpose, a claim to assets upon the joint venture’s dissolution is not considered to be an equity interest).

Joint Ventures without Equity Interest

In the absence of a specific contractual formula outlining participants’ claim to joint venture assets, no explicit and measurable equity interest is deemed to exist.

Reporting

Only joint ventures with an equity interest are reported on the face of the financial statements.

Most often, a government’s explicit equity interest in a joint venture is tied to its claim to the joint venture’s fixed assets. Only that portion of a governmental fund’s equity interest (if any) that does not reflect a share of the joint venture’s fixed assets would be reported in the governmental fund.

Pennsylvania LEAs:

Most area vocational-technical schools (AVTS) and their related authorities are joint ventures of their member districts (school districts). Terms in the Articles of Agreement will dictate whether the joint venture contains an equity interest or not. This is important for determining who reports general fixed assets and AVTS/Authority debt.

It is important to note that if a school district pays the AVTS it’s (school districts) share of the debt and the area vocational-technical schools pays the authority or trustee, the school district records the payment to an expenditure account - Other Vocational Education Programs.

Other Types of Joint Arrangements

In addition to joint ventures, there are a number of other common types of joint arrangements. These include jointly governed organizations, pools, undivided interests in joint operations, and cost-sharing agreements.

Jointly Governed Organizations

Some organizations meet all of the criteria for classification as a joint venture except there is no ongoing financial interest or financial responsibility. Such arrangements are known as “jointly governed organizations.” Jointly governed organizations are not reported either on the balance sheet or in the operating statement of participating governments.

Pool

Many governments participate in pools with governments (e.g., intergovernmental investment pools). At first glance, many such pools would seem to meet the definition of a joint venture. Nonetheless, the GASB has explicitly declined to classify pools as joint ventures. The GASB reasoned that governments should already be reporting their equity interest in pools as assets on the balance sheet, and that no real benefit would be gained by classifying pools as joint ventures.

Undivided Interests in Joint Operations

In some “joint operations,” individual participating governments retain a claim to specific assets and remain responsible for specific liabilities. Such “undivided interests” in joint operations are not classified as joint ventures. Instead, participating governments simply report whatever assets and liabilities belong to them on the face of their balance sheet.

Cost-Sharing Agreements

Often governments agree to share costs without setting up a separate organization or activity. Such arrangements do not meet the definition of a joint venture and should be reported like any other similar contractual arrangement.

Annual Financial Reporting Pursuant to GASB

Pursuant to GASB Codification Section 2200, the minimum requirements for MD&A, basic financial statements, and required supplementary information other than MD&A are:

- (1) Management's discussion and analysis.
- (2) Basic financial statements. The basic financial statements should include:
 - (a) Government-wide financial statements.
 - (b) Fund financial statements.
 - (c) Notes to the financial statements.
- (3) Required supplementary information other than MD&A.

The financial reporting entity consists of (1) the primary government, (2) organizations for which the primary government is financially accountable, and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's basic financial statements to be misleading or incomplete. The reporting entity's government-wide financial statements should display information about the reporting government as a whole, distinguishing between the total primary government and its discretely presented component units as well as between the primary government's governmental and business-type activities. The reporting entity's fund financial statements should present the primary government's (including its blended component units, which are, in substance, part of the primary government) major funds individually and non-major funds in the aggregate. Funds and component units that are fiduciary in nature should be reported only in the statements of fiduciary net position and changes in fiduciary net position.

Annual Financial Reporting for Pennsylvania LEAs

The requirement for Pennsylvania Local Educational Agencies (LEAs) to submit Annual Financial Reports (AFRs) with the Pennsylvania Department of Education is in accordance with the provisions of 24 PS Sections 218 & 921-A of the School Code as follows:

“Financial accounting and reporting by LEAs shall be in accordance with Generally Accepted Accounting and Reporting Standards, except that management discussion and analysis and related notes and the following financial statements shall not be required components of the annual financial report: entity-wide financial statements, including the statement of activities and the statement of net position; the reconciliation of the balance sheet - governmental funds to statement of net position; and the reconciliation of the statement of revenues, expenditures and changes in fund balances - governmental funds to statement of activities. The Department of Education shall establish a reporting standard for the annual financial report.”

Note for Charter Schools: If a charter school has 501c(3), non-profit status, they must still file a *governmental* AFR, using the Pennsylvania Department of Education provided AFR report.

The AFR Contains the Following:

Financial Statements

- Governmental Fund Financial Statements

- Balance Sheet (NAG)

The NAG is prepared using the current financial resources measurement focus and the modified accrual basis of accounting.

- Statement of Revenues, Expenditures and Changes in Fund Balance (REG)

The REG is the operating statement of the LEA. The operations measurement focus is on sources, uses, and balances of fund financial resources.

- Proprietary Fund Financial Statements

- Statement of Net Position (NAP)

This statement is prepared using the economic resources measurement and the accrual basis of accounting. Internal Service funds are presented on this statement however the information is not included in the total column for proprietary funds.

- Statement of Revenues, Expenses and Changes in Fund Net Position (REP)

This statement is the basic statement of activities for the proprietary funds and must utilize the same major fund categories as the statement of net position. The revenues and expenses must distinguish between operating and non-operating.

- Statement of Cash Flows (CFP)

A statement of cash flows should be presented for proprietary funds based on the provisions of GASB Codification Section 2450. The direct method of presenting cash flows from operating activities (including a reconciliation of operating cash flows to operating income) should be used.

- Fiduciary Fund Financial Statements

- Statement of Fiduciary Net Position (NAF)

This statement is prepared using the economic resources measurement focus and the accrual basis of accounting.

- Statement of Changes in Net position (CNAF)

The statement of changes should include information about the additions to, deductions from, and net increase (or decrease) for the year in net position.

*This statement is not applicable to agency funds.

Other Supplemental Schedules Required by the Pennsylvania Department of Education (PDE)

In addition to the above, a number of other supplemental schedules are required to be filed as part of the Annual Financial Report. A detailed description of other required schedules and financial reports are located in the AFR User Manuals at: www.education.pa.gov

Certifications required to be filed with the AFR

- Accuracy Certification Statement (ACS)

Signed by the Chief School Administrator and Board Secretary, the ACS provides assurance that the electronic AFR data submitted, is a complete and accurate statement of the financial operations and status of the LEA and that it has been completed using GAAP and Commonwealth reporting guidelines.

- Audit Certification

An Audit Certification form submission is required for all School Types (except IUs) pursuant to Section 218 of the School Code. The audit certification is due no later than 12/31. This form requires original signatures of the Chief School Administrator and the Board Secretary.

Note: An Audit Certification Statement is not a required filing of IUs.

TYPES OF AUDITS

Local Educational Agencies (LEAs) may be involved in several different types of audits over the course of a year. Some of these audits are mandated by state and / or federal regulations, such as:

Financial Audits

School districts, charter schools, cyber charter schools or area vocational-technical schools are required by Sections 2401& 218 of the School Code to conduct annual financial statement audits of their books and records. Financial audits are designed to provide reasonable assurance about whether the audited financial statements present fairly the financial position, results of operations, and cash flows of the LEA in accordance with generally accepted accounting principles. Financial information, compliance requirements and internal controls are evaluated.

Pursuant to *24 P.S. Section 921-A* of the School Code **Intermediate Units** are required to file audited financial reports to the Pennsylvania Department of Education by October 31st of each year.

Single Audits

A single audit is an entity-wide financial audit consisting of two (2) main parts: an audit of the basic financial statements and an audit of the entity's federal assistance programs. LEAs that expend federal awards at or above the threshold established by the U.S. Office of Management and Budget during their fiscal year are required to have a single audit. Pass-through agencies and the recipients of pass-through funds must be especially cognizant of the threshold. Local, state, and federal pass-through funds should be brought to the attention of the auditor. For more information on audit requirements, please visit: <http://www.budget.pa.gov/>

Auditor General Audits

The Department of the Auditor General is authorized to perform audits of the fiscal records of all LEAs to determine whether the LEAs have received the state revenues to which they were entitled and to determine compliance with applicable state laws and regulations. For more information on Auditor General Audits please visit: <http://www.paauditor.gov/>

Calculations completed by Office of Comptroller Operations

Tuition Rate Certification

The Office of Comptroller Operations will certify and issue Elementary and Secondary Tuition Rates on the form PDE-2061 each May. The legislative basis for tuition rate certification is Section 2561 and 2562 of the School Code. Tuition rates are based on financial information from the school's Annual Financial Report (AFR) and data included on various child accounting data. It is important to note that federal expenditures are not included in the tuition rate calculation.

The tuition rate calculation is important because it is used by the school district to calculate charges made to other districts for educational services provided to non-resident students. These rates are also used to calculate certain state subsidies and non-cash deductions taken from state subsidy payments. These calculated rates may be the basis of tuition charges for students attending both Approved Private Schools (APS) and Private Residential Rehabilitative Institutions (PRRI).

Since all financial data is taken from the AFR, the amounts on the tuition rate should agree with those on the AFR, except for objects 220, Social Security Contributions and 230, Retirement Contributions. The PDE-2061 will utilize the school entity share of object 220 and 230 amounts reported on the AFR expenditure pages. All business administrators should be careful when completing the detailed expenditure section of the AFR to ensure accurate tuition rates for their school districts.

Elementary expenditures include kindergarten through sixth grade, while secondary expenditures include seventh grade through twelfth grade, inclusive. For example, if the district operates a middle school with grades six, seven, and eight, the sixth grade expenditures must be allocated and reported as elementary expenditures and seventh and eighth grade expenditures must be reported as secondary expenditures on the AFR. Incorrect allocations could have a significant effect on the district's elementary and secondary tuition rates.

Each school district should maintain a permanent tuition rate file .The PDE-2061 form for each LEA is published on the Financial Accounting Information System (FAI) upon completion.

Actual Instructional Expense (AIE)

The Office of Comptroller Operations will issue an AIE, PDE-2058, each May. The Actual Instructional Expense (AIE) calculation, PDE-2058, is defined under Section 2501 paragraph 11.1 of the School Code using financial information from the school's Annual Financial Report (AFR).

The PDE-2058 form for each LEA is published on the Financial Accounting Information System (FAI) upon completion.

Chapter 10: Advanced Accounting Issues

Accounting Changes

GASB Codification 2250.128, defines accounting changes as a change in an accounting principle, accounting estimate, or the reporting entity. The correction of an error in previously issued financial statements is not an accounting change.

Change in Accounting Principle

Defined

A change in accounting principle results from adoption of a generally accepted accounting principle different from the one used previously for reporting purposes. The term *accounting principle* includes not only accounting principles and practices but also the methods of applying them.

GAAP assumes that an accounting principle will not change once it has been adopted. Frequent changes in accounting principles used or the methods of applying them reduce comparability of financial data from one period to the next. Also, the issuance of new accounting principles by standard setting bodies (i.e., a new GASB Standard) may require a LEA to make a change in accounting principle.

Reported

The following disclosures should be made when reporting a change in accounting principle:

- Financial statements for prior periods included for comparative purposes should be presented as previously reported.
- The cumulative effect of changing to a new accounting principle on the amount of net position/fund net position at the beginning of the period in which the change is made should be reported as an adjustment to amounts previously reported.
- The adjustment to beginning net position/fund net position for the cumulative effect of changing to a new accounting principle is the difference between (a) the balance of net position/fund net position at the beginning of the period of a change and (b) the balance of net position/fund net position that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods that would have been affected.
- The effect of adopting the new accounting principle on the change in net position/fund net position of the period of the change should be disclosed.
- Changes in net position/fund net position computed on a pro forma basis should be shown on the face of the flows statements for all periods presented as if the newly adopted accounting principle had been applied during all periods affected.

Pennsylvania LEAs:

Do not revise prior years' AFRs. **Do** report the effect of the new accounting principle on beginning fund balance on the revenues, expenditures and changes in fund balance (REG) statement.

Change in Accounting Estimate

Defined

Changes in estimates used in accounting are necessary consequences of periodic presentations of financial statements. Preparing financial statements requires estimating the effects of future events. Examples of items for which estimates are necessary are uncollectible receivables, inventory obsolescence, service lives and salvage values of depreciable assets, and periods benefited by a deferred cost. Future events and their effects cannot be perceived with certainty; estimating, therefore, requires the exercise of judgment. Therefore, accounting estimates change as new events occur, as more experience is acquired, or as additional information is obtained.

Reported

A change in accounting estimate that is recognized in whole or in part by a *change in accounting principle* should be reported as a change in an estimate because the cumulative effect attributable to the change in accounting principle cannot be separated from the current or future effects of the change in estimate.

The effect of a change in accounting estimate should be accounted for in (a) the period of change if the change affects that period only or (b) the period of change and future periods if the change affects both. A change in an estimate **should not be accounted for by restating amounts reported in financial statements** of prior periods or by reporting pro forma amounts for prior periods.

- Uncollectable Taxes - Change in Estimate

A school discovered at the end of the accounting period that the allowance for uncollectible accounts for the current period was overstated or understated. To record the revised estimate, adjust the allowance and revenue accounts.

An estimated uncollectible rate could be incorrect for several years, resulting in consistently overstating or understating uncollectible amounts.

Examples:

- The uncollectible account should have been six (6) percent, instead of five (5) percent. The entry to record the revision at the end of the year would be:

$$20,000,000 \times 6\% = \$1,200,000$$

$$20,000,000 \times 5\% = \$1,000,000$$

$$\$1,200,000 - 1,000,000 = \$200,000$$

Revenue – Current Real Estate Taxes	\$200,000	
Estimated Uncollectible Taxes		\$200,000

- The uncollectible accounts were understated by \$120,000 in prior years and by \$200,000 for the current year. The change in estimate is recorded as follows in the current period.

Revenue – Current Real Estate Taxes	\$320,000	
Estimated Uncollectible Taxes		\$320,000

Pennsylvania LEAs:

Do not revise prior years' AFRs. Report the effect of the change in estimate in the period of change and in future periods, if necessary. **Do not** restate beginning fund balances/retained earnings.

Change in the Reporting Entity

Defined

One special type of change in accounting principle results in financial statements that, in effect, are those of a different reporting entity. This type is limited mainly to changing the organizations included in a reporting entity's financial statements. A different group of organizations comprise the reporting entity after each change.

Reported

Accounting changes that result in financial statements that are, in effect, the statements of a different reporting entity should be reported by restating the financial statements of all prior periods presented in order to show financial information for the new reporting entity for all periods.

Prior-Period Adjustments

Reported

Items that are reported as prior-period adjustments should, in single-period statements, be reflected as adjustments of the opening balance of net position. When comparative statements are presented, corresponding adjustments should be made of the amounts reported in the flows statement and the statement of net position for all of the periods reported therein to reflect the retroactive application of the prior-period adjustments.

When prior-period adjustments are recorded, the resulting effects on the change in net position of prior periods should be disclosed in the notes to the financial statements in the period in which the adjustments are made. When financial statements for a single period only are presented, the disclosure should indicate the effects of such restatement on the balance of net position at the beginning of the period and on the change in net position of the immediately preceding period. When financial statements for more than one period are presented, the disclosure should include the effects for each of the periods included in the statements. Disclosure of restatements in annual reports issued subsequent to the first such post-revision disclosure is not required.

Correction of an Error

A correction of an error in previously issued financial statements should be accounted for and reported as a prior-period adjustment and excluded from the change in net position section of the flows statement for the current period.

Pennsylvania LEAs:

Do not revise prior years' AFRs. Do report the effect of the new accounting principle on beginning fund balance / retained earnings on the revenues, expenditures and changes in fund balance (REG) statement.

Extraordinary and Special Items

Defined

GASB Codification Section 2200.143 thru .150

Extraordinary Items

Extraordinary items are transactions or other events that are both unusual in nature and infrequent in occurrence.

Special Items

Special items are significant transactions or other events within the control of management that is either unusual in nature or infrequent in occurrence.

Criteria

The following criteria should be met to classify an event or transaction as either unusual in nature or infrequent in occurrence:

Unusual in Nature

Unusual items are the underlying event or transaction should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the government, taking into account the environment in which the government operates.

Infrequency of Occurrence

These are the underlying events or transactions that would not reasonably be expected to recur in the foreseeable future, taking into account the environment in which the government operates.

Reported

Special and extraordinary items in the governmental fund statement of revenues, expenditures, and changes in fund balances should be reported separately after “other financing sources and uses.” Special and extraordinary items should be reported after non-operating revenues and expenses in the proprietary fund statement of revenues, expenditures, and changes in fund net position.

In addition, significant transactions or other events which are either unusual or infrequent but not within the control of management should be separately identified within the appropriate revenue or expenditure category in the statement of revenues, expenditures, and changes in fund balances or disclosed in the notes to the financial statements.

Escheat Property

Defined

Governments often take possession of property where rightful owners cannot be identified or located (i.e., estates without heirs, abandoned bank accounts). Such property is ‘escheat’ to the government.

Abandoned and unclaimed property results from either the failure of the person legally entitled to property, such as an uncashed check, to make a valid claim against your entity. If a check recipient cannot be located and the check is not claimed, the amount of the check becomes abandoned property and an unclaimed liability.

Reported

Escheat property generally should be reported as an asset in the governmental or proprietary fund to which the property ultimately escheats. Escheat property held for individuals, private organizations, or another government should be reported in a private-purpose trust fund or an agency fund, as appropriate (or in the governmental or proprietary fund in which escheat property is otherwise reported, with a corresponding liability).

When escheat property is reported in governmental or proprietary funds, escheat revenue should be reduced and a governmental or proprietary fund liability reported to the extent that it is probable that escheat property will be reclaimed and paid to claimants. The liability should represent the best estimate of the amount ultimately expected to be reclaimed and paid, giving effect to such factors as previous and current trends in amounts reclaimed and paid relative to amount escheated, and anticipated changes in those trends. (This liability may differ from the amount specified in law to be separately held for payments to claimants.)

Pennsylvania LEAs:

Pennsylvania LEAs should account for escheat assets in the fund to which the property will ultimately be recorded to be remitted to the State Treasurer, i.e., the general fund. An unclaimed and abandoned property liability account should be established to report your best estimate of the amount expected to be reclaimed and paid to the legal owner or remitted to the State Treasurer.

Pennsylvania law stipulates that most property types are presumed to be abandoned or unclaimed if the owner had not taken specific action regarding the property for three years. LEAs should refer to Pennsylvania's Unclaimed Property Act for additional information. The Act along with other information regarding unclaimed property can be found at: www.patreasury.org