

**Manual of Accounting and Financial Reporting for  
Pennsylvania Public Schools**

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**Chapter 1**

# Chapter 1

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## Principles of Accounting, Budgeting, and Financial Reporting for Pennsylvania Local Education Agencies (LEAs)

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**\*\* Updated 5/1/05 \*\***

This Chapter describes the accounting and financial environment in which Local Education Agencies (LEAs) operate. This environment follows governmental accounting standards and differs significantly from private sector accounting. Chapter 1 will discuss the following topics:

- ❖ Three key groups instrumental in providing assistance to LEAs in Pennsylvania;
- ❖ Generally Accepted Accounting Principles (GAAP) And The Governmental Environment;
- ❖ The Establishment Of The Governmental Accounting Standards Board (GASB);
- ❖ The Authoritative Sources Of Governmental Accounting Principles;
- ❖ The GASB Standard Setting Process;
- ❖ The Twelve Governmental Accounting Principles.

### ❖ *The Pennsylvania Department of Education (PDE)*

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 Department of Education to administer school laws and assist school districts in providing educational programming to Pennsylvanians.

The mission of the Pennsylvania Department of Education (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. To learn more about the PDE please refer to its website [www.pde.state.pa.us](http://www.pde.state.pa.us)

### ❖ *The Labor, Education and Community Service (LECS) Comptroller's Office*

The LECS Comptroller's Office is part of the Office of the Budget of the Commonwealth of PA. The Comptroller's Office works in tandem with the Department of Education in assisting the Secretary of Education and Governor in enforcing established policies and standards regulating the expenditure of public funds, and advises on the formulation of financial policy. These goals are accomplished by providing payments, support and accounting related information to school entities.

The School Finance Division of this office processes over \$6.8 billion in payments to schools throughout the fiscal year. The Federal subsidies section processes over \$1.3 billion in federally sponsored payments.

The collection, processing and review of the Annual Financial Report (PDE forms 2056 and 2057) is under the purview of this office. Other functions of this office include the maintenance of a uniform accounting manual, Chart of Accounts and calculations of the tuition rate, actual instructional expense and restricted indirect cost rate. Additional information regarding the LECS Comptroller's Office can be found at [www.pde.state.pa.us/school\\_acct](http://www.pde.state.pa.us/school_acct)

### ❖ *The Role of the PASBO Accounting Committee*

The Pennsylvania Association of School Business Officials (PASBO) accounting committee is one of the major PASBO committees. The number and makeup of the accounting Committee is determined annually by the PASBO president. The committee's purpose is to review and comment upon all matters relevant to school or governmental accounting and to act in an advisory



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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.

Currently, there are about 20 committee members with a wide range of experience and credentials from school districts, intermediate units, vocational-technical schools, CPA firms, and the Commonwealth of PA LECS Comptroller's Office and Bureau of Audits. These members share a strong spirit of dedication, professionalism and teamwork to address major accounting issues for school business officials.

Each year the committee makes significant progress concerning several major issues affecting school accounting. At times, technical accounting sub-committees are established to address a particular issue in more detail for the accounting committee.

### ❖ **Generally Accepted Accounting Principles (GAAP), The Government Environment, And Governmental Accounting Standards Board (GASB)**

Generally Accepted Accounting Principles (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, to develop the GASB as a separate, but independent, standards-setting organization that would be responsive to the unique financial environment in government. The GASB was established in 1984 and is the successor organization to the NCGA.

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, the budget as an expression of public policy and financial intent and 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 interperiod equity and the idea that governmental financial reporting should provide information on whether current-year revenues were sufficient to pay for current-year expenditures. This concept might be likened in some ways to a measure of annual profit or loss and might therefore eventually result in governmental reporting that is more similar to that for the private sector.

### ❖ **Authority Of Government Accounting Standards Board (GASB) Standards**

The AICPA's Ethics Rule 203 provides that a member of the AICPA will not express an opinion that financial statements are presented in conformity with GAAP if such statements contain any departure from an accounting principle promulgated by bodies designated by the AICPA to establish such principles. The AICPA has designated the GASB as the body to establish financial accounting principles for state and local government pursuant to Rule 203. Therefore, to receive a "clean" auditor's opinion, a government must apply GASB standards.

GASB standards are not the only source of GAAP for governments, however. The "hierarchy" of GAAP for governments is governed by the AICPA Auditing Standards Board Statement No. 69, *The Meaning of "Present Fairly in Conformity with Generally Accepted Accounting Principles" in the Auditor's Report*, which was issued in January 1992. That hierarchy lists the priority sequence of pronouncements that an entity should look to for accounting and reporting guidance. By definition, guidance at a higher level of this hierarchy supercedes any inconsistent guidance at a lower level. With regard to state and local governments, the sequential order of the hierarchy beginning with the great authority is as follows:

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<b>LEVEL 1</b>	<p><b>GASB Statements and Interpretations</b></p> <p>Also, AICPA and FASB pronouncements specifically made applicable to state and local governments by GASB Statements or Interpretations. Level 1 guidance can be found in GASB's <u>Codification of Governmental Accounting and Financial Reporting Standards</u>, issued annually. The Codification has the same authority as the original GASB pronouncements. Major governmental accounting issues are published in GASB statements only after all aspects of due process described in the next section have occurred.</p>
<b>LEVEL 2</b>	<p><b>GASB Technical Bulletins</b></p> <p>Also, if specifically made applicable to governments by the AICPA and cleared by the GASB: AICPA Industry Audit and Accounting Guides and AICPA Statements of Position.</p>
<b>LEVEL 3</b>	<p><b>AICPA Practice Bulletins</b></p> <p>If specifically made applicable to governments and cleared by the GASB. Also, consensus positions of a group of accountants organized by the GASB that attempts to reach consensus positions on accounting issues applicable to governments. (Note that the GASB has not yet organized such a group.)</p>
<b>LEVEL 4</b>	<p><b>Implementation Guides</b></p> <p>(Known as Q&amp;As for their question-and-answer format), published by the GASB staff. Also, practices widely recognized and prevalent in state and local government.</p>
<b>LEVEL 5</b>	<p><b>Other Accounting Literature</b></p> <p>Including GASB Concepts Statements and AICPA and FASB pronouncements when not specifically made applicable to government by the GASB.</p>

This hierarchy was developed as a result of a review of the GASB's standards-setting structure in 1989. One significant problem identified during that review was that the GASB expended too much of its efforts reacting to newly-issued FASB standards. That was because the previous hierarchy provided that, in the absence of a GASB standard, governments were required to follow FASB standards. Thus, when the FASB, which had a more mature agenda and standards-setting process, issued a pronouncement on a topic that had broad or significant applicability to government but that also was a topic the GASB was addressing, the GASB often would issue a pronouncement to "block" the applicability of the FASB standard to governments. The change in the hierarchy was designed to alleviate this diversion of GASB resources as well as the negative impression that such "blocking" brought to the standards-setting process.

Another significant issue of the 1989 structural review was the GASB's jurisdiction as the standards setter for all governmental entities. Since 1984, it had been agreed that the FASB would set standards for private sector entities – both commercial and not-for-profit organizations --- and the GASB would set standards for state and local governmental entities. Some industries exist in two or all three of these categories, such as colleges and universities, hospitals and utilities. These industries, known as “special entities,” had become increasingly disgruntled by the differences in GAAP within their industries that resulted from having two standards-setting Boards. During the structural review, those special entities requested that the standards-setting responsibilities for their industries be assigned to a single board. However, the FAF reaffirmed that the GASB's jurisdiction encompassed all governmental entities, including special entities, not only when they are included as part of a government's financial report, but also when they issue their own separate financial statements.

### ❖ *The Standards-Setting Process*

The GASB is the highest source of accounting and financial reporting guidance for state and local governments. The GASB is comprised of seven members with diverse backgrounds related to government. With the exception of the Chairman of the GASB, those members serve part-time. Although the GASB functions under the sponsorship and oversight of the FAF, it is independent of that organization in its standards-setting function. The GASB consults on its standards-setting process with the Governmental Accounting Standards Advisory Council (GASAC), a large body comprising representatives of major groups interested in governmental GAAP, such as the AICPA and the GFOA, who provide the Board counsel and who serve as liaison between the GASB and their representational organizations. The GASB is served by a staff of approximately a dozen professional accountants, most of whom have extensive experience in government.

The GASB may only issue Statements and Interpretations after extensive “due process.” Due process is a method designed to ensure that all parties interested in governmental GAAP have the opportunity to make their positions known to the GASB during the course of its deliberations. The GASB decides when to add an accounting issue to its technical agenda. Potential issues are identified through various sources, such as public hearings, the GASAC, written requests by constituents, and GASB staff. GASB staff will research agenda projects, often with the assistance of a task force of knowledgeable individuals appointed by the GASB Chairman. Once the project is researched, the GASB staff may issue a Discussion Memorandum (DM) or an Invitation to Comment (ITC) to outline the basic problems and potential solutions and to solicit public comment. Public hearings may be held on the document.

Once the GASB has considered the responses to the DM or ITC, it arrives at tentative conclusions on how to resolve the issue. At that point, the GASB may issue a Preliminary Views (PV) on a potential solution or an Exposure Draft (ED) of a proposed Statement or Interpretation that outlines the guidance being proposed. Again, the GASB solicits public comments in writing and at public hearings.

Final Statements and Interpretations, which are consecutively numbered, are issued after the GASB has considered the responses to an ED of the proposed guidance. If

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that consideration causes the GASB to determine that it should materially change the proposed guidance, a revised ED would be issued.

The GASB also issues Technical Bulletins (TBs) and Implementation Guides (Q&As). Because these are staff documents, they are not subject to the due process described earlier. However, the GASB staff does seek input from knowledgeable persons on drafts of these documents and they may not be issued if a majority of the GASB objects to their release. The standard-setting process is illustrated on the following page.

### ❖ [The Twelve Principles Of Accounting, Budgeting And Financial Reporting For Pennsylvania Local Education Agencies \(LEAs\)](#)

In 1979, the National Council on Governmental Accounting (NCGA) set forth twelve (12) basic principles of accounting and financial reporting in Statement 1, Governmental Accounting and Financial Reporting Principles. The principles established in Statement 1 are accepted 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).

The accounting, budgeting and financial reporting principles for Pennsylvania Local Education Agencies (LEAs) presented in this manual are based on the principles detailed in Statement 1.

Adoption of the accounting principles described herein will (a) provide management with financial information that presents fairly and with full disclosure the financial position and results of financial operations of the LEA; (b) provide reliable financial information as a basis for program evaluation and budgetary planning; (c) give the LEA'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 LEA's accounting system; and (d) enhance the comparability of LEA financial reporting.

## STATEMENT AND EXPLANATION OF THE TWELVE (12) ACCOUNTING PRINCIPLES APPLICABLE TO LEAs. A detailed explanation follows each principle.

### PRINCIPLE 1

#### Accounting And Reporting Capabilities

The accounting system of an LEA shall provide the information necessary to: (a) prepare financial reports that present fairly and with full disclosure the financial position and results of financial operations of the funds and account groups of the LEA in conformity with generally accepted accounting principles (GAAP); (b) determine and demonstrate compliance with finance-related and contractual provisions (such as subsidy calculations).

#### *Explanation:*

LEAs annual financial reporting to the Pennsylvania Department of Education (PDE) Comptroller's Office and other external users will be in accordance with

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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 accounting principles advocated relate to year-end financial reporting. An LEA is encouraged to adopt the principles and practices in the preparation of internal interim financial reports and at a minimum to use accounting and encumbrance procedures that properly reflect the results of operations and give a true picture of the LEA's financial position.

An LEA can continue to maintain its accounting records on the basis currently used; but at year-end, it must make and record the accounting adjustments necessary to meet the financial reporting requirements established in this manual.

An LEA's 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 System

The LEA accounting system must be organized and operated on a fund basis.

#### *Explanation:*

Governmental accounting systems must be organized and operated on a fund basis. The diverse nature of governmental operations and the necessity of assuring legal compliance preclude recording and summarizing financial transactions in a single accounting entity. Instead, the required accounts are organized on the basis of funds, each of which is completely independent of any other. Each fund must be so accounted for that the identity of its resources, obligations, revenues, expenditures, and fund equities is continually maintained.

A fund is a fiscal and accounting entity, with a self-balancing set of accounts recording cash and other resources, together with all related liabilities and residual equities or balances, or changes therein. Funds are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

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## PRINCIPLE 3

### Types Of Funds

The fund accounting system concept involves an accounting segregation, not necessarily the physical separation of resources; e.g., separate funds may combine their cash for investment purposes. Thus the Capital Reserve Fund could combine its cash with that of the General Fund to get a better return on an investment while the accounting records would maintain the investment independently for each fund. However, resources may also be physically segregated.

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 school laws. Adherence to legal and GAAP requirements results in the following types of funds for Pennsylvania LEAs. There are different categories and types of funds. Listed below are the three (3) major fund categories, the specific fund types located within those categories, and the two account groups. All funds must be classified within the following categories:

#### **A. Governmental Funds (Emphasizing Major Funds)**

1. General Fund
2. Special Revenue Fund
3. Capital Projects Fund
4. Debt Service Fund
5. Permanent Funds

#### **B. Proprietary Funds**

6. Enterprise Fund (Emphasizing Major Funds)
7. Internal Service Fund

#### **C. Fiduciary Funds**

8. Pension (And Other Employee Benefit) Trust Funds. These funds 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 plan, or other employee benefit plans.
9. Investment Trust Funds. These funds report the external portion of investment pools reported by the sponsoring LEA, as required by Statement No. 31, paragraph 18.
10. Private-Purpose Trust Funds. These funds should be used to report all other trust arrangements under which principal and income benefit individuals, private organizations, or other governments.
11. Agency Funds.

See Chapter 2 for details on funds and fund accounting.

## PRINCIPLE 4

### Number Of Funds

LEAs 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.

#### *Explanation:*

The general rule is to establish the minimum number of separate funds consistent with legal specifications, operational requirements and the principles of fund classification discussed previously. Using too many funds causes inflexibility and undue complexity in budgeting, accounting, and other phases of financial management, and is best avoided in the interest of efficient and economical financial administration. Only one general fund should be maintained.

Some LEAs may need several funds of a single type such as Activity or Capital Reserve Funds. Some LEAs may find it necessary to use only a few of the specified types of funds.

## PRINCIPLE 5

### Accounting For Capital Assets And Long-Term Liabilities

Capital assets include land, improvement to land, easements, buildings, building improvements, vehicles, machinery, equipment, works of art and historical treasures, infrastructure, and all other tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period.

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. Examples of infrastructure assets include roads, bridges, tunnels, drainage systems, water and sewer systems, dams and lighting systems.

A clear distinction should be made between general capital assets and capital assets of proprietary (business-type activities and internal services funds) and fiduciary funds.

- Capital assets of proprietary funds (enterprise and internal service) should be reported in both the government-wide and fund financial statements.
- Capital assets of fiduciary funds should be reported only in the statement of fiduciary net assets.
- 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 assets.

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Likewise, 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 assets. 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 assets and in the government-wide statement of net assets.
- Long-term liabilities directly related to and expected to be paid from fiduciary funds should be reported in the statement of fiduciary net assets.

All other unmatured 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 assets.

## PRINCIPLE 6

### Valuation Of Capital Assets

LEA capital assets should be recorded at cost or estimated cost. Donated capital assets should be recorded at fair market value at the time received.

#### *Explanation:*

Capital assets are valued at cost. If cost cannot be reasonably determined, then an estimated cost should be used. Capital assets that are contributed are accounted for at the fair value at the time received.

Capital assets require capitalization of costs and charges for the asset classes; land, buildings, improvements, machinery and equipment and construction in progress. In the case of land, these costs and charges include: legal and title fees, surveying fees, appraisal and negotiation fees, damage payments, site preparation costs and demolitions.

Costs of buildings and improvements others than land include the purchase price, contract price, or job order cost; professional fees of architects, attorneys, appraisers, financial advisors, etc.; damage claims, costs of fixtures attached to a building or other structure; insurance premiums, interest, and related costs incurred during the period of construction; and any other expenditures necessary to put a building or structure into its intended state of operation. Machinery and equipment costs should include the total purchase price less any trade-in allowances, transportation charges, installation costs, taxes, and any other expenditures required to place the asset in its intended state of operation.

## PRINCIPLE 7

### Depreciation 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.

#### *Explanation:*

Capital assets must be depreciated over their estimated useful lives unless they are either inexhaustible (such as land and land improvements) or are infrastructure assets reported using the *modified approach*. Infrastructure assets that are part of a network or subsystem of a network are not required to be depreciated as long as the following two (2) requirements are met:

1. The LEA manages that the eligible infrastructure assets using an asset management system that has the characteristics listed below:
  - Has an up-to-date inventory of eligible infrastructure assets.
  - Performs condition assessment of the eligible infrastructure assets and summarizes the results using a measurement scale.
  - Estimates each year the annual amount to maintain and preserve the eligible infrastructure assets at the condition level established and disclosed by the LEA.
2. The LEA documents that the eligible infrastructure assets are being preserved approximately at (or above) a condition level established and disclosed by the LEA.

Depreciation expense should be reported in the following statements:

- Government-wide statement of activities;
- The proprietary fund statement of revenues, expenditures and changes in fund net assets; and
- The statement of changes in fiduciary net assets.

## PRINCIPLE 8

### Accrual Basis In Governmental Accounting

- *Modified Accrual Basis of Accounting*  
In their reporting, LEAs must use the modified accrual basis of accounting for governmental funds, and agency funds.
- *Accrual Basis of Accounting*  
In their reporting, LEAs must use the accrual basis of accounting for proprietary funds and fiduciary funds.

See Chapter 2 for specific advice on basis of accounting.

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*In addition:*

LEAs are required to prepare both *government-wide financial statements* and *fund financial statements*.

- **Government-wide Financial Statements**

The statement of net assets and the statement of activities are the two (2) government-wide financial statements that are required to be prepared. These statements should be prepared using the accrual basis of accounting.

- **Fund Financial Statements**

The modified accrual or accrual basis of accounting, as described earlier in this principle, should be used in measuring financial position and operating results.

## PRINCIPLE 9

### Budgeting, Budgetary Control And Budgetary Reporting

- LEAs must by law adopt an annual budget for the General Fund. LEAs should prepare an annual budget for every fund. The General fund and Special Revenue Fund budgets are reported in the financial statements.
- The accounting system should provide the basis for appropriate budgetary control.
- LEAs shall prepare the General Fund Budget revenue and expenditure estimates on the modified accrual basis.
- Presentations to external users of an LEA's General Fund Budget must be in a fund balance to fund balance format
- Budgetary comparisons should be included in the appropriate financial statements and schedules for governmental funds for which an annual budget has been adopted

## PRINCIPLE 10

### Revenue, Expenditure, Transfer And Expense Account Classification

An LEA should provide for the classification of revenues, expenditures and expenses into certain specific categories.

*Explanation:*

1. Revenue, Expenditure and Expense Account Classification
  - a) Governmental Funds

### Revenue

Revenues are increases in fund financial resources and do not include interfund transfers, debt issue proceeds or refunds of prior year expenditures. General long-term debt proceeds, fund transfers-in and refunds of prior year expenditures are classified as “Other Financing Sources,” not as revenue.

Revenues of governmental funds should be classified by fund and source. The major revenue sources for LEAs in Pennsylvania are taxes, state subsidies and federal grants. Refer to the revenue section of the Chart of Accounts in this manual for specific information concerning revenues

### Expenditures

Expenditures are decreases in fund financial resources and represent charges incurred, whether paid or not paid, which benefit the current year. Interfund transfers are not classified as expenditures, but instead are classified as “Other Financing Uses.”

Expenditures are classified in this manual by fund, function, object, funding source and instructional organization as required dimensions for reporting purposes. See the expenditure section of the Chart of Accounts in this manual for specific information concerning expenditures.

#### b) Proprietary Funds

The classification of revenues and expenses for proprietary funds are essentially like those of private business organizations. The term “expenses” rather than the term “expenditures” is used with proprietary funds.

Expenses are charges incurred, whether paid or unpaid, for operation, maintenance, interest and other charges that benefit the current fiscal period. The major difference between expenses and expenditures is that expenses include the allocation of costs (e.g., depreciation) and expenditures do not.

2. Transfers And Interfund Transactions are distinguished from revenues, expenses, or expenditures in financial statements and are categorized as follows:

*NOTE:* The question of the legality of certain fund transfers is not addressed here.

- a) Operating Transfers are those amounts intended to be used in the operations of the fund to which transferred. These transfers usually would be of a routine or recurring nature. An example of such transfers would be the transfers on a regular basis to the Food Service Fund to defray operating costs. Operating transfers should be reported as a

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separate item in the statement of revenues and expenditures / expenses, and not included as part of revenues or expenditures on the financial statements.

- b) Interfund Transactions are not considered transfers. The following types of interfund transactions are accounted for as fund revenues, expenditures or expenses (as appropriate), or adjustments thereto:
- ❖ Quasi-External Transactions are transactions that are internal but for accounting purposes are treated in the same manner as transactions involving unrelated parties (organizations external to the LEA). Quasi-external transactions are accounted for as revenues, expenditures or expenses of the funds involved.
  - ❖ Reimbursements are transactions that constitute reimbursements to a fund of expenditures or expense initially made from it that are properly applicable to another fund. Such transactions are recorded as expenditures or expenses in the reimbursing fund and as reductions of the expenditures or expenses in the fund that is reimbursed.

## PRINCIPLE 11

### Common Terminology And Classification

LEAs consistently utilize the terminology and classification as defined in the Manual of Accounting and Related Financial Procedures for Pennsylvania School Systems (Revised) throughout the budget, accounts and financial reports of each fund.

#### *Explanation:*

The terminology and classification used in this manual generally conforms to the standard accounting terminology for governmental entities as reflected in professional publications including Codification of Governmental Accounting and Financial Reporting Standards, as of June 30, 2002 published by the Governmental Accounting Standards Board (GASB) and Governmental Accounting, Auditing and Financial Reporting, 2001 Edition, published by the Government Finance Officers Association (GFOA).

## PRINCIPLE 12

### Interim And Annual Financial Reports

LEAs should prepare) Basic Financial Statements as described in this Manual. Interim financial statements should be prepared to facilitate management control of financial operations. A Comprehensive Annual Financial Report (CAFR) should be issued by every LEA (*Codification 1100.112*) – See Chapter 15 for information concerning the CAFR.

#### *Explanation:*

Each LEA must prepare and issue Annual Financial Reports (AFR).

Requirements and standards for LEA financial reporting are derived from:

- Recognized GAAP for governmental entities;
- State laws and regulations;
- Bond indentures and contractual agreements; and
- Federally assisted program compliance requirements.

The financial statements required for state reporting purposes are patterned after the Basic Financial Statements (BFS) detailed in GASB Statement #34. The BFS provide financial report users with an overview and broad perspective of the financial position and results of operations of the LEA as a whole.

The BFS are considered the minimum acceptable financial statements necessary for a fair presentation of the financial condition of the LEA in accordance with GAAP. BFS are the following statements:

- Government Wide Financial Statements
- Governmental Fund Financial Statements
- Proprietary Fund Financial Statements
- Fiduciary Fund Financial Statements
- Note Disclosure to the Financial Statements

#### PDE Financial Reporting Requirements

LEAs should prepare their annual financial statements in accordance with the accounting principles outlined in this manual. In addition to the BFS listed, LEAs are also required to submit an MD & A and the Schedules included as part of the AFR package. Annual Financial Reports for school district type entities are due in the Labor, Education and Community Services Comptroller's Office by October 30<sup>th</sup>, following the close of the fiscal reporting period, i.e., July 1<sup>st</sup> through June 30<sup>th</sup>. Intermediate Unit AFRs are due on October 1.

The Comprehensive Annual Financial Report (CAFR) should include an introductory section, management's discussion and analysis (MD & A), basic financial statements (government-wide financial statements, fund financial statements and notes to the financial statements), required supplementary information other than MD & A, combining and individual fund statements, schedules, narrative explanations and statistical section. See Chapter 15 for detailed information concerning the AFR, CAFR and other reports.

## **Chapter 1**

*Principles of Accounting, Budgeting, and Financial Reporting for Pennsylvania Local Education Agencies (LEA)*

### **1.16**