Manual of Accounting and Financial Reporting for Pennsylvania Public Schools

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Chapter 13

Accruals and Deferrals

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This Chapter describes the application of the accounting conventions of accruals and deferrals to the operations of Local Education Agencies (LEAs). Specifically, the Chapter defines the occasions and type of transactions that merit the use of accruals and deferrals. The application of these concepts is very important because they help to better define and clarify the financial position of the LEA. This increase in financial precision is accomplished due to the manner in which accruals and deferrals provide a more accurate representation, at fiscal year end, of both the revenues at the LEA's disposal and the obligations for which they are liable. Chapters 1 and 4 include descriptions of the accounting techniques and the theory used to implement accruals and deferrals. This Chapter will discuss the following topics:

- Types Of LEA Revenues That May Be Accrued Or Deferred; and
- ❖ Types Of LEA Expenditures That May Be Accrued Or Deferred.

Accruals and Deferrals

Accruals and deferrals are necessary to recognize revenues and expenditures in the proper accounting period. Revenues should be recognized in the period in which they are earned and, in some instances, become measurable regardless of when cash is received. Expenditures should be recognized when the obligation to pay occurs regardless of when cash is disbursed. Obligation to pay occurs when goods or services are received by the LEA. Under this method of accounting, revenues and expenditures are matched to the fiscal period of benefit. The accounting entry records the transaction in the balance sheet accounts and as revenue or expenditure in the subsidiary ledgers.

GASB Statement #33, Accounting and Financial Reporting for Nonexchange Transactions, states that the modified accrual basis of accounting is used for the recognition of local tax revenue. This basis requires that revenues are measurable and available, i.e., in time to pay liabilities of the current period. Expenditures are recognized when the liability is incurred. The modified accrual basis of accounting should be used for all funds except proprietary funds and fiduciary funds.

Statement #33 defines revenue recognition with respect to the timing of nonexchange transactions. A nonexchange transaction involves a government giving or receiving value without directly receiving or giving equal value in return. 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, Statement #33 requires that all applicable eligibility requirements are met **and** the resources are available and measurable.

Statement #33 groups nonexchange transactions into four (4) classes and provides guidance for the timing of recognition for each type. This guidance is based on the usage of the accrual basis of accounting. Any revenues reported using the modified accrual basis of accounting, in addition to the following criteria, must have the resources available and measurable.

<u>Class 1: Derived Tax Revenues</u> – Revenues gained as a result of assessments by a government on exchange transactions. Income taxes are an example of a derived tax. Derived tax revenues should be recognized when the transaction takes place unless there are time constraints placed on the resources. If time constraints are placed on the revenues, then the revenues should be deferred until such time requirements are met.

<u>Class 2: Imposed Nonexchange Revenues</u> – Revenues gained as a result of assessments by governments on nongovernmental entities, that are not assessments on exchange transactions. An example of an imposed nonexchange revenue is a property tax. Revenue recognition should be delayed until the applicable period if there are time constraints. For property taxes, this is the time period for which the

taxes are levied. Resources received before the time requirements are met should be treated as deferred revenues.

<u>Class 3: Government-Mandated Nonexchange Transactions</u> – Revenues that result when one (1) government provides resources to another government at another level and mandates a specific usage of those resources. The provider government establishes purpose restrictions and may also impose time restrictions. Revenues should be recognized at the same time that receivables are recognized, ie., when all applicable eligibility requirements are met. Revenues received before the applicable time period should be recognized as advances (providers) and deferred revenues (recipients).

Government-mandated grants require revenue recognition as of the **beginning** of the fiscal year of the granting government. Grant revenue will not be recognized when expenditures occur but when the revenue becomes available. If any portion of this revenue becomes unpayable due to cancellation of an appropriation, the school will reduce the receivable and revenue.

<u>Class 4: Voluntary Nonexchange Transactions</u> – Revenues that result from legislative or contractual agreements, other than exchanges, entered into willingly by two (2) or more entities. Revenues should be recognized at the same time that receivables are recognized, i.e., when all applicable eligibility requirements are met. Revenues received before the applicable time period should be recognized as advances (providers) and deferred revenues (recipients).

CLASSES AND TIMING OF RECOGNITION OF NONEXCHANGE TRANSACTIONS						
Class	Recognition					
Derived Tax Revenues Examples: sales taxes, personal and corporate income taxes, motor fuel taxes, and similar taxes on earnings or consumption	Assets Period when underlying exchange has occurred or when resources are received, whichever is first. Revenues Period when underlying exchange has occurred. (Report advance receipts as deferred revenues.) When modified accrual accounting is used, resources also should be "available." See paragraphs 16 and 30a.					
Imposed Nonexchange Revenues Examples: property taxes, most fines and forfeitures	Assets Period when an enforceable legal claim has arisen or when resources are received, whichever is first. Revenues 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 also should be "available." (For property taxes, apply NCGA Interpretaion 3, as amended.) See paragraphs 17, 18, 30b, and 30c.					
Government-mandated Nonexchange Transactions Examples: federal government mandates on state and local governments Voluntary Nonexchange Transactions Examples: certain grants and entitlements, most donations	Assets And Liabilities Period when all eligibility requirements have been met or (for asset recognition) when resources are received, whichever is first. Revenues And Expenses Or Expenditures Period when all eligibility requirements have been met. (Report advance receipts or payments for use in the following period as deferred revenues or advances, respectively. 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 and expenses or expenditures when the resources are, respectively, received or paid and report resulting net assets, equity, or fund balance as restricted.) When modified accrual accounting is used for revenue recognition, resources also should be "available." See paragraphs 19 through 25 and 30d.					

Source: GASB Statement #33

Credit: "Portions of GASB Statement #33, Accounting and Financial Reporting for Nonexchange Transactions, copyright by the Governmental Accounting Standards Board, 401 Merritt 7, Norwalk, Connecticut 06856 are reproduced by permission. Copies of the complete document are available from the GASB."

* Revenue Accruals

Those revenues that the LEA has deemed to be earned prior to the close of the fiscal year, but which have not been received into LEA accounts at that time, should be accrued as an asset, that is accounts receivable and as a revenue. This accrued revenue should be considered revenue for the current year ending at June 30th.

Prior to GASB Interpretation #6, some controversy existed regarding the length of time after the close of the fiscal year for which expected resources should be accrued in governmental funds. The GASB's *Codification*, Section 1600.106 explains that, under the concept of modified accrual accounting, the LEA should recognize revenue when it is **both** measurable and available. This terminology has led to varying interpretations regarding the length of time beyond fiscal year end that the LEA may recognize revenue for inclusion in the current year. Governmental accounting standards define revenue as "available" if it is collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Each LEA should establish and maintain a written policy regarding any time periods for the definition of revenue recognition. This established policy should be adhered to from year to year to maintain consistency in accounting methods and should not be applied in such a way as to result in uneven recognition.

Some LEA's mistakenly apply a 60-day rule for all revenues before making a determination as to whether or not an accrual is required. This is incorrect. Significant revenues of the period should be recognized even if collected outside the LEA's normal accrual period, if exclusions would be misleading to financial statement readers.

Professional judgment must be exercised when evaluating revenues for accrual determinations. The issue of materiality and unusual circumstances must also be considered when determining the feasibility of accruals. For example, if an unusual circumstance causes the receipt of state revenue to be delayed beyond the current fiscal period, the revenue should still be recognized in the current fiscal year, if significant.

Local taxes, state subsidies, federal subsidies, interest and other local revenue sources may all be accrued at the end of the fiscal year. Local taxes collected on behalf of the LEA before June 30th and remitted to the school in the next fiscal year should be recognized as a tax receivable and tax revenue in the year of levy.

When state subsidies due in the current fiscal year will be received in the subsequent fiscal year, the revenue should be accrued if all eligibility requirements have been met. Social Security and Retirement Subsidies should be accrued for the related salaries and benefits. If there is an amount due to the school on the reconciliations of the state share of Social Security and PSERS contributions, that should be accrued at June 30th, along with the related salaries and benefit expenditures.

Federal subsidies that have not been received by June 30th for approved program expenditures need to be accrued if expenditures have been incurred and all eligibility criteria have been met.

Possible reven	ue accruals checklist follows:
F C V F	Property Per Capita Decupation Vage Real Estate Transfer Delinquent
☐Inter	est
Tuiti	on Receivable
Reve	enues From Intermediate Unit Sources
Othe	er Revenues From Local Sources
Basi	c Education / Revisions (Plus)
Soci	al Security Subsidy
Retir	rement Subsidy
Rent	al And Sinking Fund Payment Reimbursements
Othe	er State Subsidies
Fede	eral Subsidies
Rein	nbursements Due From Other LEAs
(<u>Ex. 13-1)</u>	The county collected \$5,000.00 of real estate transfer taxes during the month of June and will remit them to the LEA in July. On June 30, the revenue is accrued.
	DR 0141 Intergovernmental Accounts Receivable \$ 5,000.00 CR 0302 Revenue Control \$ 5,000.00
(<u>Ex. 13-2)</u>	The LEA received \$75,000.00 of a \$100,000.00 federal grant. The grant was fully expended before June 30. On June 30, the \$25,000.00 due to the LEA is accrued.
	DR 0143 Federal Subsidies Receivable \$ 25,000.00 CR 0302 Revenue Control \$ 25,000.00

* Revenue Deferrals

If the LEA has received revenue prior to the fiscal year end that does not qualify as revenue earned for the current year, that revenue must be deferred to the following year. The methods of accounting for deferred taxes are explained in the General Fund Accounting Entries Section of Chapter 4.

Federal Subsidies received before June 30th that will be expended in the subsequent year must be deferred if the program requires expenditures are incurred before revenue is earned.

A list of some i	evenues that might be deferred for	ollows:			
Receipt Of	Money Before Eligibility Requiren	nents Are Met			
Local Taxes	s Received In Advance of the Fisc	cal Year For Whic	h They Ar	e Levi	ed
	e Driven State And Federal Gra Expenditures Are Incurred	nts Where Funds	s Are Rec	eived	Before
Taxes Paid	In Protest				
(<u>Ex. 13-3)</u>	The LEA received \$50,000.00 o will be expended after June 30.	•			•
	DR 0302 Revenue Control CR 0480 Deferred Revenues	\$	8,000.00	\$	8,000.00

Expenditure / Expense Accruals

Any goods or services **received** prior to the end of the fiscal year and remaining unpaid at the beginning of the subsequent fiscal year, requires an expenditure / expense accrual. This ensures that all goods and services received in the closing fiscal year are accounted for as expenditures / expenses in that fiscal year. For example, salaries and wages earned before June 30th and paid in the next fiscal year must be accrued as an expenditure / expense and accounts payable. The benefits that relate to the accrued salaries should be calculated and also recorded as an expenditure accrual. Following is a listing of expenditures / expenses that the LEA might reasonably expect to accrue:

(Ex. 13-4) The LEA received a supply shipment on June 15. Payment of \$500.00 for the goods will be disbursed in July. On June 30, the cost of the supplies is accrued.

DR 0602 Expenditure Control \$
CR 0421 Accounts Payable

\$ 500.00

(Ex. 13-5) The LEA will pay teacher salaries of \$500,000.00 in July and August that were earned in the closing year. The related benefits are \$130,000.00. The salaries and benefits are accrued.

DR 0602 Expenditure Control
CR 0461 Accrued Salaries And Benefits

630,000.00 \$ 630,000.00

500.00

Expenditure Deferrals

Expenditures made in the current fiscal year that provide an economic benefit to the LEA that extends beyond the current fiscal year may require at least part of their costs to be allocated / deferred into the following fiscal period. An example of such a transaction would be a fire insurance policy purchased in April which provides coverage until the following April. The LEA would expense, in the current year, only that portion of the cost of the policy that pertained to the April through June time period. The remainder of the cost of the policy would be deferred. The approach taken by most LEAs is described above. However, Governmental Accounting Standards allow for recognition of the full expenditure in the year of payment for governmental funds under the modified accrual basis of accounting. These expenditures would be recognized in the period of acquisition and would not be allocated to a subsequent year on the fund level statements. Expenditures that are commonly deferred include:

□ Prepaid Rent□ Prepaid Insurance□ Prepaid Maintenance Expenses□ Prepaid Supplies

(Ex. 13-6) The LEA paid an annual insurance premium of \$12,000.00 on May 1. On June 30, the amount pertaining to the subsequent year is deferred.

DR 0181 Prepaid Expenditures CR 0602 Expenditure Control \$ 12,000.00

\$ 12,000.00