Date: November 27,1995
Bulletin: 95-016

AUDITOR OF STATE BULLETIN

TO: ALL SCHOOL DISTRICT TREASURERS
ALL EDUCATIONAL SERVICE CENTER TREASURERS
ALL IPAS

SUBJECT: SCHOOL GAAP ISSUES

The purpose of this bulletin is to provide information to school districts that may be useful in the preparation of their GAAP financial statements for the 1995 fiscal year. Although it is already late in the statement preparation process, the bulletin may help reduce the number of audit issues that arise later on. The bulletin will respond to some of the more frequently asked questions and address issues that have been treated inconsistently in Ohio, as well as identifying some of the changes in GAAP that are now in effect.

The Accrual of Property Taxes

Current GAAP states that a receivable for property taxes should be established for taxes that have been levied. Property tax revenue is to be recognized in the year for which it is levied (the year in which it is available for appropriation), provided it is available. Property taxes are considered available if they are due, or past due and received within the available period, and collected within the current period or soon enough thereafter to be used to pay liabilities of the current period. The tax calendar for schools is based on four settlements occurring within the fiscal year as follows:

```
July 1                                          June 30
 [------------------------------------------------------]
      Aug 94     Oct 94     Feb 95          June 95
```

August and February represent real and public utility property tax settlement dates. October and June represent personal property tax settlements. These settlements are for several different tax years. Taxes are levied and collected on a calendar year basis. 1993 real property taxes are levied by school districts in April 1993, and settled in February and August of 1994.

1994 personal property taxes are levied by school districts in April 1993, and settled in June and

October of 1994. 1993 public utility taxes are levied by school districts in April 1993, and settled with real property taxes in February and August of 1994. The following chart for the settlements occurring in the 1995 fiscal year may make this process a little easier to understand.

Settlement	Type of Tax	Tax Year	Levy Date
August 94	Real Property	1993	April 93
	Public Utility	1993	April 93
October 94	Pers. Property	1994	April 93
February 95	Real Property	1994	April 94
	Public Utility	1994	April 94
June 95	Pers. Property	1995	April 94

You can see from the chart that all settlements occurring within a fiscal year are levied prior to the beginning of the fiscal year. It would be therefore be appropriate to establish a receivable at June 30, 1995, for the 1996 fiscal year's estimated settlements. It would not be appropriate to recognize revenue at June 30, 1995, for the 1996 fiscal year's estimated settlements since the anticipated taxes were levied for the 1996 fiscal year. The receivable is therefore offset by a credit to deferred revenue. The only exception to this approach occurs when second half real property taxes are available as an advance prior to year end. Since state statute allows boards of education to appropriate advances available at June 30, 1995, for the 1995 fiscal year, it should be recognized as revenue rather than deferred. This approach may differ from what your district has been doing. If so, a restatement of beginning of the year balances would be required if the amount to be recognized is material.

Rollback and Homestead

In a recent bulletin dealing with foundation payments (Bulletin #95-012, dated September 13, 1995) we identified new guidelines for the recognition of revenue from entitlements. The guidelines state that an entitlement may not be recognized as revenue prior to the year it is intended to finance. Several school districts have asked about applying the new guidelines to homestead and rollback reimbursements received within the available period. Homestead and rollback payments are entitlements paid by the State to a political subdivision. They are intended to reimburse the subdivision for reductions in property tax revenue caused by credits granted to certain property owners by state statute. Based on guidance provided in "Governmental Accounting, Auditing and Financial Reporting" published in 1994 by the Government Finance Officers Association, the year that an entitlement is intended to finance is based on the year in which it is appropriated by the State.

The homestead and rollback payment made following the August settlement is appropriated by theState in the 95/96 fiscal year and therefore may not be recognized as revenue in fiscal 95 by school districts.

New Pronouncements in Effect for FY 1995

GASB Statement 10 "Accounting and Financial Reporting for Risk Financing and Related Insurance Issues" is effective for self- insurance programs. The statement provides that if one fund is going to be used to account for a self-insurance program, it must either be the general fund or an internal service fund. Guidelines identify the proper accounting treatment based on the fund selected. The statement also creates note disclosure requirements for self-insurance programs.

GASB Statement 20 "Accounting and Financial Reporting for Proprietary Funds "is effective this year. The statement provides guidance for determining which pronouncements apply to accounting for proprietary activities, and authorizes a choice regarding certain pronouncements issued after November 30, 1989. Local governments must disclose in the notes to the financial statements which pronouncements are being applied to accounting and reporting for proprietary fund activities.

GASB Statement 21 "Accounting for Escheat Property" establishes the fund type in which to report escheat and unclaimed property. Escheat property represents assets that revert to a government because there are no legal claimants or heirs. Unclaimed assets revert to a government due to the failure of the person who is legally entitled to the property to make a valid claim within a certain period of time. Escheat and unclaimed property should be reported in an expendable trust fund or in the fund that will ultimately receive the assets if they are not claimed. Escheat and unclaimed property should be offset by a liability to the extent it is believed the property will be claimed. Property held for another government should be reported in an agency fund.

GASB Statement 22 "Accounting for Taxpayer Assessed Tax Revenues in Governmental Funds" establishes that revenue should be recognized for income taxes to the extent they are measurable and available at year end, net of estimated refunds. If the amount accrued equals the actual payment received during the available period, an estimate of refunds is not necessary. The State Treasurer withholds from the quarterly payments amounts needed for the payment of refunds. Most school districts with an income tax will already have been following the guidelines of this statement. If not, the notes to the financial statements should recognize that the statement went into effect for this year and report any material restatement caused by the change as of June 30, 1994.

GASB Statement 16 "Accounting for Compensated Absences" was effective last year, but some reports did not indicate that it had been adopted. Statement 16 expanded the scope of the liability for compensated absences to include benefit payments that are probable, rather than just reporting those that are already vested.

GASB Statement 23 "Accounting and Financial Reporting for Refundings of Debt Reported by

Proprietary Activities" is effective for fiscal 1995, but is unlikely to apply to a school district in Ohio.

GASB Technical Bulletin No. 94-1 "Disclosures about Derivatives and Similar Debt and Investment Transactions" is effective for fiscal 1995. The Bulletin defines derivatives and establishes disclosure requirements for districts that have used, held or written derivatives during fiscal 1995.

Year-End Accounts Payable

Year-end accounts payable represent goods or services received prior to year-end for which payment has not yet been made. All outstanding year-end accounts payable should be reported as fund liabilities on the balance sheet, not just those paid during the available period. This means that a search for payables that is limited to the available period may not be adequate. The search should be continued until you are no longer discovering significant additional payables.

Accrued Liabilities

Accrued liabilities are obligations that have been incurred as of the balance sheet date but for which payment is not yet due. In general, accrued liabilities are presented as fund liabilities. GASB, however, has specifically identified the following liabilities to which this rule does not apply: claims and judgments, compensated absences, unfunded pension contributions, and special termination benefits. These liabilities are to be reported as fund liabilities only to the extent they will normally be paid with expendable available financial resources. The amount that will not normally be paid from available financial resources is to be reported in the General Long-term Debt Account Group. Determining what, if any, portion of these liabilities will be reported as a fund liability is difficult. Although other methods may be considered acceptable, two methods are preferable.

The first method reports the portion of the liability that is paid during the available period as a fund liability. The second method reports the portion of the liability that is "funded" as a fund liability. A liability incurred during the year is funded to the extent that a local government sets aside money in the current budget to pay it. The result of funding liabilities as they are incurred is the accumulation of money that will eventually be used to pay the liability. In Ohio, accumulating significant resources to make payments in future years is only permitted if specifically authorized by state statute. To date, school districts are not authorized to accumulate money for the liabilities listed above.

Fringe Benefits Owed to Employees

As of June 30, many school district employees have fulfilled the requirements of their employment contracts. These contracts often run from September 1 through August 30 and require the school district to provide insurance benefits to the employee for the entire term of the contract.
If the district is legally responsible for providing the insurance based on services already provided by the employee, whether or not the employee is rehired for the following school year,

then the district should report a liability to the employee for the cost of the coverage for July and August in its annual financial statements for the year ended June 30, 1995. If the liability has not been recorded in previous years, a restatement of the July 1, 1994, fund balances/retained earnings will have to be presented either in the financial statements or in the notes to the financial statements.

Amounts Owed to the Retirement Systems

School districts that pay the employer share of retirement contributions through a deduction from foundation payments are two months behind in payments to STRS and six months behind in payments to SERS. Multiplying the foundation deduction times either two or six will provide an acceptable estimate of the liability, provided the salary estimate upon which the deductions were based was reasonable. This is an accrued liability that must be reported as a fund liability. The allocation of the liability among funds should consider the policy of the district in allocating the foundation deductions. The result should be an annual expenditure/expense for employer contributions reported within each fund that equals the employer contribution rate times total covered payroll.

Workers' Compensation

Payments made to workers' compensation in one calendar year are to pay for coverage provided for the previous calendar year. Payments made in 1995 pay for 1994 coverage. The liability at June 30, 1995 equals the 1994 contribution rate times 1994 salaries plus the 1995 contribution rate times salaries for January through June of 1995 minus any payments made in January through June of 1995. This is an accrued liability that must be reported as a fund liability. The liability should be allocated to the funds that will pay it, remembering that GAAP suggests that an appropriate allocation be made to proprietary funds.

Compensated Absences

The liability for compensated absences is now based on guidance provided by GASB Statement 16. The liability for payments to be made from proprietary funds is reported entirely within the proprietary funds. The liability for payments to be made from governmental funds must be allocated between the funds and the GLTDAG. The portion of the liability reported within the funds represents the amount estimated to be paid using current available financial resources. Two methods for calculating the fund liability are identified in the "Accrued Liabilities" section of this bulletin. The first method calculates the fund liability by summing payments made during the available period that reduce the year-end liability. The fund liability under the second method equals the portion of the liability that has been funded.

Reporting Entity

Defining the reporting entity under the guidance of GASB Statement 14 is still generating many questions. The most frequent areas of concern include data acquisition sites, self- insurance pools, booster organizations and cash activity that is not on the books of the school district treasurer.

Data Acquisition Sites

Most data acquisition sites (DAS) are being reported as jointly governed organizations. Exceptions occur when the agreement among the participating districts states that the districts have a responsibility for paying the outstanding obligations of the DAS (such as a capital lease of computer equipment) if the DAS is unable to make the payments, and when control of a DAS is placed in one district. In the first instance, the DAS should be reported as a joint venture. In the second, the DAS is reported as an internal service fund of the district with control.

A DAS would be considered a joint venture and each district would report an equity interest on its balance sheet when the agreement specifies the method for distribution of assets upon dissolution of the DAS and each district's interest upon dissolution arises from annual operating subsidies rather than operations. Although this situation is a possibility, it rarely occurs.

Self-Insurance Pools

There are three types of self-insurance pools operating in Ohio. The first is a shared risk pool. A shared risk pool operates like an insurance company. Subject to the terms of the agreement creating the pool, premium payments may be used to pay the claims of any participant. Premium payments made by a school district are recorded as expenditures/expenses by the district and as revenue by the pool. The pool should issue financial statements that identify the operation and financial condition of the pool as a whole.

The second type of pool is a claims servicing pool. The pool reviews and pays claims of the participants, either directly or through services provided by a third party administrator, and invests available balances. The financial activity related to each participating school district is kept separate. A school district's payments to the pool may only be used to pay its own claims, not those of other participants. Most school districts report their participation in this type of pool through a self-insurance internal service fund. Revenues of the fund represent payments by the other funds of the district. Expenses include claims, administrative charges and the purchase of stop-loss coverage. The fund should also reflect any year-end cash balance held by the pool as "Cash with Fiscal Agent" on the balance sheet.

Some additional comments regarding claims servicing pools may help some school districts avoid potential problems.

The claims expense reported for the year should include the amount of the liability for unpaid claims costs as of June 30. This liability is a year-end estimate, usually provided by the third party administrator, of the additional costs that will be paid for ongoing claims and the cost of claims that have been incurred but have not yet been reported.

Third party administrators are service providers as that term is defined in Statement on Auditing Standards No.70. See Bulletin 95-10, issued by this Office on September 7, 1995.

Routinely determine that your stop-loss insurance provider is financially sound either by requesting a copy of the audited year-end report or by checking the company's rating with Best Ratings.

School districts are required under Ohio Rev. Code Section 9.833 to establish adequate reserves for their self-insurance programs for health care benefits, and to have the adequacy of the reserves evaluated annually by an actuary. The report of the actuary is to be filed with the administrator of the program.

The third type of pool is a group purchasing pool. This pool shops for insurance as a group with the intention of securing better rates than if each participant purchased insurance separately. The pool may collect the premiums from the participants for payment to the insurer. Payments to the pool should be reviewed to determine when payment is made to the insurer and the period covered by the payment. Payments to the insurer may be current expenditures/expenses or they may be a prepaid. Each participant’s proportionate share of money still held by the pool at year-end should be reflected on the participant's financial statements.

If you report the activity of a self-insurance program on your financial statements, take care to insure that revenues and expenses are properly matched to the correct fiscal year. This can be difficult if financial information is provided by a third party for use in your report.

Booster Organizations

Booster organizations are not currently presented as part of the school district's financial statements under GAAP unless the money of the organization is considered public under state statute. In general, if a booster organization gives the impression that contributed money will be under the control of the board of education, then the contributed money will be considered public.

Cash Off The Books

It is not unusual for GAAP statements of a school district to include cash that is not on the books of the treasurer at year end. Examples include money with a financial institution for servicing debt, money held in escrow during construction, money held by a third party administrator providing claims servicing for a self-insurance program, money held in a deferred compensation program under section 457 of the internal revenue code, and money in a payroll account that does not reconcile to zero. In each instance, journal entries should be made to present this money on the balance sheet of the district, and may be necessary to correctly present revenues and expenditures. Examples may be found in the generic GAAP plan for schools available from the Local Government Services Division of the State Auditor's Office.

The Auditor's Office is aware that the accounting information presented in this bulletin is of a summary nature and may raise additional questions about applying this information to your district. Questions are welcome and should be directed to the Local Government Services Division at (800) 345-2519 or the Audit Division at (800) 282-0370. Any legal questions raised by this bulletin should be directed to your legal counsel.

Jim Petro, Auditor of State
State of Ohio