

CHAPTER 3 – Accounting Guidelines

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INTERNAL CONTROL STRUCTURE

Introduction

This chapter provides school boards, superintendents, business managers, and other school district personnel with a background and approach to establishing and maintaining an effective system of internal controls.

These internal control policies are based on the 1994 report issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and standards adopted by the American Institute of Certified Public Accountants and the federal Office of Management and Budget.

The COSO report defines internal control as “a process, effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations.
- Reliability of financial reporting.
- Compliance with applicable laws and regulations.”

Internal control is a management process to assist a school district in achieving the educational objectives adopted by the school board. This management control system should include procedures and policies to help ensure resources are guarded against waste, loss, and misuse; that reliable data is obtained, maintained, and fairly disclosed in financial statement and other reports; and resource use is consistent with laws, regulations, and policies.

Basic Internal Control Requirements

Each school board is responsible for establishing and maintaining an effective system of internal control throughout the school district.

An internal control system should provide *reasonable assurance* that a school district will accomplish its educational objectives. The concept of reasonable assurance recognizes that the cost of an internal control activity should not exceed the benefit derived from it. Reasonable assurance equates to a satisfactory level of confidence given considerations of costs, benefits, and risks.

School district management should identify and analyze the risks in achieving educational objectives and determine how to most effectively and efficiently manage those risks. Management defines the level of risk that the school district is willing to accept and strives to maintain risks within those levels.

Each school district should adopt methods to assess risk and review control activities. The methods developed should address each school district’s specific needs.

Components of Internal Controls

The five components of good internal controls within a management control system are:

1. **Control Environment**—The control environment sets the tone of a school district. Providing discipline and structure, it is the foundation for all other components of internal control. Control environment factors include the integrity, ethical values, and competence of the school district’s staff; management’s philosophy and operating style; the way management assigns authority and responsibility; the way management organizes and develops its staff; and the attention and direction provided by the board.
2. **Risk Assessment**—Every school district faces a variety of risks from external and internal sources, all of which must be assessed. A precondition to risk assessment is establishment of objectives, linked at different levels and internally consistent. Risk assessment is the identification and analysis of obstacles to achieving the objectives, and it forms a basis for determining how risks should be managed.
3. **Control Activities**—Control activities are the internal policies and procedures that help ensure management directives are carried out. They help ensure necessary actions are taken to address risks to achieving the school district’s objectives. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, review of operating performance, security of assets, and segregation of duties.
4. **Information and Communication**—Pertinent information must be identified, captured, and communicated in a form and time frame that enables people to carry out their responsibilities. Information systems produce reports containing operational, financial, and compliance related information, making it possible to efficiently manage the school district.
5. **Monitoring**—Management systems and internal activities need to be monitored to assess the quality of their performance over time. Assessment is accomplished through ongoing monitoring activities, separate evaluations, or a combination of the two. Deficiencies should be reported upstream, with serious matters reported to top management.

Common questions about internal control

What is a risk assessment?

A risk assessment is a process to identify, analyze, and manage risk. A school district needs a plan to identify both external and internal risks. The plan will help management understand how those risks affect their activities, assess their significance, manage their effect, and provide for continuous monitoring. Risk identification can often be integrated with a school district’s planning activities.

Risk analysis involves a careful, rational process of estimating the significance of a risk, assessing the likelihood of its occurrence, and considering what actions and controls need to be taken to manage it. Risk analysis also involves estimating the cost to the school district if something does go wrong.

How does a school district identify risk?

Identification of risk can start from existing systems. The budget process, audits, strategic planning, and other chapters included in this manual all provide opportunities for managers to conduct quantitative and qualitative reviews and to identify and prioritize.

How does a school district control or minimize risk?

Control of risk starts with management deciding on the actions necessary to reduce the potential occurrence and significance and monitoring conditions to remain aware of changing circumstances.

Control activities

The control activities presented in this section are intended to provide school boards, superintendents, business managers, and other school district personnel with an overview, use, and potential limitations of control activities to manage the risk of achieving school district objectives.

Control activities are the policies and procedures that help ensure management directives are carried out. They help ensure that necessary actions are taken to address and minimize the risk of achieving school district objectives.

Control activities, no matter how well designed and executed, can provide only reasonable assurance regarding achievement of objectives. The likelihood of achievement is affected by limitations inherent in all control systems.

Loss of Public Funds

Known or suspected loss of public funds or other illegal activity must be immediately reported to the State Auditor's Office (RCW 43.09.185). Districts should contact their local audit manager.

Audit Resolution Standard

School district management is to follow WAC 392-115 for state and federal audit findings.

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PAYROLL PROCESS

The payroll process implements management policies and procedures to properly compensate employees for services rendered. State and federal government laws and regulations impact the process and dictate some procedural practices.

Personnel Decisions

The personnel department of each school district should be responsible for the determination of the individuals to be included on the payroll of the district. The personnel department should inform employees of mandatory benefits, available optional benefits, and other paid or nonpaid benefits. The personnel department then communicates the employee's choices regarding these compensation issues to the payroll department. The personnel department should also communicate any changes in employee benefit programs to the employees and to the payroll department. Management procedures need to ensure that the responsibility for personnel assignments is clearly delineated to ensure appropriate duty and financial accountability.

Payroll Database

The payroll process requires many periodic updates to the information database that ensures an accurate and reliable production of pay instruments. These periodic changes may occur randomly or on a regularly scheduled basis, such as a day, week, month, or year. In many instances, governmental regulation or contract terms determine when changes in the database will occur. Employee options also effect changes. The following database items need to be considered:

- **Demographic Data:** Information to identify the employee as a unique individual, including name, address, social security number, withholding exemptions, marital status, etc.
- **Hours of Work:** The normal work schedule that is related to the payroll department on a timesheet declaration from the employee or is understood by a professional contract.
- **Overtime Work:** Hours worked beyond the normal work schedule.
- **Payroll Period:** The frequency at which employees provide services and are paid. (In school districts, usually monthly.)
- **Pay Date:** The regularly identified date on which employees are paid.
- **Salary Schedule(s):** The documents that determine the periodic pay rates for individuals.
- **Paid and Unpaid Leaves:** The policy or procedures that determine which leaves of absence are paid or unpaid.
- **Unemployment Compensation:** The unemployment benefit program administered by the Employment Security Department. The district may participate in a tax rate basis or reimbursement rate basis of replenishing the fund. The reimbursement rate basis may be self-administered or administered through a cooperative arrangement with other school districts or the local ESD.
- **Optional Benefits and Deductions:** The district-sponsored benefits to which the district may or may not contribute, including health insurance, life insurance, disability insurance, annuity, United Way, credit union, deferred compensation, etc.
- **Social Security:** The federal government-sponsored program of pensions and disability income to qualified individuals supported by payroll taxes.

- Retirement Systems: The state government-sponsored retirement systems supported by payroll deductions and contributions by the district.
- Workers' Compensation Insurance: The state government-sponsored program of pensions, disability income, and/or medical expenses for qualified individuals who have sustained injuries on the work site as a result of performing duties for the district. The program is administered by the Department of Labor and Industries and the district may be self-administered or a member of a cooperative arrangement to administer claims.

Time and Effort Records

Time and effort records are employee-generated time records reporting the employees' effort in support of federal grant(s) and other assignments. The federal government's Office of Management and Budget requires these records. (For additional information regarding time and effort reporting, see Office of Management and Budget Circular A-87.) Time and effort records are to be completed monthly, unless a substitute system has been approved by OSPI. Additionally, semi-annual certifications may be completed in lieu of monthly time records if the employee works on a single cost-objective, as defined in Circular A-87.

REVENUES AND RECEIPTS

Governmental fund reporting focuses on current financial resources through use of the modified accrual basis of accounting (cash basis may be used for those districts with under 1,000 FTEs). Revenues are defined as an increase in the governmental unit's current financial resources regardless of form. Revenues are recognized when they are susceptible to accrual, which means they must be both measurable and available. Revenues are measurable when the amount of the revenue is subject to reasonable estimation. In order to be available, revenues must be subject to collection within the current period or after the end of the current period but in time to pay the liabilities outstanding at the end of the current period.

The economic resources measurement focus and accrual basis of accounting is used for the districtwide financial statements. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions should be recognized when the exchange takes place. Transactions are external events where something of value or benefit passes between two or more parties. In exchange-like transactions, the values exchanged may not be quite equal or directly benefit the parties to the transaction but are sufficient to justify treating the transaction as an exchange for accounting recognition. (GASB Statements 33 and 34.)

Timely Deposit

Article XI, Section 15, of the Constitution of the State of Washington requires that all moneys, assessments, and taxes belonging to or collected for the use of any public or municipal corporation shall immediately be deposited with the treasurer, or other legal depository. Chapter 28A.400.030(3) RCW requires the superintendent of a public school district to keep accurate and detailed accounts of all receipts and expenditures of school money.

Cash Receipts

Each public school district is responsible for the establishment of procedures for the daily collection of cash, other forms of money, and for the issuance of payee receipts consistent with reliable internal control processes. (See Chapter 3, Section 1.)

Revenue Accruals

Governmental fund types: The modified accrual criterion of measurable and available is used. It is applicable to each major source or revenue classification within the source. Accruals are not applicable to those public school districts electing under RCW 28A.505.020 to use cash basis accounting.

- *Local taxes*: Local property taxes are recorded at the net amount collected (cash basis) during the current fiscal year. This is a departure from GAAP as defined by GASB 33 and Interpretation 5 and should be disclosed in the notes to the financial statements. (See discussion of Nonexchange Transactions later in this section.)

- *Local nontaxes:* Accounts in this major source may be recorded at the amount collected (cash basis) during the current fiscal year. Some revenue accounts in this source may be susceptible to accrual including, but not limited to, rental income, investment earnings, and tuition.
- *General-purpose state revenues:* Accounts in this major source meet the measurable criteria but not the available criteria; therefore, accruals are not required. As a practical matter all material amounts are received during the current fiscal period. However, known and probable reductions must be recognized when material.
- *Special purpose state revenues:* Many accounts meet the measurable criteria but not the available criteria; therefore, accruals are not required. However, grants paid on a reimbursable basis meet the measurable and available criteria and are, thus, subject to accrual.
- *General-purpose federal revenues:* Most accounts in this source are not measurable or available; therefore, these amounts are recorded as collected (cash basis) during the current fiscal period. For those sources that meet the measurable and available criteria, the amounts are accrued.
- *Special purpose federal revenues:* Most accounts in this source are from grants paid on a reimbursable basis that meet the measurable and available criteria; therefore, these amounts are subject to accrual. For those sources that do not meet the measurable and available criteria, the amounts are recorded as collected (cash basis) during the current fiscal period.
- *Revenues from other school districts:* Many accounts in this major source meet the measurable and available criteria making them susceptible to accrual. Some accounts are measurable but not available (e.g., payments from nonhigh districts); therefore, these amounts are recorded as collected (cash basis) during the current fiscal period.
- *Other agencies and associations:* Many accounts in this major source meet the measurable and available criteria making them susceptible to accrual. Some accounts are measurable but not available; therefore, these amounts are recorded as collected (cash basis) during the current fiscal period.
- *Other financing sources:* All accounts in this major source are recorded as collected (cash basis) during the current fiscal period. These amounts are not recorded as revenues on the income statement but as the source title says, as other financing sources.

Revenue Carry Over

Revenues that are received for a legally restricted purpose but have not yet been expended in the current fiscal period are susceptible to the reservation of fund balance. Any unexpended amounts shall be recorded in General Ledger Account 810 – Reserved for Other Items, at the fiscal year end. An example of these special purpose revenues are Student Achievement and LAP. See Chapter 4, Section 3-Fund Balance, “Reserve” and “Reserved” Accounts, for more information.

Deferred Revenues

(Not for cash basis districts.)

There are two meanings for deferred revenue in the public sector.

- **Unearned revenue.** Under both the accrual and the modified accrual basis of accounting, revenue may be recognized only when it is earned. If assets are recognized in connection with a transaction before the earnings process is complete, those assets must be offset by a corresponding liability for deferred revenue. An example of this would be reimbursement grants or state forest money received in August that will be recovered in January.
- **Unavailable revenue.** Under the modified accrual basis of accounting, it is not enough that revenue has been earned if it is to be recognized as revenue of the current period. Revenue must also be susceptible to accrual (it must be both measurable and available to finance expenditures of the current fiscal period). If assets are recognized in connection with a transaction, but those assets are not yet available to finance expenditures of the current fiscal period, then the assets must be offset by a corresponding liability for deferred revenue. This type of deferred revenue is unique to governmental funds, since it is tied to the modified accrual basis of accounting, which is used only in connection with governmental funds.

Nonexchange Transactions

Nonexchange transactions that involve the exchange of equal or approximately equal value are common in governments. GASB Statement 33—*Accounting and Financial Reporting for Nonexchange Transactions* prescribes the accounting for such transactions. In governmental funds where the modified accrual basis of accounting is used, revenue recognition of nonexchange transactions takes place only when the transaction has occurred *and* the revenues are available. The timing of recognition is as follows:

- *Derived tax revenues* result from assessments imposed by governments on exchange transactions. Examples include taxes on earnings or consumption such as sales or motor fuel tax. Under modified accrual, revenues received before the underlying exchange has occurred should be reported as deferred revenues (liabilities).
- *Imposed nonexchange revenues* result from assessments by governments on nongovernmental entities such as individuals. Examples are property taxes and most fines and forfeits. Revenues are recognized when the use of the resources is required or first permitted by time requirements (such as the period for which property taxes are levied). Resources received or recognized as receivable before the time requirements are met should be reported as deferred revenues.
- *Government-mandated and voluntary nonexchange transactions* include grants to districts for state or federally mandated programs, entitlements, and most donations. Under modified accrual, revenue is recognized when all applicable eligibility requirements are met *and* the resources are available. If the provider requires the recipient to use (sell, disburse, consume) the resources in, or beginning in, the following fiscal period, resources provided before that period should be recognized as advances to the providers and deferred revenue to the recipients.

Receivables

Revenues or other positive increments in financial resources should be treated as an account receivable at the time the invoice is issued or a grant claim is filed. This principle is applicable to accrued revenues and material nonaccrued sources if the period to which the nonaccrued source is attributable has ended. (GASB Cod. Sec. 1600.114 and 115.)

In addition, material revenues received prior to the normal time of receipt, or in advance of the period to which they apply, should be recorded as deferred revenues in the period received and recognized as revenue of the period to which they apply. (GASB Cod. Sec. 1600.116.)

Interfund receivables and payables may result from services rendered or goods provided by a department financed from one fund to a department financed from another fund or from interfund loans. Each fund, being a separate entity, should reflect the amounts due from other funds, as well as the amounts owed to other funds. The receivables and payables should not be offset (netted) in the accounts, but they may be reported at the net amounts in the respective fund balance sheets. (GASB Cod. Sec. 1300.110.)

Electronic Funds Transfer

The deposit to, or disbursement from, a bank account by means of wire or other electronic communication is permitted by RCW 39.58.750.

Revenue Versus Contra-Expenditure Recognition

For financial reporting purposes, revenues and expenditures should be presented on the gross versus net basis because the measurement focus is on the flow of current financial resources.

Examples of expenditure reimbursements that should be reflected as revenue and not a refund of expenditure include: substitute teacher reimbursement from other districts, student fees for fieldtrips, and teacher training reimbursement from OSPI.

An exception to this relates to interfund reimbursements between funds for expenses and/or expenditures. An example of this type of transaction is when an expenditure is made from one fund (fund 1) on behalf of another fund (fund 2). Reimbursement of the expenditure is transferred from fund 2 to fund 1. Fund 1 records the moneys received as an adjustment to the original expenditure.

EXPENDITURES AND DISBURSEMENTS

This section contains guidance on the treatment of expenditure and disbursement documents.

Employee Travel

Travel expenses include amounts paid for the use of personal automobiles, other transportation, and actual expenses or reimbursement in lieu of actual expenses for meals, lodging, and related items.

Travel reimbursements include amounts paid for the use of private or commercial transportation, actual or per diem charges for meals, lodging, and other related items pursuant to school board policy or procedures adopted under the guidance of RCW 42.24.115 through 42.24.160.

The school district board must pass an ordinance or resolution to establish rules and regulations for the reimbursement of travel expenses. There should be rules to cover all district officials and employees. The ordinance or resolution should discuss the board policy on tipping and charging expenses to the district, and should prohibit reimbursement for personal expenses and entertainment.

If a district wishes to issue credit cards for travel-related expenditures, the board must pass an ordinance or resolution to establish rules and regulations that satisfy the provisions of chapter 42.24 RCW, including:

- Submission of a fully itemized travel expense voucher by the employee or officer.
- Settlement by the officer or employee within 30 days of the billing date.
- Establishment of a lien against salary for any disallowed charges.

Claims for reimbursement of travel expenses must contain a signed certification that includes the following language: "I hereby certify under penalty of perjury that this is a true and correct claim for necessary expenses incurred by me and that no payment has been received by me on account thereof."

In addition, if an officer or employee is filing a claim on behalf of others, he or she must prepare a detailed account that includes:

- Names of the others who traveled, partook of meals, or otherwise incurred expenses.
- Whether they were district employees and, if not, who they were and what connections they had with district business. This should not be construed to permit promotional hosting.
- Who provided the lodging, meals, or other services in question, with dates and times.
- A detailed breakdown of amounts.
- Some statement sufficiently explicit to show what municipal business was being carried out when the expenses were incurred.

If a district chooses the option of using monthly reimbursements for the use of personal automobiles for official business, the following procedures apply:

- The monthly rate schedule established should be limited to officers and/or employees who actually use their personal automobiles for travel on a regular basis. It is the responsibility of the district to ensure that each traveler is on official business.
- The rate must be based on actual costs.
- A periodic review must be performed to determine whether or not the rate continues to reflect actual costs.
- A record is needed of the board's determination.

If the above procedures are not followed, the "monthly reimbursement for use of personal automobiles" may be treated as additional compensation. According to the Internal Revenue Service, districts could be assessed the withholding tax of the employees if the amounts advanced/reimbursed for travel were not for expenses incurred or reasonably expected to be incurred, unless these amounts are reported as taxable wages on the employee's W-2. (See IRS questions and answers on OSPI's website <http://www.k12.wa.us/safs/INS/ACC/faq.asp>.)

Advance Travel Expense Account

If a district chooses to establish an advance travel expense account (imprest account), pursuant to RCW 42.24.120, the following procedures apply:

- The imprest amount must be established and maintained in accordance with the procedures prescribed for petty cash (e.g., ordinance or resolution must establish amount).
- Upon receipt of the moneys, the custodian will open a checking account in a local bank in the name of the school district entitled "Advance travel expense account—Jane Doe, custodian." Moneys received from the following sources will be deposited to the account:
 - From the district disbursing officer, the total amount originally establishing the account or subsequently added.
 - From officers and employees, refunds of any unexpended advances.
 - From the warrant issuing official, amounts that reimburse the custodian for travel expenses allowed in the settlement of employee advances.
- The advance travel expense account must be used solely for travel advances, **not direct payments to vendors**. In other words, moneys may be advanced to an individual who is going on travel status for travel-related expenses that he/she will pay out of his/her own pocket. It must not be used for personal loans, preregistration fees, reimbursements to employees or officers for travel already incurred, etc.
- A check register will be maintained in which all transactions of the account will be recorded, including deposits, disbursements, and bank service charges. Reconciliation shall be made with the bank statement at the end of each month.
- Employee advances for travel expenses will be made by the issuance of checks drawn on the imprest bank account, payable to the applicant. Approved requests will be retained in the files of the custodian to support such advances until final settlement is made and claim

for reimbursement has been submitted. Requests for such advances shall be reasonable estimates of the applicant's travel expense requirements and shall contain as a minimum the following information:

- Date of request.
 - Name of applicant.
 - Destination.
 - Purpose of travel.
 - Anticipated departure and return dates.
 - Amount requested.
 - Signature of applicant.
 - Official approval of trip.
 - Check number, amount, and date (to be provided by the custodian when the advance is made).
- Settlement of advances will be made on or before the 15th day following the close of the travel period by filing with the custodian an expense voucher as required by RCW 42.24.090. The custodian will verify the amount shown on such form as having been advanced to the employee. In the event the traveler's actual expense is less than the amount of the advance received, the unexpended portion of the advance will accompany his/her expense voucher. The expense voucher and original request for the advance will then be used to support the custodian's claim for a warrant replenishing the account. The other copy of the expense claim will be submitted to the warrant issuing officer for reimbursement of the excess to the traveler. Claims for reimbursement to the account should be submitted by the custodian periodically as needed and at the end of the fiscal year in order that all expenses incurred will be charged against the appropriations for the period then ending.
 - Any default in accounting for or repaying an advance shall render the full amount which is unpaid immediately due and payable with interest at the rate of 10 percent per annum from the date of default until repaid. To protect against any losses on advances, the governing body shall have a prior lien against and a right to withhold any and all funds payable or to become payable to such officer or employee to whom such advance has been given up to the amount of the advance and an annual interest rate of 10 percent until repayment or justification is made (RCW 42.24.140). No advance of any kind may be made to any officer or employee at any time when he is delinquent in accounting for or repaying a prior advance.

Imprest Bank Accounts, Petty Cash, Stamp, and Change Funds (Accounts)

These accounts are any sum of money or tangible asset set aside for a specific purpose, usually for minor disbursements, making change or similar uses requiring immediate action outside the normal formal vendor invoice and payment voucher system (accounts payable). Incorporation into the accounts payable system will occur on a summary basis on a routine time schedule for replenishment of the appropriate imprest account and/or petty cash, stamp, or change funds (accounts). These accounts are defined as:

- *Imprest bank accounts:* Accounts established at commercial banks for the purpose of making minor disbursements by issuing checks as instruments of payment.

- *Petty cash funds (accounts)*: Cash amounts kept in secure areas used to make minor disbursements.
- *Stamp funds (accounts)*: Consists of U.S. postage stamps and postage meters.
- *Change funds (accounts)*: Cash amounts kept in secure places for the purpose of making change by converting paper bills or coins into smaller denominations.

The accounts are administered by use of the following requirements:

- The board of directors of the school district must authorize the initial amount, any changes in the account, and the maximum amount allowable by resolution. Such resolution may specify controls such as surprise cash counts by district staff.
- A custodian shall be appointed over each account. The custodian is the individual responsible for maintaining the security of the tangible asset and determining access.
- The account shall be established, increased, and replenished by issuance of a warrant drawn on the appropriate fund.
- Disbursements from imprest bank accounts and petty cash funds (accounts) shall be restricted to payments evidenced by appropriate documentation including, but not limited to, invoices from vendors, receipts for goods, etc.
- Replenishment expenditures shall be itemized for inclusion into the accounts payable vouchers on a periodic basis, usually monthly, unless the nature of the account dictates some other periodic cycle. The replenishment request should include such information as board policy or procedure prescribes including, but not limited to, identification of vendor invoice, vendor receipt, account code, or other data deemed pertinent.
- Imprest bank accounts and petty cash, stamp, and change funds (accounts) should be reconciled to the authorized maximum amount. All accounts should be replenished to their maximum amount at the end of the fiscal year.
- In the event the imprest bank account or petty cash fund (account) was established at an amount, which the fund does not have sufficient moneys to replenish, a journal voucher shall be prepared and recorded debiting General Ledger Account 530 Expenditures, and crediting General Ledger Account 200 Imprest Cash for the amounts previously disbursed.

Voucher Certification and Approval

All claims for the provision of goods and services, other than payroll, to the school district must be preaudited and certified by the district's auditing officer or his/her delegate. The certification may be made on each individual claim voucher or subject to the acceptance and approval of the board of directors. A blanket voucher certification may be used so long as it indicates the particular vouchers so certified. The use of a blanket certification does not relieve the auditing officer of the responsibility and liability for each individual voucher so certified. The certification must be signed and dated by the auditing officer or his/her delegate. For all claims, except travel reimbursements certified by employees or school officials, the certification must include the following language:

"I, the undersigned, do hereby certify under penalty of perjury that the materials have been furnished, the services rendered, or the labor performed as described herein and that the claim is a just, due, and unpaid obligation against _____ School District No. _____ and that I am authorized to authenticate and certify to said claim."

The auditing officer’s certification for employee or school official travel reimbursement claims must include the following language:

“I, the undersigned, do hereby certify under penalty of perjury that the claim is a just, due, and unpaid obligation against _____ School District No. _____ and that I am authorized to certify to said claim.”

The certification by the district auditing officer does not relieve members of the board of directors from the responsibility and liability for each voucher approved. It is the board’s responsibility to ensure that the system of auditing and certifying vouchers is operating in a manner to provide the greatest possible protection for the board members and the school district.

Indication of board of director approval for payment of claim vouchers and payroll should be recorded in the minutes of the board meeting by use of the following statement:

“The following vouchers as audited and certified by the auditing officer, as required by RCW 42.24.080, and those expense reimbursement claims certified, as required by RCW 42.24.090, are approved for payment. In addition, payroll warrants in the amount of \$ _____ are also approved.

(Fund Name)

Voucher numbers _____ through _____ totaling \$ _____.

Payroll warrant numbers _____ through _____ totaling \$ _____.”

Under authority granted by the board of directors, school districts may issue warrants before the board of directors approve the claims. The board must enact the following policies and procedures as required by chapter 42.24 RCW in order to grant this authority:

- The auditing officer and the official designated to sign the checks or warrants must have an official bond in an amount determined by the board, but not less than \$50,000 as required by RCW 42.24.180.
- The board should adopt contracting, hiring, purchasing, and disbursing policies that implement effective internal controls.
- The board must review and approve the claims paid without their prior approval at its next regularly scheduled public meeting.

If the board disapproves any claim paid prior to their approval, the auditing officer and the official designated to sign the check or warrant related to the disapproved claim must recognize this claim as a receivable of the district and pursue collection diligently until the amount is either collected or the board is satisfied and approves the claim.

The board of directors may stipulate that certain kinds or amounts of claims shall not be paid before the board has reviewed the supporting documentation and approved the issuance of checks or warrants in payment of those claims.

The original copy of all vouchers shall be filed in the office of the district's auditing officer. The detailed accounts to which the expenditures are to be posted must be clearly designated on the voucher. Supporting documentation must be retained and either attached to the vouchers or canceled by the auditing officer to prevent reuse. Original supporting documentation for vouchers for the claims against the associated student body program fund may be retained in the school building with ready availability to the auditing officer. Summary data required for auditing and certification of the vouchers in the Associated Student Body program fund may be forwarded to the auditing officer as required by board policy or procedure.

School districts that do not issue their own warrants shall send original vouchers and supporting documentation to the office of the appropriate county auditor.

Facsimile Signatures

The "Uniform Facsimile Signature of Public Officials Act of 1969," chapter 39.62 RCW allows the use of facsimile signatures on public securities and instruments of payments provided that certification and filing of manual signatures with the Secretary of State have been accomplished. (RCW 39.62.020.)

INVENTORY

Inventory systems should be designed and established to meet the needs of the school district to provide and maintain adequate control of supplies, materials, and associated transactions. Inventories may be accounted for using the purchases method where inventories are treated as expenditures when acquired, or the consumption method which recognizes expenditures as the goods are used. Districts with central warehouses will generally use the consumption method.

When the purchases method is used, significant amounts of inventories and prepaids are still reported as assets in the districtwide statement of net assets.

Tangible Materials

The two approved methods used to account for the inventory of tangible materials are “perpetual” and “periodic.”

- The **perpetual method** is common in districts employing central warehouses for the receiving, storage, and distribution of available inventory items. A continuous record of the additions and reductions to the inventory items is kept. Expenditures are recorded at the time materials are withdrawn from the warehouse for consumption by end users. An annual physical count of materials in the warehouse is required to verify and/or adjust the dollar value and quantities reflected in the stock on hand. The perpetual method generally is applied when there is a significant volume of items being purchased over which district management has determined that central control will ensure effective and efficient use of materials and associated acquisition expenditures. Perpetual methods are labor-sensitive due to the central record-keeping requirement.
- The **periodic method** is applied to establish the value and report inventory on hand at the end of the annual fiscal period. All additions to tangible materials are initially charged to expenditures at the time they are received. At the close of the fiscal period, a physical count is taken of tangible material not consumed by end users and valued at the most current purchase price. The dollar values obtained by this process are placed in the appropriate inventory account and credited to expenditures as part of the closing entries. The beginning entries of the subsequent fiscal period would reverse the inventory amounts and debit them to expenditures. Then the cycle repeats itself by charging all fiscal year acquisitions to expenditures, taking a physical count of items at the end of year, valuing them at the most recent acquisition price, and making the closing entries.

Inventory accounting is required for districts using central warehouses. This is because items are purchased for which the using program/activity is unknown, and therefore expenditure coding is impossible at the time of purchase. Additionally, there may be a timing problem when items are received prior to the fiscal year in which they will be consumed. For districts not using a central warehouse, the use of the inventory accounts is optional.

Inventory accounting for food service programs (separate inventory is optional for USDA commodities) is required because goods may be stored in both the central warehouse or in the building kitchen area(s) (General Ledger Account 420). (See Child Nutrition Bulletin 82-01.)

If USDA commodities are inventoried separately (optional), items are considered to be in inventory only when the unit (e.g., package, crate, container, or box) remains unopened. Once the unit is opened, the entire unit is recorded as an expenditure, even though not fully consumed.

Inventory Cost Valuation Methods

The inventory method selected should clearly reflect the flow of resources. Two methods are commonly used in school districts:

- The *first-in, first-out* (FIFO) method assumes costs are charged against revenue in the order in which they occur. This means the remaining inventory consists of the most recent costs.
- The *weighted-average* method assumes costs are charged against revenue based upon an average of the number of items acquired at each of the price levels. This amount is determined by dividing the total cost of an inventory item by the total number of items purchased, including beginning inventory, and applying it to the ending inventory.

Expenditure Recognition Alternatives

Inventory items may be considered expenditures either when purchased (purchases method) or when used (consumption method), but significant amounts of inventory should be reported on the balance sheet (GASB Cod. Sec. 1600.124.)

Prepaid Items

Generally, prepaid items refer to services to be provided (consumed) in a future fiscal period but for which payment has been made in a prior fiscal period. Expenditures of these items are prorated to the period during which the services were provided.

The value of tangible materials acquired for future fiscal period consumption may be debited to prepaid items when timing of the expenditure is relevant to the proper recognition of expenditures. This situation arises primarily at the end of one fiscal period and the beginning of another and generally involves districts using the periodic method of inventory.

Governmental funds may account for inventories and prepaids using either the purchases method or consumption method. When the purchases method is used, inventories and prepaids are reported as assets in the districtwide Statement of Net Assets.

CAPITAL ASSETS

Designing and establishing the capital asset accounting system of a school district requires systematic planning in basic areas such as:

- Establishing the objectives of the capital asset system and making permanent policy decisions that will effect the initial establishment and maintenance of the system.
- Designing the plan for taking the initial inventory, verifying and testing the data, and establishing a value for each recorded asset.
- Determining when and how to implement controls over additions and deletions to the inventory.
- Fixing accountability for the custody of individual items and in determining who is responsible for seeing that care and maintenance are attended to.

Although capital assets are not reported in the fund financial statements (F-196), districts will need capital asset information to prepare required note disclosures and ensure accountability for their assets.

Capital assets, net of accumulated depreciation/amortization, are reported on the districtwide Statement of Net Assets. In Note 1 of the Notes to the Financial Statements, the district must disclose its policy for capitalizing and depreciating capital assets and its policy for estimating the useful lives of those assets. See Chapter 8 for additional information and conversion schedule.

The Individual Capital Asset Record

An adequate capital asset accounting system ensures the school district will meet statutory requirements, produce records and reports, and properly guard assets. A policy on the dollar value at which capital assets will be included in the system is referred to as the “capitalization” policy. Consideration needs to be given to the uses of the system for insurance recoveries or other determinations of what is a permanent asset and what is a consumable. The capital asset record contains the information necessary to identify each item or lot in the inventory and may include:

- Description of the property identifying the category of the asset (land, building, transportation vehicles, or equipment), including legal descriptions of real property and improvements.
- A serial number or other identification number or information.
- The source of property (purchased, constructed, or donated).
- The acquisition, completion, or donation date.
- Reference to a source document (voucher/invoice, construction contract, trust agreement, etc.).
- The acquisition or construction cost of assets or the estimated fair market value of donated assets and/or assets held by the district before the capital asset system was established.
- Documentation of who holds title to the property.

- Source of the resources used for the acquisition (local, state, federal or percentage of each).
- The location and condition of the property.
- Special insurance, maintenance, and repair instructions.
- Dates of physical inspections and physical inventories. Physical inventories are required for assets purchased with federal resources at least once every two years.
- Disposition information on assets removed from inventory (date of disposal and sales price, lost, stolen, or surplus).

Asset Cost

The original cost of an asset is referred to as the “historical cost.” It is the amount paid to acquire an asset, including the price of the asset, related taxes, commissions, installation charges, consultant fees, architects, construction contractors, and any other costs related to acquiring the asset or preparing the asset for use. Expenditures that do not add to the utility of the asset should not be capitalized. Therefore, repairs to damaged equipment should be charged to an expenditure account and not entered in the capital asset record. Judgment should be exercised in determining which portions of the asset cost should be capitalized in the capital asset record.

Donations of cash to be used in conjunction with the construction or purchase of a specific asset should be reported as revenue in a governmental fund type.

Major repairs or improvements are capitalized. If the outlay adds to a capital asset or enhances the value of an integral part of it, the outlay should be capitalized. Thus, drainage to land, addition of a room to a building, and changes in equipment that increase its output or reduce its cost of operation are recognizable as additions to assets. Difficulty arises when large-scale outlays are partial replacements and additions or betterments. For example, a composition roof is replaced with more durable material. To the extent that the project replaces the roof, outlays should not be capitalized unless the cost of the old roof is removed from the accounts; to the extent that the project provides a better roof, outlays should be capitalized. The distribution of the total cost in such a case is largely a matter of managerial determination. Perhaps the best result might be obtained by crediting the appropriate asset account for the cost of the replaced part, thus removing the amount, and then debiting the asset account for the total cost of the replacing item.

Maintaining a Capital Asset System: Accounting

The school district should adopt appropriate policies and procedures that will ensure that assets that should be capitalized are properly recorded and records are adjusted when assets are disposed of or revalued. Standard data collection processes and periodic physical inventories ensure correct information is recorded in a reasonable time frame and provide a basis for reconciliation of accounting and inventory records.

Other than the acquisition and disposal of assets, other events that may require entries to the accounting system are location transfers, additional construction or demolition, and other improvements or changes in the physical appearance of the asset that should be reflected in its valuation. These adjustments should be recorded in the individual capital

asset record. The internal control system should ensure that transactions are noted and recorded. If adjustments are numerous, a capital assets journal may need to be maintained to accumulate the database necessary for adjusting the general ledger and individual asset records.

The capitalization policy of the district defines the dollar limits at which assets will be entered into the capital asset records. The policy should also consider treatment of capitalized leases; cost accumulation on self-constructed assets; control of small attractive assets that are not capitalized; and accounting for any infrastructure such as roadways, utility lines, etc. District personnel should be trained on the appropriate application of the capitalization policy to each acquired or disposed of tangible asset. Assets purchased with federal funds costing \$5,000 or more must be capitalized.

Internal control and information flow regarding asset additions or deletions should ensure that the individual responsible for maintaining the capital asset records is included in the cycle. Documents that may be required are receiving reports, invoices, lease agreements, progress billings on construction contracts, itemized work sheets of costs on self-constructed assets, board resolutions of declared surplus items, property insurance claims, etc.

Small attractive assets that are not capitalized, but to which the district desires to apply a security control, will need a similar internal control and information flow scheme.

When assets are transferred from locations or sites, or when they change internal ownership by fund type, procedures should delineate the communication cycle necessary to ensure the individual responsible for the capital asset records is informed of the changes.

Maintenance of the capital asset records implies that several reconciliations and reports will be performed and/or generated.

- Reconcile physical inventory to individual capital asset records.
- Reconcile individual capital asset records to general ledger accounts for both asset and equity information.
- Reconcile capital outlay expenditures to total additions in capital assets.
- Analyze expenditure object details for additions to lists of uncapitalized assets.
- Reconcile significant capital grants shown on the grant inventory for governmental type funds with increases to the investment in capital asset accounts.
- Analyze proceeds from insurance claims and sales or auction lists, claim reports, etc., to total capital asset disposals.
- Reconcile capital assets transferred to other locations, custody, or fund/account groups with assets transferred from the same.

Maintaining a Capital Asset System: Physical Inventory

A physical inventory of capital assets verifies the existence and the condition of the asset (required every two years for assets purchased with federal sources). The inventory is useful in determining the value of the asset, both for market value and insurance claim processing.

Board policy and procedure should determine when inventory is to be taken, who conducts the inventory, and what training, skills, and knowledge the conductors of the inventory should have.

To conduct the inventory, the district should have a work plan based on district control over the inventory process with responsibility assigned for supervision of the process and training of the staff. The work plan may include prelistings of existing asset records sorted by building, floor, room, or other location identifiers, or sorted by asset type. A systematic checklist approach should be employed to ensure that locations are not missed or duplicated in the inventory process. Procedures should instruct the staff about processes to employ when locating assets that appear to meet the capitalization policy but do not appear on the prelists. Procedures should also include clear instructions on how to record observations about the condition of assets.

Internal control guidelines should be employed in determining who will conduct the inventory to ensure that whoever has day-to-day custody of the asset is not the individual conducting the inventory. If the practical situation calls for the custodian of the asset to take the inventory, then the inventory results should be spot-checked for accuracy by the inventory supervisor.

Completed inventory records should be reconciled to the individual capital asset records. If the inventory process is conducted on a routine periodic basis, then the prelists would have been reasonably accurate and up-to-date, resulting in the reconciliation concerning itself with (1) identifying those assets that were not added to or deleted from the capital asset records at the time of their acquisition or disposal, and (2) investigating and making a final determination of assets not located. Other reconciliations mentioned in the prior section on accounting for capital assets might also need to be conducted as a result of the physical inventory.

Depreciation of Capital Assets

Depreciation of capital assets is not required under the F-196 other comprehensive basis of accounting (OCBOA) method as prescribed by the State Auditor's Office. However, depreciation is required under GASB 34 for all fund types for those districts who issue GAAP financial statements.

Districts who choose not to depreciate assets for accounting purposes may choose to keep depreciation records for other reasons, such as providing management a means of budgeting for replacement of capital equipment.

General guidelines regarding the recording of depreciation on capital assets are:

- Depreciation of capital assets is not required under the other comprehensive basis of accounting, but it may be part of a district cost accounting system.
- Scrap value can be ignored in establishing the amount to depreciate, unless it is expected to exceed 10 percent of the original cost of the asset.
- Depreciation must be based on a reasonable estimate of the length of time that the district expects to use the asset in its operations.
- An asset that is declared surplus or is held for possible future use is an investment and should not be depreciated.

- The amount of depreciation charged must be constant for each time period, called the straight-line depreciation method, or for each unit of service such as quantity of output, hours or miles of operation, etc.

Depreciation is required for districts reporting on GAAP basis. It is suggested that districts depreciate their capital assets using the straight-line method using the useful lives prescribed by the state Office of Financial Management. These are available at <http://www.ofm.wa.gov/policy/30.20.htm> and <http://www.ofm.wa.gov/policy/30.50.htm#30.50.10>.

- Depreciation must be based on the entire cost of the asset including any donated or contributed amounts.
- Assets may have components that will have an estimated useful life considerably shorter than the asset taken as a whole. Component depreciation for such assets may be much more accurate and simpler to maintain.
- When it is necessary to revise the estimates of useful life of an asset, such changes should be applied prospectively. The rate should be recalculated based on the remaining useful life at the time of the revision, and the new rate should be applied in the present and future accounting periods with no changes made to prior periods.

GAAP require that depreciation be reported in the districtwide financial statements.

There are two different applications of group-life depreciation:

- One type is applied to assets of a similar nature acquired at about the same time. The group is treated as a single asset; any gain or loss upon disposal is deferred until the entire group has been retired. When items within the group are retired ahead of schedule, the original cost of that item is removed from both the asset account and the accumulated depreciation account. Depreciation continues to be charged on the remaining assets at the original rate. If some items within the group are subject to major repair, the periodic depreciation should be adjusted for the change in useful life and the new rate charged for the remaining life.
- The second type is applied to dissimilar assets that are related by the mode of operation in which they are used. The rate of depreciation is a weighted average of the rates applicable to the individual assets that comprise the group. This method is intended to eliminate gains and losses on asset retirements, except when an entire operating system or facility is retired from service.

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INVESTMENTS

Each school district should, by action of the board of directors, authorize any moneys which are not required for immediate expenditure and which are in the custody of the county treasurer to be invested. All school districts are empowered by statute to invest in the following types of securities:

- Certificates, notes, or bonds of the United States, its agencies, or any corporation wholly owned by the government of the United States.
- Obligations of government-sponsored corporations which are eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System.
- Bankers' acceptances purchased on the secondary market.
- Repurchase agreements for securities listed in the three items above, provided that the transaction is structured so that the public treasurer obtains control over the underlying securities.
- Investment deposits with qualified public depositories.
- Offerings of the Washington State Treasurer's Investment Pool.

To the extent that a school district has moneys not required for immediate expenditure, and such moneys are in the control of the county treasurer, and the district has not exercised authority to request the county treasurer to invest the moneys on behalf of the district, the county treasurer may invest such moneys on behalf of the county.

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DEBT AND LEASES

Limitations of Indebtedness

RCW 39.36.015 and 39.36.020 provide that debt cannot be incurred in excess of certain percentages of the taxable real and personal property in the district without the assent of the voters stated as follows:

- 3/8ths of 1 percent—Without a vote of the people.
- 2 1/2 percent—With a vote of the people, 60 percent assent of those who voted.
- 5 percent—With a vote of the people, provided the indebtedness in excess of 2 1/2 percent is for capital outlay, 60 percent assent of those who voted.

These debt limits range from the least restrictive to the most restrictive, without a vote, with a vote, with a vote for capital purposes, and are cumulative for overall debt authority.

Claims and Judgments

Filed and unfiled claims and other impairments of the district's assets should be recorded in the district's accounts and/or otherwise disclosed in the financial statements. Such claims may include:

- Job-related illness, injury to employees, workers' compensation claims.
- Unemployment compensation claims.
- Compensated absences, vested and accrued sick leave, and vacation time.
- Arbitrage rebate.
- Judgments and other damages.
- Auditor's exceptions and monetary findings.
- Acts of God.

The accounting treatment of claims and judgments is dependent upon the degree of likelihood that can be attributed to the occurrence of the event or events. If the likelihood is:

- Probable, where the future event(s) occurrence is likely. If the future event is probable and the amount can be reasonably estimated, then expenditure is made for the liability known and estimated (incurred but not reported), and a fund payable is recorded for amounts that would normally be liquidated with current financial resources. If the amount is one of a range, then the amount posted is the minimal most likely.
- Reasonably possible, where the change of the future event or events occurring is more than remote but less than likely. This situation would require a note disclosure using amounts as calculated above.
- Remote, where there is a slight chance of the future events occurring. This would not require any action on the part of the statement preparer.

Warrants

Warrants are issued when the president or majority of the board signs an order for such and it is countersigned by the secretary (RCW 28A.330.230). Second class districts are required to obtain the approval of the Superintendent of Public Instruction to draw and issue warrants for the payment of money. The superintendent signs all orders for warrants (RCW 28A.400.030).

Districts of the first class derive their authority to issue warrants from RCW 42.24.180. Districts of the second class are required to obtain their authority to issue warrants from the Superintendent of Public Instruction on a one-time basis.

Based on board policy and/or a board resolution, warrants may be issued before approval of the legislative body if the following four conditions have been or are met:

- The auditing officer and the officer signing the instrument of payment have been bonded for at least \$50,000.
- Internal control procedures are in place and are adequate.
- The documents supporting the issuance are made available for review at the next scheduled meeting of the legislative body.
- If upon review the legislative body disapproves any of the items paid, the issuing officer shall pursue collection of the amounts not approved (RCW 42.24.180).

In addition to other duties, the county treasurer:

- Affixes the date of redemption on the face of warrants.
- Endorses "interest-bearing warrant" on the face of such warrants, pays out the interest on interest-bearing warrants, enters the interest paid out in the warrant register, and makes warrant calls when there are funds to redeem such warrants (RCW 36.29.010 through 36.29.060).
- Issues a statement of canceled (redeemed) warrants (RCW 28A.510.270[3]).

Warrants bear interest at the rate authorized by the issuing authority (RCW 39.56.020). The issuing officer fixes the rate of interest to be paid (RCW 39.56.030). When there are insufficient funds, the issuing authority may establish a line of credit for payment of warrants and interest (RCW 43.09.2853).

Warrants shall be canceled after one year, and the records shall be as if the warrants were never issued (RCW 39.56.040).

ASB warrants cannot be issued without funds on deposit (RCW 28A.325.030).

A facsimile signature for any officer may be obtained by filing with the Office of the Secretary of State authorizing them to sign:

- Public securities such as bonds, notes, certificate of indebtedness, or other evidences of obligation.
- Instruments of payment such as checks, drafts, or warrants or orders for payment, delivery, or transfer of funds.

Short-Term Obligations

When a school district borrows money, it can face some difficult budgeting and accounting problems. Over-expending its budget can result if these transactions are not properly recorded. Short-term debt is very different from long-term debt in terms of creating budget capacity—long-term debt can create budgetable resources, while short-term debt cannot.

This section discusses accounting and budgeting for the following three types of school district debt:

1. Short-term obligations (Chapter 39.50 RCW).
2. Conditional sales contracts for acquisition of property (RCW 28A.335.200).
3. General obligation notes and bonds issued without vote of the people for the purchase of real and personal property (RCW 28A.530.080).

Short-Term Debt Contrasted with Long-Term Debt

Short-Term Debt: Any debt obligation with an original maturity of less than twelve months or any debt obligation issued under Chapter 39.50 RCW (Short-Term Obligations—Municipal Corporations). Chapter 39.50 RCW defines short-term obligations as “warrants, notes, or other evidences of indebtedness, except bonds.”

Under this definition, revenue anticipation notes (RANS) are considered short-term obligations regardless of their maturity. Repayment of a revenue anticipation note can only be made out of anticipated future revenues. Section B50 in the Codification of Governmental Accounting and Financial Reporting Standards, published by the Governmental Accounting Standards Board (GASB), states the tax and revenue anticipation notes should be reported as a fund liability in the fund receiving the proceeds. This means revenue anticipation notes are short-term obligations and do not increase fund balance. They do not produce budgetable resources and cannot be used to balance budgets.

Section B50.102 Reporting in Fund Financial Statements—Governmental Funds

For governmental funds, if all legal steps have been taken to refinance the bond anticipation notes and the intent is supported by an ability to consummate refinancing the short-term notes on a long-term basis in accordance with the criteria set forth in FASB Statement 6, they should be reported only as general long-term liabilities in the governmental activities column of the government-wide statement of net assets. If the necessary legal steps and the ability to consummate refinancing criteria have not been met, then the bond anticipation notes should be reported as a liability in the governmental fund receiving proceeds as well as in the government-wide statement of net assets. Tax and revenue anticipation notes should be reported as a liability in the governmental fund receiving proceeds. (NCGAI 9 GASBS 34 82.)

Revenue anticipation notes include tax anticipation notes (TANS) or any similar type of short-term obligation that will be repaid out of anticipated revenues. For example, a revenue anticipation note can be simply a loan from a bank.

Long-Term Debt: In school district budgeting and accounting, the use of conditional sales contracts, or nonvoted notes and nonvoted bonds is considered to be long-term financing if the debt obligation matures at least twelve months from the date of the conditional sales contract or the date of issuance of the note or bond. This definition is part of what is called the “measurement focus” of long-term debt, which identifies the type of debt to be considered long-term.

Budgeting Short-Term vs. Long-Term Debt

RCW 39.50.020 states that short-term obligations are subject to “any applicable budget requirements.” An often overlooked problem associated with the use of short-term debt obligations is that the proceeds cannot be used to balance budgets. A school district must balance its budget on a fund balance basis. Short-term debt obligations simply increase cash balance and do not increase fund balance because the increase in cash from the loan is offset by the liability for repayment by the fund.

In contrast to short-term financing through the use of RANS, financing acquisitions using long-term nonvoted debt creates budgetable resources. This is because the liability created is not accounted for as a liability of the issuing fund, thereby increasing the fund balance of the acquiring fund by the amount of the liability being excluded from the fund’s balance sheet. Two subsidiary revenue accounts to General Ledger Account 965 Other Financing Sources are used to recognize the amount financed in the acquiring fund. These accounts are Account 9100 Proceeds from the Sale of Bonds and Account 9500 Long-Term Financing.

Accounting and Budgeting for RANS

RANS are loans to the school district. They are accounted for as balance sheet transactions only. Payments for principal on a RAN should never be recorded as expenditures but as reductions of the payable account. They should not be recorded in Expenditures Program 97 Debt Service. Only the interest expenditures resulting from the issuance of the RAN should be recorded in Program 97, Activity 83 Other Interest in the General Fund or the Transportation Vehicle Fund or Expenditure Type 91 Interest in the Capital Projects Fund.

See sample journal entries in Chapter 7, Section 12.

Accounting and Budgeting for Conditional Sales Contracts and Long-Term Nonvoted Debt

A Conditional Sales Contract is a form of sales contract in which the seller retains title until paid off.

A nonvoted note is a loan from a bank or similar lender, or a transaction that has the elements of a conditional sales contract, except that the district receives title to the acquisition immediately and the original vendor is paid off with the loan proceeds.

Long-term conditional sales contracts and long-term nonvoted notes are accounted for in the same way. In all situations, the district should record the transaction on a gross basis, before trade-in values, rather than recording a composite amount that represents only the net amount of offsetting transactions. The fact that payment is made directly to a vendor on

a district's behalf does not alleviate the need for fully reporting the transaction in the district's accounting system.

Second Expenditures or Double Expenditures in Long-Term Conditional Sales Contract or Nonvoted Note Financing

Financing through the use of a long-term conditional sales contract or a long-term nonvoted note results in a second expenditure that school districts should be aware of in budgeting, even though this additional expenditure is fully offset by a credit in General Ledger Account 965 Other Financing Sources, subsidiary Account 9500 Long-Term Financing.

The first expenditure arises because the acquiring fund must recognize as an expenditure the full purchase amount of the asset when it is acquired, regardless of the method of financing its purchase. This expenditure is recorded as a Capital Outlay (Object 9) in either the General Fund or the Transportation Vehicle Fund, or in the appropriate expenditure type in the Capital Projects Fund.

In addition to this expenditure, GAAP require that expenditures for long-term debt principal be recognized at maturity. This is the second or double expenditure, and is recorded as an expenditure for debt payment in Program 92 Debt Service, Activity 84 Debt Principal. Since the Capital Projects Fund does not have the same expenditure program format as do the other two funds, Expenditure Type 91 Debt Principal should be used.

While this may seem to be counterintuitive, it is not a new concept at all; its analogue already exists in the present relationship between the Debt Service Fund and the Capital Projects Fund, under which the proceeds of a bond sale are expended by the Capital Projects Fund. Bond retirements are later recognized as debt service expenditures in the Debt Service Fund. The only difference with long-term conditional sales contract or nonvoted note financing is that only one fund is used. To the district in its entirety, under either situation, a second or double expenditure exists.

The principal portion of matured long-term nonvoted notes should be charged to Program 92, Activity 84 Principal. The interest portion of any matured debt should be recorded in Program 92, Activity 83, Object 7. Unmatured principal is recorded in the Schedule of Long-Term Debt.

See sample journal entries in Chapter 7, Section 12.

Nonvoted Bonds under RCW 28A.530.080

Under RCW 28A.530.080 nonvoted bond proceeds must be deposited in the district's General Fund, Transportation Vehicle Fund, or Capital Projects Fund as applicable. All bonds are accounted for and retired in the Debt Service Fund, including nonvoted bonds issued under RCW 28A.530.080. This differs from the retirement of nonvoted notes or conditional sales contracts, in which the debt is retired in the fund that received the proceeds.

Bonds are more formal than notes. Bonds are usually underwritten by an underwriter, frequently for placement with another client of the underwriter. Bonds are accompanied by a legal opinion and are almost always long-term. Payments for maturing bonds and payment

of interest are usually, but not necessarily, paid by a fiscal agent. See sample journal entries in Chapter 7, Section 12.

Local Option Capital Asset Lending (LOCAL) Program

LOCAL Program financing is administered through the Office of the State Treasurer (OST) and is a type of Certificate of Participation (COP). A COP is a third-party borrowing option for financing capital acquisitions. Other COPs are typically lease-purchase agreements. See Chapter 8, Section 14.

The LOCAL Program is an expanded version of the state agency lease/purchase program. The program was originally created by the Legislature in 1989 (RCW 39.94) to provide the lowest cost financing for state agency purchases by pooling funding needs into larger offerings of securities. The Legislature passed legislation in 1998 to provide local governments, including school districts, access to the program. Local government agencies can finance equipment or real estate needs through OST subject to existing debt limitations and financial considerations.

LOCAL financing agreements must be recognized as long-term debt. As such, they are included in the district's schedule of long-term debt and notes to the financial statements and recorded in and paid from the Debt Service Fund. Districts should recognize the "revenue" or money provided by the financing agreement by booking General Ledger Account 965 Other Financing Sources and expenditure account 530, equal to the amount of the financing agreement. See sample journal entries in Chapter 7, Section 14.

Regular Method of Advance Bond Refunding

In this method, the proceeds from the sale of refunding (new) bonds are placed in the custody of the trust department of a bank through the county treasurer. The bank establishes an escrow account and invests the proceeds. The cash realized from the maturing investments, together with interest earned, is used to meet the debt service requirements of the refunded (old) bonds and to redeem the balance of the old bonds when they become callable or mature. The old debt is removed from the appropriate fund and the new debt is added to the appropriate fund at the time the proceeds of the sale of the new bonds are paid to the trust department of a bank.

Crossover Method of Advance Bond Refunding

This method provides for the sale of refunding (new) bonds whose proceeds are used to purchase certain investments that are placed in the custody of the trust department of a bank. The investments provide interest earnings that are used to pay interest on the refunding (new) bonds until the crossover date when the refunded (old) bonds are callable or mature. When the call date or maturity date arrives, the old bonds are redeemed with the resources in the escrow account. After the old bonds are redeemed, the source of revenue applicable to the old bonds is used to service the new bonds. The refunding (new) bonds are entered in the appropriate fund at the time they are sold. The refunded (old) bonds continue to be reported in the original fund until the crossover date at which time they are removed from the original fund.

Arbitrage

Arbitrage in government finance is generally defined as the process of investing tax-exempt bond proceeds in higher yielding taxable securities with the resulting interest revenues exceeding the interest costs.

The Tax Reform Act of 1986 requires that issuers of tax-exempt debt comply with the arbitrage yield restrictions and the ultimate rebate requirements of any excess earnings in order to maintain the tax-exempt status of the debt instrument. The arbitrage yield restrictions limit the retainable earnings from debt issuance proceeds to the yield rate of the debt instrument issued. Any excess earnings are to be rebated or paid to the U.S. Treasury. These arbitrage rebate requirements are in addition to other pre-existing restrictions that can make a debt issue taxable.

The Treasury Department's arbitrage rules and their application extend far beyond the issuance of general obligation and revenue bonds and notes. Part of the regulation is the requirement that installment purchase agreements of state and local governments are also included and subject to the same limitations. These purchase arrangements go by many names: tax-exempt leases, municipal leases, installment sales, lease-purchase agreements, conditional sales contracts, certificates of participation (COPs), and lease-to-ownership agreements.

Arrangements such as these, coupled with other borrowings or issues, could put a district over the small issuer threshold and subject other borrowings to the rebate calculations and penalties.

Arbitrage rebate is a tax and should be shown as an expenditure like any other tax. Arbitrage rebate is an income tax at a 100 percent marginal rate.

Whether the arbitrage liability is probable or only possible will depend on the circumstances of each case. If the financial report preparer believes that it is probable that an asset has been impaired, or a liability incurred, and the amount of the liability can be reasonably estimated, then a charge to current operating expenditures is appropriate.

The liability represents a claim against the financial resources of the school district. The current portion of the liability is represented in the government that has received the investment proceeds. The current portion is the amount that would be paid with expendable available financial resources regardless of when the amount is due. The amount of the liability is the current value of the future payable and represents a portion of the interest income of the fund (that amount represented as an excess over what the investments would have produced if invested at the issued security net rate).

Arbitrage is a very complicated issue. Districts are advised to seek competent counsel concerning the calculation of the liability.

Capitalized Leases or Leases with Option to Purchase

RCW 28A.335.170 affords the district the right to enter into contracts to provide pupil transportation services; lease building space and portable buildings; and lease or have maintained security systems, computers, and other equipment with board approval.

If a lease meets any of the criteria listed below for capitalized leases, it is accounted for as if a purchase contract had been entered into (FASB Statement 13).

- 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 75 percent or more of the estimated economic life of the leased property.
- The present value of the minimum lease payments at the inception of the lease, excluding executory costs, equals at least 90 percent of the fair value of the lease property.

Capital assets acquired through a capital lease agreement should be recorded in the appropriate fund at the lesser of (1) the present value of the rental and other minimum lease payments or (2) the fair value of the leased property. This amount should be established in the appropriate fund as other financing sources and an expenditure. Outstanding principal should be disclosed on the Schedule of Long-term Debt.

Note disclosure is required for capitalized leases.

See RCW 28A.335.200 for conditional sales contracts for the acquisition of property or property rights. See sample journal entries in Chapter 7, Section 11.

Operating Leases

RCW 28A.335.170 affords the district the right to enter into contracts to provide pupil transportation services; lease building space and portable buildings; and rent/lease or have maintained security systems, computers, and other equipment.

Leases that do not satisfy any of the criteria for capitalization are operating leases. Operating leases do not generate asset or liability recognition at their inception. The lease payments are recognized as expenditures as they become payable.

Note disclosure is required for operating leases.

Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and sick leave. Consideration should be given to the different characteristics of various types of compensated absences. For example, employees usually receive full compensation for vacation leave—either as paid time off or as compensation at termination or retirement. Thus, employees earn the right to be compensated for vacation leave based only on rendering past service. On the other hand, paid time off for earned sick leave is contingent on an illness—a specific event that is outside the control of the employer and employee. In some cases, however, subject to board policy, employees may be compensated for a portion of their sick leave when they die, terminate employment under certain circumstances, or retire. In those cases, employees earn the right to be compensated for sick leave at termination based only on rendering past service. (RCW 28A.400.210, WAC 392-136-020.)

Vacation leave and other compensated absences with similar characteristics should be accrued as a liability as the benefits are earned by the employees if the leave is attributable to past service and it is probable that the employer will compensate the employees for the benefits through paid time off or some other means, such as cash payments at termination or retirement.

Sick leave and other compensated absences with similar characteristics should be accrued as a liability as the employees earn the benefits, but only to the extent it is probable that the employer will compensate the employees for the benefits through cash payments conditioned on the employees' termination or retirement (termination payments). Alternatively, the liability should be measured based on the sick leave and other compensated absences with similar characteristics accumulated at the balance sheet date by those employees who currently are eligible to receive termination payments as well as to other employees who are expected to become eligible in the future to receive such payments. When the liability is calculated, these accumulations should be reduced to the maximum amount allowed as a termination payment.

The compensated absences liability should be measured using the pay or salary rates in effect at the balance sheet date. Certain salary-related payments directly and incrementally associated with the payment of compensated absences, for example, the employer's share of social security and Medicare taxes, should also be accrued. Payments made that are not ordinarily directly and incrementally connected with the amount of leave paid to employees (such as life insurance and health insurance) should not be accrued.

For governmental and permanent funds, the current portion of the liability should be reported as a current liability in the funds; the remainder of the liability should be reported as a long-term liability in the funds. Compensated absences expenditures should be recognized using a modified accrual basis of accounting. A complete explanation of the method of calculating accruals, including examples, can be found in GASB Statement 16, which is discussed in Appendix C.

Auditor's Exceptions and Monetary Findings

Audit reports with material monetary findings or internal control findings that could cast doubt on the validity of the financial reports are subject to a broad array of accounting treatments.

The audit report is subject to a desk review by the Superintendent of Public Instruction (chapter 392-115 WAC). The audit monetary finding is *prima facie* case for recovery of funds that, unless rebutted, is sufficient to sustain the conclusion drawn in the audit.

The timing of the exception determines how it will be reported in the district's year-end financial report. If the item of dispute is discovered before the books for the current fiscal year have been closed, the necessary adjustment to the records can be made. If the finding arises after the books have been closed but before the financial statement has been published, a note disclosure would be included. Any questions as to materiality of the finding should be addressed first.

Unemployment Compensation, Self-Insured

The unemployment compensation laws codified in Title 50 RCW are administered by the Employment Security Department.

The self-insurance provision of the unemployment compensation act makes no provision for group coverage. The act provides only for the election to make payments in lieu of contributions or to reimburse the department for payments made on behalf of the school district to the district's ex-employees (RCW 50.44.20 and 50.44.060).

If an employer has elected the reimbursement method, they will be billed at the end of each calendar quarter for payments made by the Employment Security Department for that quarter.

The Employment Security Department may require a surety bond or the deposit of money or securities in an amount estimated to cover one year's claims, but not to exceed an amount equivalent to one year's premium. The amount of the security is subject to review and renewal by the department.

The school district will have to be certain that the rate of accrual at which the expense is incurred will produce an estimated benefit payable sufficient to cover:

- Claims incurred and claimed but not paid.
- Claims incurred but not claimed.
- Claims not yet incurred but highly possible.

If excess insurance is purchased, the cost of the insurance should be charged to the benefit accrual.

Workers' Compensation, Self-Insured

Claims for injury resulting from employment exposures are not subject to regular civil action. The jurisdiction of courts for this class of torts has been abolished by legislative action and industrial accidents and resulting compensated losses are administered by the state (Title 51 RCW).

The self-insured portion of workers' compensation covers two items: medical aid that pays for illness or injury medical treatment, and workers' compensation that provides compensation for losses including wages and survivor benefits. Both of these are the district's expense. A third element, prior pension and asbestos fund, is an assessment against the employee with an equal amount paid by the employer (RCW 51.32.073).

Districts can become self-insured by application to the Department of Labor and Industries either on an individual basis, or there is a provision for group insurance where any two or more school districts or educational service districts may form a group for purposes of self-insuring workers' compensation benefits.

The agreement between the school district and the risk pool may transfer part or all of the risk to the risk pool. Self-insurers may reinsure their risks but not to exceed 80 percent.

There is a surety requirement for school districts that shall be an amount that will satisfy 100 percent of the claims for the succeeding fiscal period. The minimum security requirement shall be \$100,000; in addition, a cumulative reserve of no less than 25 percent of the surety requirement must also be established.

The Department of Labor and Industries may require a deposit to be placed in an escrow or depository account, the deposit of money or securities, or the posting of a surety bond.

Monetary assets are accumulated for the purpose of meeting claims or expenses by the same payroll process that would accumulate and transmit the premium for state insurance claims processing. This procedure assesses the district a monetary amount for each hour of employment with the employees classified into three groups. The three classes are:

- Professional (e.g., clerical, teaching, administrative).
- Maintenance workers, bus drivers, food service workers.
- Volunteers (medical aid only).

If the district lacks a system of recording hours of attendance and absences for salaried employees, the district is to use the assumed hours rule and report salaried employees at 40 hours per week and 160 hours per month. The assumed hours for premium calculation for teachers are to be calculated at 180 days at eight hours per day—1,440 hours. This can be reported at either 120 hours per month for 12 months or 160 hours per month for nine months. The accumulation of most of the accrued liability, estimated industrial insurance benefits payable, takes place during the payroll taxes and benefits calculation portion of the payroll process.

If there are enough volunteer hours in the district to justify the entry, a periodic journal voucher charging the appropriate programs with the equivalent standard premium should be prepared. The number of hours times the medical aid rate for volunteers is the amount that should be charged.

In addition to the claims processed which are charged against the accrual generated by the medical aid and workers' compensation charges, the following items are also charged to the account:

- Administration expense assessed by the Department of Labor and Industries.
- Second injury fund assessment by the Department of Labor and Industries.
- Third party claims management and administrative fees.
- Surety bond expense.
- Excess insurance premium.
- Supplemental pension and asbestos fund (this portion of the accrual was generated by a separate charge on both employee and employer and this portion of the program is handled by Labor and Industries).

A report is due the Department of Labor and Industries by July 1 of each year showing estimated claims liability and the sources of revenue to meet those obligations. The documentation of the cumulative reserve must specify the type of funding and reflect the account balance. Surety requirements for governmental units are subject to periodic review by the department.

When this report is prepared, it would be the opportune time to assess the validity of the accrued benefit payable to make certain that the accrual rate is providing resources sufficient to pay claims incurred but not paid, as well as claims incurred but not reported. Any projected over- or under-accrual would be compensated for by adjustment of the assessment rates on each class of employee.

Duplicate Instruments

From time to time, payment instruments (warrants or checks) are lost by the recipient and it is necessary to issue a duplicate payment.

Before a duplicate instrument is issued, the issuing officer shall require the recipient or the person representing the recipient to make application for the issuance of the duplicate by filing a written affidavit specifically alleging on oath that he/she is the proper owner, payee, or legal representative of such owner or payee of the original instrument. Additional information required in the affidavit is the date of issue, the number, the amount, and for what services, claim, or purposes the original instrument or series of instruments of which it is a part of was issued, and that the original has been lost or destroyed and has not been paid.

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INTERFUND TRANSACTIONS

Interfund activity is classified as reciprocal and nonreciprocal. Reciprocal interfund activity is the internal counterpart to exchange and exchange-like transactions and includes interfund loans and interfund services. Nonreciprocal interfund activity is the internal counterpart to nonexchange transactions and includes interfund transfers and interfund reimbursements.

Interfund Loans

Interfund loans are authorized (WAC 392-123-135 through 160), when approved by resolution by the school district board of directors as required, subject to the following:

- Loans are allowable to and from specific funds:

FROM:	TO:
General Fund (GF)	Capital Projects Fund (CPF)
	Debt Service Fund (DSF)
	Transportation Vehicle Fund (TVF)
Capital Projects Fund (CPF)	General Fund (GF)
	Debt Service Fund (DSF)
	Transportation Vehicle Fund (TVF)

- An interfund loan is considered to be a temporary loan of moneys between one district fund and another. An interfund loan is not considered to be an investment. As a temporary loan, it is to be completely liquidated in less than one year from the date of issuance.
- Loans shall not be made from any fund to the detriment of any function or project for which the fund was established. Moneys loaned should only include moneys that are clearly inactive or in excess of current needs.
- Interest shall be paid by the borrowing fund to the loaning fund and shall be at a rate not less than the warrant interest rate in the county in which the school district is considered to be located. The interest shall be a revenue of the loaning fund and an expenditure of the borrowing fund. Interest earned cannot be transferred to another fund.
- Financial reports of the district shall specify all outstanding interfund loans and all interest charges involved. The interfund loan shall not be used to balance the budget of the borrowing fund.
- The board of directors shall authorize the interfund loan by adopting a resolution stating the exact amount of the loan, the funds involved, the specific source of the repayment, the schedule for the repayment, and the interest rate involved.
- Interfund loans should be reported as interfund receivables in the lender funds and interfund payables in the borrower funds. This activity should not be reported as other financing sources or uses in the fund financial statements.

Interfund Transfers

GAAP defines interfund transfers as “flows of assets (such as cash or goods) without equivalent flows of assets in return and without a requirement for repayment.” These transfers are permanent. Interfund transfers are recorded as other financing uses in the fund making the transfer and other financing sources in the fund receiving the transfer.

Transfers of resources between funds are allowed in situations when the transfer is justified by meeting certain criteria outlined as follows:

- Transfers may be made from the General Fund to the Transportation Vehicle Fund as authorized by the adoption of a resolution of the board of directors. However, the district’s board adopted budget, if it accurately reflects the desired transfer, may serve as the required resolution.
- Transfers may be made to the Debt Service Fund from any fund issuing debt through nonvoted bonds (i.e., General Fund, Capital Projects Fund, and/or Transportation Vehicle Fund) to meet debt service payments. Authorization for the transfer should have been granted in the resolution authorizing the issuance of the debt.
- Transfers for the redirection of state apportionment may be made from the General Fund to the Capital Projects Fund and/or Debt Service Fund, subject to the following conditions and requirements:
 - The transfer will not result in a negative estimated ending fund balance in the General Fund.
 - The district board of directors must execute a resolution requesting OSPI to approve the transfer. The transfer must specify the justification in detail and the dollar amount to be transferred. This resolution must be received by OSPI on or before the tenth of the month in which the transfer is to begin.
- The spring of 2007 Legislative session provided districts with additional authority to:
 - Transfer moneys related to state forest revenue from the Debt Service Fund to the Capital Projects Fund.
 - Transfer monies from the Capital Projects Fund to the General Fund for certain technology expenditures.

See Appendix E for further guidance.

Residual equity transfers are no longer specifically named in GAAP but are a type of nonreciprocal interfund transfer. Residual equity transfers are included in this section and are allowed in situations when the transfer is justified by meeting certain criteria outlined as follows:

- Equity transfers are initiated by board resolution and occur when the purpose for which a fund was established no longer exists, however, the district’s board adopted budget, if it accurately reflects the desired transfer, may serve as the required resolution.
- All claims against the fund to be closed must be resolved before the authority to make the equity transfer is executed.
- Examples of equity transfer situations include:
 - Closing the Debt Service Fund to the General Fund after all bonds, interest, and transfer fees have been paid.
 - Closing the Capital Projects Fund after all capital construction projects are complete and claims have been paid. (Surplus moneys originally acquired by bond resolution in the Capital Projects Fund are first transferred to the Debt Service Fund for

payment of any remaining debt. Once the remaining debt is repaid, remaining surplus moneys must be transferred to the General Fund to reduce General Fund levies.)

- Subsequent tax collections in either example should be credited to the General Fund.

Interfund Reimbursements

Interfund reimbursements are repayments from the funds responsible for particular expenditures to the funds that initially paid for them. See Chapter 3, Section 3, page 4 for further guidance.

Crediting Investment Earnings

When authorized by the board of directors, any interest or earnings on investments being credited to a fund different from that which earned the interest or earnings shall only be expended for instructional supplies, equipment, or capital outlay purposes as long as it is not restricted or prohibited by another statute (RCW 28A.320.320).

For example, RCW 28A.160.130 does not permit transfer of funds from the transportation fund to any other fund. Similarly, RCW 28A.325.030 requires all moneys generated through the programs and activities of any Associated Student Body be deposited in the Associated Student Body program fund. It allows investment *for the sole benefit of the Associated Student Body program fund* in the items enumerated in RCW 28A.320.320.

RCW 28A.530.030 and RCW 28A.230.330 require moneys from bonds issued and sold be deposited to the Capital Projects Fund where they and interest earnings on them be used only for capital purposes under RCW 28A.530.010 or be deposited to the Debt Service Fund. Once in the Debt Service Fund only the interest on the bond interest, not the bond interest itself, would be eligible for credit to another fund for uses described above under joint ventures and interlocal governmental agreements.

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JOINT VENTURES AND INTERLOCAL GOVERNMENTAL AGREEMENTS

Authority

RCW 39.34 authorizes school districts as well as public agencies, to form joint ventures, generally referred to as “Shared Service Arrangements” or “cooperatives,” for the provision of services or the sharing of facilities. (For more information on accounting for shared service arrangements, see Section 11 of this chapter.) Joint ventures can be among school districts, other local government agencies, state government agencies, federal government agencies, or a combination of such governments. Such joint ventures are either “joint operating agencies” or “contracted interlocal agreements” depending on the form of governmental organization that meet the geographic, economic, population, or other factors influencing the decision to form the joint venture. Specific law dictates other limitations or requirements on the joint venture. School districts use these forms of cooperatives to provide athletic league management, special instructional facilities and programs, and employee benefit programs.

Descriptions of cooperative requirements are as follows:

- The interlocal agreement is a contract allowing the parties to jointly exercise some power, privilege, or authority already capable of being exercised by the parties as independent agencies of government. The manner of financing the joint venture shall be as provided by law. The duties, rights, and responsibilities of the cooperating agencies should be delineated in the agreement.
- The agreement may establish a separate legal or administrative entity, which must be legally authorized. The agreement must specify the duration of the agreement, organization of the administrative entity, purpose of the agreement, manner of financing, and the methods of termination. The entity would be subject to audit in the manner provided for all public entities.
- If the agreement does not establish a separate legal entity, the agreement must specify the items in the preceding paragraph and provide for an administrator or a joint board responsible for administering the cooperative undertaking. The agreement must detail the manner of the joint board in acquiring, holding, and disposing of real and/or personal property used in the joint venture.

RCW 39.34.040 requires interlocal governmental agreements be filed with the county auditor or, alternatively, listed by subject on a public agency’s web site or other electronically retrievable public source.

Accounting Procedures

To determine the accounting treatment, the interlocal agreement must be evaluated by each member district to determine if there is a financial interest and/or oversight responsibility for the joint venture. If no equity interest or responsibility is retained by the district, or the district does not exercise oversight responsibility, the interlocal agreement should be footnoted and accounted for in an appropriate fund of the district.

SHARED SERVICE ARRANGEMENTS

A Shared Service Arrangement (SSA) is formed when two or more entities agree to join together and perform specific services. SSAs are also referred to as cooperatives or consortiums.

An SSA is not a separate legal entity, but may be governed by a legal document (i.e., interlocal agreement). The legal document may describe the services to be furnished and address the provision of various administrative functions.

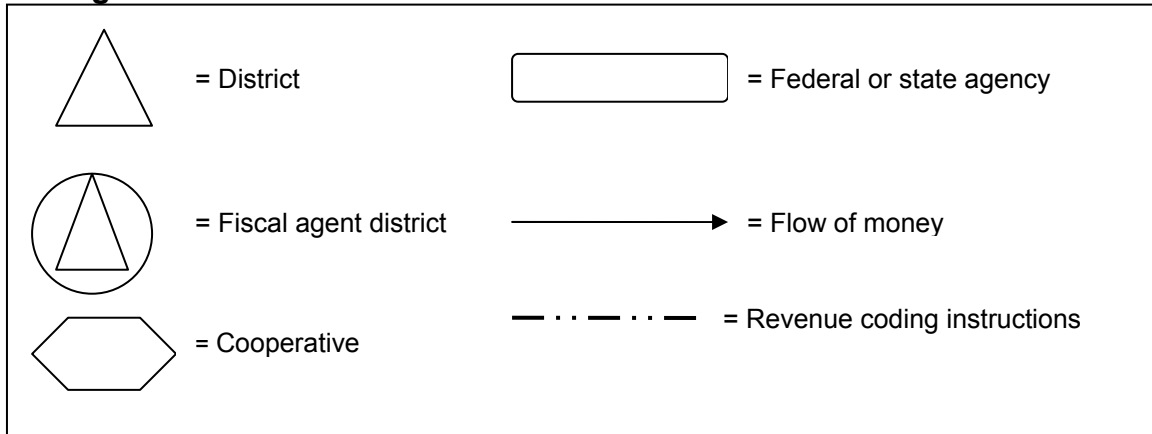
Numerous federal programs, as well as many state-funded programs, encourage, and in some instances, require districts to be a part of an SSA. This additional nuance to SSAs requires us to define some specific terms when involved in these arrangements:

- **Fiscal Agent:** An entity which has been empowered to handle fiscal matters for another entity, including disbursement or passing through of funds. This may include ensuring that the funds are used only for specific purposes defined by the grant or agreement.
- **Sub-Recipient:** An entity that expends grants or other financial assistance received from a fiscal agent and/or a pass-through entity.
- **Pass-Through Entity:** An entity that provides grants or other financial assistance received by a governmental entity to transfer to, or spend on behalf of, a secondary recipient or sub-recipient.
- **Vendor:** A dealer, distributor, merchant, or other seller providing goods or services that are required for the conduct of a federal or state program. These goods or services may be for an organization's own use or for the use of beneficiaries of the federal or state program. (For example, an ESD or school district that provides a service to another ESD or school district would be considered a "vendor.")

The preceding definitions are illustrated in the following charts:

Funding Flow Charts for Shared Service Arrangements

Legend:

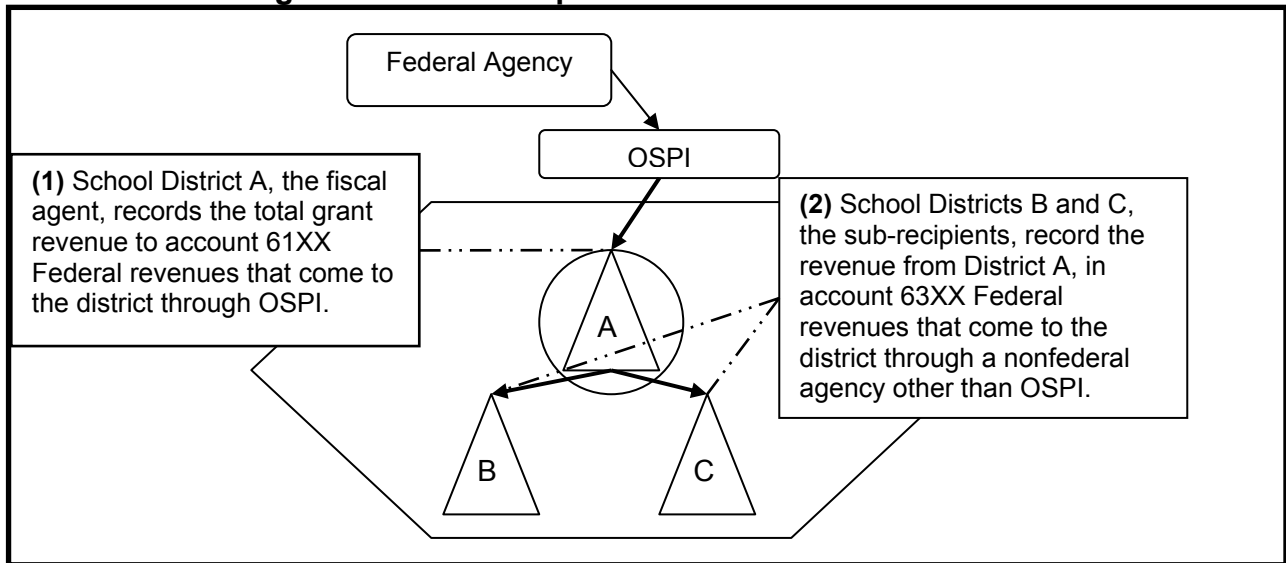


Fiscal Agent and Sub-Recipient

In this example, we have a federal grant that is being passed through from one district to another. The grant requires there to be a fiscal agent who passes through grant money to member districts. Refer to Chapter 7, Section 9 for more information on participating and non-participating fiscal agents.

- District A is the fiscal agent for the grant.
- Districts B and C are sub-recipients of the grant.
- Districts A, B, and C are in a shared service arrangement.
- When the proceeds of the grant are awarded from the federal agency to OSPI, OSPI passes the funds through to District A (the fiscal agent), who records the total grant revenue to account 61XX, Federal revenues that come to the district through OSPI. See (1) on Chart 1.
- District A will then “pass through” the appropriate amount of grant proceeds to Districts B and C (the sub-recipient districts). Districts B and C then record the grant revenue to account 63XX, Federal revenues that come to the district through a nonfederal agency other than OSPI. See (2) on Chart 1.

Chart 1 – Fiscal Agent and Sub-Recipient

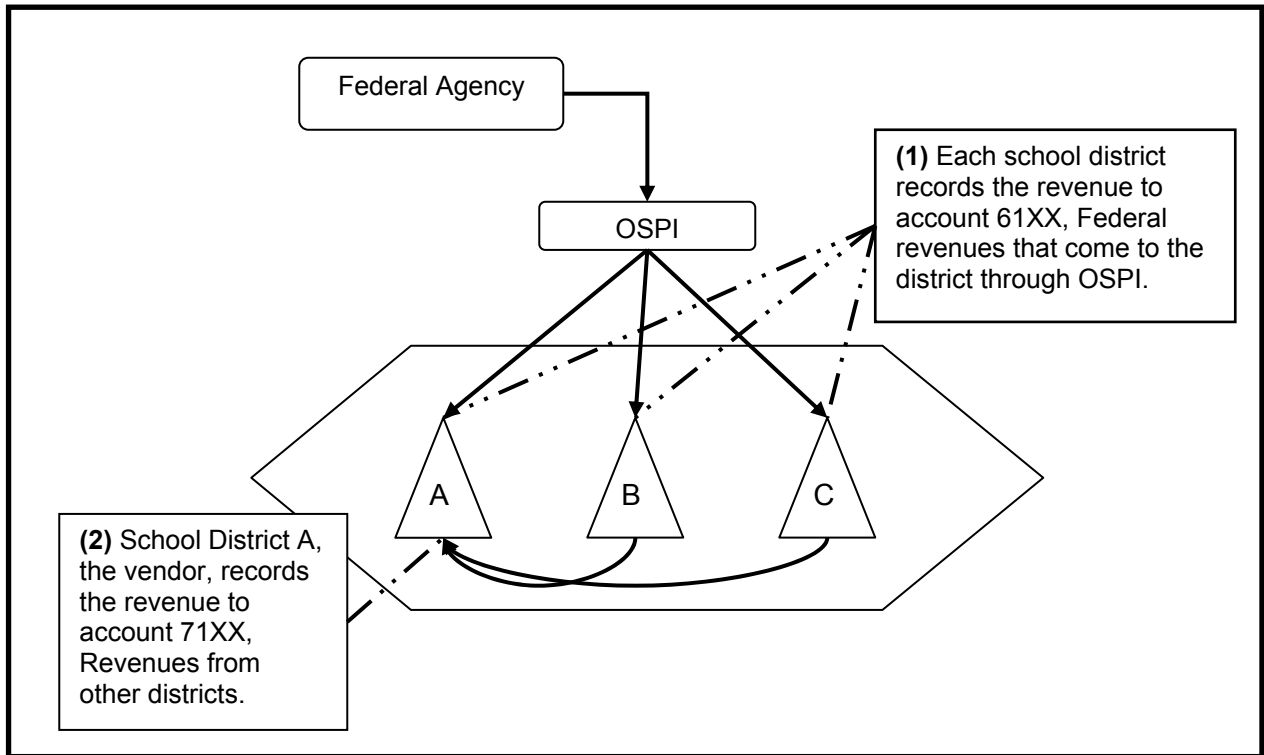


Vendor

This is an example of a school district providing a contracted service to other school districts. School Districts A, B, and C are receiving federal funding from OSPI for xyz program. School Districts A, B, and C have entered into a shared service arrangement (or a cooperative). District A, the **vendor**, provides xyz program services to their own district as well as Districts B and C. School District A bills School Districts B and C, who then pay School District A for services provided.

- All the districts (A, B, and C) record the federal revenue to account 61XX, Federal revenues that come to the district through OSPI.
- School District A, the vendor, bills Districts B and C for services provided. See (1) on Chart 2.
- School District A records the revenue from Districts B and C to account 71XX, Revenues from other districts. See (2) on Chart 2.

Chart 2 – Vendor

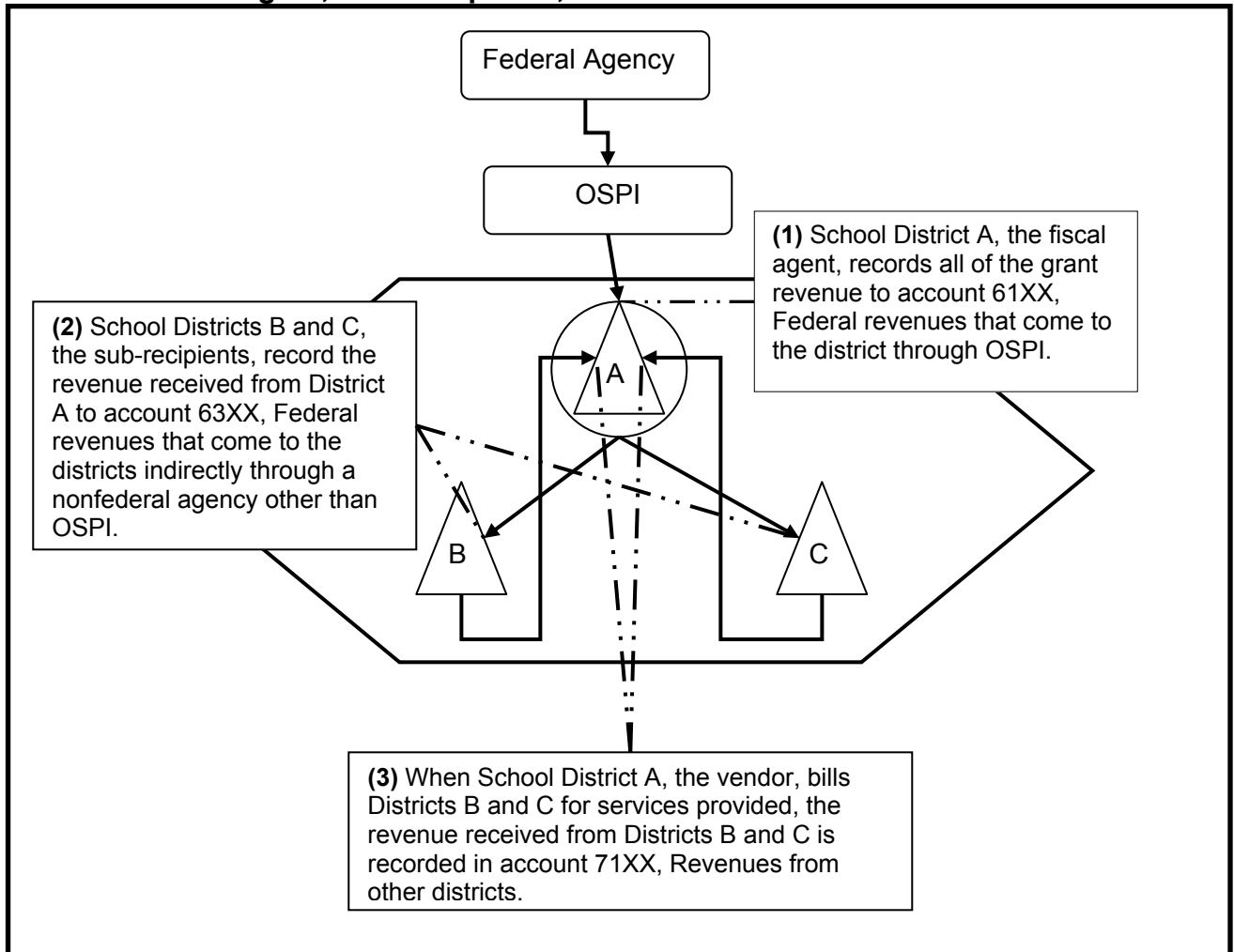


Fiscal Agent, Sub-Recipients, and Vendor

School Districts B and C apply for a federal grant; however, the districts do not qualify for the grant on their own, but may be able to receive the grant money if they use a qualifying school district to be the **fiscal agent**. School District A agrees to be the fiscal agent of the grant for School Districts B and C, the **sub-recipients**. In addition to the fiscal agent responsibilities for the grant, School District A is also providing services to the member districts as a **vendor**.

- School District A, the fiscal agent, receives the federal revenues from OSPI and records all of the grant revenue to account 61XX, Federal revenues that come to the district through OSPI. See (1) on Chart 3.
- School Districts B and C, the sub-recipients, receive their portion of the grant and record the revenue received from District A to account 63XX, Federal revenues that come to the districts indirectly through a nonfederal agency other than OSPI. See (2) on Chart 3.
- When School District A, the vendor, bills Districts B and C for services provided, the revenue received from Districts B and C is recorded in account 71XX, Revenues from other districts. See (3) on Chart 3.

Chart 3 – Fiscal Agent, Sub-Recipients, and Vendor



Responsibilities of the Fiscal Agent

The fiscal agent usually performs the budgeting and accounting responsibilities related to the project. The fiscal agent generally is responsible for ensuring revenues are used in accordance with grant provisions and **may** be responsible for ensuring other requirements, such as matching and maintenance of effort, are met.

If the program revenues are not used in accordance with the grant provisions, the fiscal agent may be financially responsible for the consequences of instances of noncompliance. The fiscal agent may also be financially responsible if a member school district is unable to pay back its respective portion of questioned costs.

As the title suggests, the entity selected as the fiscal agent for a shared service arrangement is responsible for the overall financial management of the program. This **may** include:

- **Processing Financial Transactions:** Includes the request for and deposit of grant revenue, payment of all allowable expenditures, and preparation of journal vouchers.
- **Maintaining Source Documentation:** Includes invoices, bills, payroll records, etc. to substantiate expenditures.
- **Preparing and Submitting Requests:** Includes requests for program revenues to the granting agency.
- **Preparing and Distributing to Member Units:** Includes a final financial report allocating total program costs to each of the member units. (Individual districts are responsible for reporting their share of expenditures on the annual financial reports submitted to the granting agency.)

Responsibilities of Member Districts

Member district responsibilities usually concern employment of personnel, budgeting, accounting, and reporting. A shared service arrangement's agreement should specifically address these or other responsibilities, as appropriate, for the specific agreement. *In general*, the responsibilities may include the following:

- **Budgeting:** It is the responsibility of each member district to budget the portion of the moneys it receives through the fiscal agent.
- **Accounting:** Each member district is responsible for maintaining and having available for audit accounting records for that portion of the moneys it receives from the fiscal agent.
- **Reporting:** The member district is responsible for reporting moneys expended by **its district only** to the granting agency. In addition, the member district is responsible for submitting detailed expenditure information to the fiscal agent for required state or federal reporting.

Note: Responsibilities will vary depending on the specific program and agreement. A written agreement, signed by the fiscal agent and all members, is strongly encouraged.

Fiscal Agent Accounting Treatment

The fiscal agent may be a recipient of the program under the arrangement (a *participating district*), or can administer the arrangement and not receive program revenues (a *non-participating district with or without administrative responsibilities*).

- **Fiscal Agent as a Participating District:** A district that enters into an agreement to administer the grant funds. The district receives the specified funds and disburses such funds in accordance with the outside entity's approval. The district is one of the grant recipients and their district is involved in defining the program and is involved in any program decisions over the allocation or expenditures of such funds at their district.
 - **Accounting Treatment:** All money received by this district should be *recognized as revenue and expenditures* in the fund financial statements. See Chapter 7, Section 10, Scenario 1.
- **Fiscal Agent as a Non-Participating District with Administrative Responsibilities:** A district that enters into an agreement with another entity to administer the entity's specific grant funds, as prescribed by the grantor. The district receives the specified funds and disburses such funds in accordance with the outside entity's approval. The district is not one of the grant recipients, but is responsible for grant compliance.
 - **Accounting Treatment:** All money received by this district should be *recognized as revenue and expenditures* in the fund financial statements. See Chapter 7, Section 10, Scenario 2.
- **Fiscal Agent as a Non-Participating District with No Administrative Responsibilities (Cash Conduit Only):** The district does not have administrative responsibilities, but does receive the specified funds, and disburses such funds in accordance with the outside entity's approval. The district is not one of the grant recipients, is not involved in defining the program, and is not involved in any program decisions over the allocation or expenditures of such funds at their district.
 - **Accounting Treatment:** In infrequent cases, such as this, in which a recipient entity serves only as a cash conduit, the funds should be reported in the agency fund (fund 7). A recipient government serves only as a cash conduit if it merely transmits grantor-supplied moneys without having administrative or direct financial or programmatic involvement in the program. See Chapter 7, Section 10, Scenario 3.
- **Fiscal Agent as a Participating District and On Behalf Payments:** This is the same as the Fiscal Agent as a Participating District, but the fiscal agent purchases services or equipment for themselves and/or the sub-recipients of the program (or on behalf of the other district) in addition to the fiscal agent responsibilities. Purchases are made in accordance with the agreement and the program requirements.
 - **Accounting Treatment:** All money received by this district should be *recognized as revenue and expenditures* in the fund financial statements. See Chapter 7, Section 10, Scenario 4.

GENERAL FUND FUNDRAISING

Based on Attorney General Opinion Cite AGO 2003 No.1, dated February 19, 2003, districts have broad discretion to engage in fundraising activities.

If a school district engages in General Fund fundraising, it is required to establish a board policy.

See the full Attorney General Opinion at www.atg.wa.gov for additional information.

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INDIRECT COST LIMITS, CARRYOVER, AND RECOVERY

Overview

Indirect cost limits ensure that state and federal moneys are expended for intended uses and for allowable costs. Allowable costs include expenditures directly traceable to the program called **direct expenditures**, plus a limited allowance for overhead or **indirect expenditures**. In addition, some programs permit part of the allocation to be **carried over** from the current fiscal period to a future fiscal period. Indirect cost limits and carryover limits are defined in laws, rules, or program requirements. OSPI recovers money from districts that report insufficient direct program expenditures, after allowance for indirect charges and carryover, if permitted. This section describes indirect cost and carryover limits and recovery procedures for many state and federal programs.

For budgeting purposes, districts typically calculate the **minimum direct expenditure** amount by dividing the program revenue by 1.00 plus the district's indirect expenditure rate. The remaining revenue is the maximum indirect charge. For example, if the total allocation is \$100,000 and the indirect limit is 3.0 percent, the following calculations are performed:

$\$100,000 \div 1.03 = \$97,087$ Minimum direct program expenditures.

$\$100,000 - 97,087 = \$2,913$ Maximum indirect charges to the program.

The district may charge **less** than the maximum indirect charges.

Any carryover from the prior year increases the district's minimum direct expenditures in the current year.

State Programs

Many state formula-funded (apportionment) revenues are subject to recovery if not expended for a specific purpose during the school year. In most cases, the recovery calculation is based on school year expenditures as reported on Form F-196, Annual Financial Statement. In some cases, a special report is used to determine recovery.

The 2006–07 school year apportionment recoveries were made in January 2008 based on the final 2006–07 state allocations and year-end expenditures reported to OSPI. The 2007–08 school year recoveries will be made in January 2009 based on final 2007–08 state allocations and year-end expenditures reported to OSPI. At the end of the school year, a spreadsheet for estimating recoveries will be posted on the SAFS web page under Training/Tools at the following link: <http://www.k12.wa.us/safs/TT/tt.asp>.

Federal Programs

Indirect expenditure rates allowed on federal grants awarded school districts are established by the Office of Superintendent of Public Instruction (OSPI) pursuant to an agreement with the U.S. Department of Education (ED). This agreement prescribes the method of rate computation and the resulting rates establish the maximum amount of indirect expenditures that may be claimed

for a federal grant. One fixed with carry-forward indirect cost rate is calculated for each district for all of its restricted federal grants and another fixed with carry-forward indirect cost rate is calculated for all of its unrestricted federal grants.

Rates are annually computed for each district and are unique for each district.

Restricted Versus Unrestricted Indirect Expenditure Rates

Restricted rates are used with grants where “supplement but not supplant” language is in the authorizing legislation. Almost all federal programs fall into this category. Restricted rates must be used for all federal programs except those for which the restricted rate is not required. Questions regarding restricted and unrestricted rates should be made to School Apportionment and Financial Services.

Indirect Expenditures for Cooperative Projects

When there is a cooperative project, the indirect expenditure rate of the administering district is to be used on all direct expenditures claimed in the cooperative project. The indirect expenditure reimbursement is paid to the administering district.

How the Federal Indirect Expenditure Rates Are Computed

Federal indirect expenditure rates for the current year are based upon financial information in each school district’s annual financial statement, SPI Form F-196, for the 2 years prior to the current year. Therefore, the rates depend upon base-year data that are two years old.

An indirect expenditure rate determines what proportion each grant or contract shall bear of the joint or common expenditures benefiting all school district programs. These expenditures are specifically allowed by the U.S. Department of Education to be allocated to all other school district programs. In general, the districtwide federal fixed with carry-forward indirect rate for each school district is computed by dividing total General Fund indirect expenditures by total General Fund direct expenditures. The result of this calculation is the indirect rate.

Indirect expenditures for determining federal restricted rates are selected administrative and service expenditures in Program 97 Districtwide Support. These include expenditures for business office and selected expenditures for superintendent’s office, data processing, printing, warehousing and distribution, and motor pool. Excluded are expenditures for capital outlay and interest.

Each school district also has one districtwide federal unrestricted indirect cost rate for the few federal grants that allow unrestricted rates. The unrestricted rate is the same as the restricted rate except expenditures for maintenance and grounds are included, resulting in a higher rate. Direct expenditures for determining both federal restricted and unrestricted rates consist of all other General Fund expenditures except those for capital outlay and interest which are excluded from the calculation.

For more information regarding federal restricted and unrestricted rates, refer to the Administrative, Budgeting, and Financial Reporting Handbook, Bud Prep Chapter 2, Section 5.