CliftonLarsonAllen

Best of Accounting Complexities – FGFOA Nature's Coast Chapter Spring Meeting

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Learning Objectives

- This session will provide answers to a series of questions that present complex and often overlooked accounting and financial reporting issues. Examples include the following:
  - Debt Issuance in a Governmental Fund
  - Capital Asset Transfer Between Funds
  - Restricted Net Position & Fund Balance
  - Capital Outlay & Capital Asset Additions
  - Revenue Recognition for Property Taxes

Question #1 Debt Issuance in Gov't Fund

- On March 10, 2016, the City of Kissimmee issued $7,500,000 of general obligation bonds to finance the construction of a new recreation center. Debt issuance costs were $60,000, and the bonds were issued at a discount of $282,000. The bond discount and $44,000 of underwriters' fees, bond insurance, and rating agency fees were deducted from the bond proceeds. A month later, the City paid the remaining $16,000 of issuance costs upon receiving an invoice from bond counsel. The initial debt service payment is due on 11/10/16, which includes $150,000 of interest.

Question #1 Debt Issuance in Gov't Fund

- Within the debt service fund on the governmental fund financial statements, the City recorded $7,174,000 ($7,500,000 minus 282,000 minus $44,000) as an other financing source. The remaining $16,000 of issuance costs was recorded as an expenditure when paid. Furthermore, since the debt service payment was to be made within 60 days after year end, the City recorded accrued interest of $125,000 relating to the period 3/10/16 to 9/30/16. Did the City record this correctly?

Answer #1 Debt Issuance in Gov't Fund

- GASB 34, para 87 requires bond issuance costs to be reported as expenditures, not as other financing uses or netted against bond proceeds, on the closing date
- GASB 34, para 88, as amended by GASB 37, para 16, requires issuance discounts and premiums related to general long term debt to be reported as **separate** financing sources and uses

Answer #1 Debt Issuance in Gov't Fund

- GASBI No. 6, para 13 states that a government may report a liability and expenditure for debt service on general long-term debt before it is due for payment only if:
  - "Dedicated" financial resources have been accumulated in a debt service fund **AND**
  - The debt service is due and payable within one to several days after year end but no more than one month after year end

Question #2 – Capital Asset Transfer

- Seminole County is transferring vehicles and equipment out of one fund and into another. The assets have an original cost of $1,340,265 and accumulated depreciation of $766,244.
- What would be the entries to record this transfer from…
  - One enterprise fund to another enterprise fund?
  - An internal service fund to an enterprise fund?
  - A governmental fund to an enterprise fund?

Answer #2 – Capital Asset Transfer

- ***7.74.4. Q***—How should the reassignment of a capital asset between an enterprise fund and governmental activities be reported?
- ***A***—If the assets reassigned from governmental activities to an enterprise fund are capital assets, the transaction is not "interfund" because it involves only one fund; consequently, the enterprise fund would report the receipt of the capital assets as a capital contribution from governmental activities (in the last section of the statement of revenues, expenses, and changes in net position). In the reverse situation, in which a capital asset is reassigned from an enterprise fund to governmental activities, the disposal of the capital asset would be reported by the enterprise fund as a nonoperating expense. In either case, governmental funds would not report the event because there has been no flow of current financial resources. In the statement of activities, the reassignment of the capital asset between governmental and business-type activities would be reported as a transfer, requiring a reconciling item in the governmental funds' reconciliation because a difference is created between the change in fund balances and the change in total net position.

Question #3 – Restricted Fund Balance/Net Position

- The City of Palmetto has the following funds that contain restricted fund balance at September 30, 2016:
  - CRA Fund (entire fund balance restricted) to redevelop the a CRA district = $360,542
  - Street Improvement Fund (capital projects fund that has restricted, committed, and assigned fund balance) = $545,282 restricted. This fund also had unspent bond proceeds totaling $132,365.
  - Debt Service Fund (legally required to set up sinking fund to accumulate cash to pay off debt at maturity) = $229,170

Question #3 – Restricted Fund Balance/Net Position

- The City also has the following modified accrual / full accrual differences to consider:
  - Capital assets, net (general gov't activities) = 22,068,412
  - Bonds & notes payable (general gov't activities) = 5,417,633
  - Pension related amounts and compensated absences allocated across funds based on headcount: 3 employees in Community Redevelopment Fund; zero employees in Street Improvement Fund & Debt Service Fund
  - Grant revenue in Street Improvement Fund awarded in FY '16, collected in January 2017 (City's availability criterion is within 60 days after year end), and spent in FY '17 & FY '18 (eligibility criteria have been met) = $165,438
  - Accrued interest payable in gov't activities (payment recorded in debt service fund) = $123,114

Question #3 – Restricted Fund Balance/Net Position

- The City of Palmetto participates in the Florida Retirement System. It has 26 employees, and 18 of those employees participate in the traditional pension plan, while the remaining 8 employees participate in the Investment Plan (defined contribution plan option). All employees participate in the health insurance subsidy plan ($150 per month stipend upon retirement). As of June 30, 2016, the City's net pension liability consisted of the following:

Amount	FRS Pension (18 employees)	HIS Plan (26 employees)
Net Pension Liability	$1,472,770	$750,660
Deferred Outflows of Resources	$964,240	$94,285
Deferred Inflows of Resources	$905,353	$0
Contributions 7/1/15 – 6/30/16	$278,000	$28,137
Contributions Subsequent to PY Measurement Date	$61,191	$6,228
Contributions Subsequent to CY Measurement Date	$67,791	$8,843

Question #3 – Restricted Fund Balance/Net Position

- Compensated Absences:
  - FRS Pension Plan (multi-employer cost sharing defined benefit) employees (6.8% employer contribution) - 18 employees total:
    - ◊ Liability: # of hours x applicable wage rate = $663,540
  - FRS Investment Plan (defined contribution) employees (3.3% employer contribution) - 8 employees total:
    - ◊ Liability: # of hours x applicable wage rate = $214,680
- Comp Absences & Net Pension Liability:
  - Two CRA employees are in the FRS traditional pension plan; one CRA employee is in the FRS Investment plan

Question #3 – Restricted Fund Balance/Net Position

- The City also is partially self-funded for health-related benefits for its employees. The City has a Medical Self Insurance Fund that reports claim activity within this plan. At September 30, 2016, claim liability (including IBNR) was $334,615. The City is also required under an escrow agreement with the medical benefits claims processor to establish a deposit account with this TPA that maintains a balance of $200,000 that must constantly be replenished to that level.

Answer #3 – Restricted Fund Balance/Net Position

- GASBS 16, para. 11: an additional accrual should be made for salary-related payments such as the employer's share of social security and Medicare taxes and the employer's contribution to a defined contribution or cost-sharing multiple-employer defined benefit pension plan (**WAIT! That's been amended; see next slide)**
- GASB Implementation Guide Ch. Z.16.2: recognize governmental fund liability to the extent that the liability has matured (come due for payment) each period. Payments come due each period upon the occurrence of relevant events such as employee resignations and retirements

Answer #3 – Restricted Fund Balance/Net Position

- 5.255.1. Q—If an employer is required to include amounts paid for compensated absences balances in the amount of payroll on which the employer's contributions to a defined benefit pension plan is based, should the employer accrue the anticipated amounts as a liability for salary-related payments in conformity with the requirements of Statement No. 16, *Accounting for Compensated Absences*, paragraph 11?
- A—No. The employer's additional contributions to the pension plan that are expected to arise as a result of the payment of compensated absences should not be accrued as an additional liability under Statement 16. Instead, the pension benefits, if any, that are expected to arise as a result of the projected payment of the compensated absences to the employee should be included in the projection of benefit payments for purposes of Statement 68 and, therefore, would be included in the net pension liability. Payments to the pension plan that are made as a result of the compensated absence would be recognized as an increase in the pension plan's fiduciary net position in the period in which the payments are due and would, at that time, reduce the employer's net pension liability.

Answer #3 – Restricted Fund Balance/Net Position

- 7.24.5. Q—A general state statute pertaining to local government finances requires that "revenues derived from a fee or charge shall not be used for any purpose other than that for which the fee or charge was imposed." If certain fees of a local government in that state have been charged for the purpose of future infrastructure replacement, should those accumulated fees be reported as *restricted net position* in the statement of net position?
- A—Yes. The general statute applies to all jurisdictions in the state and creates a legally enforceable restriction on the use of resources raised through fees and charges. Therefore, in this example, the residual net position should be displayed in a restricted net position account.

Answer #3 – Restricted Fund Balance/Net Position

- GASBS 54 para 8: Except as provided for in paragraph 7, amounts that are restricted to specific purposes, pursuant to the definition of *restricted* in paragraph 34 of Statement 34, as amended by Statement No. 46, *Net Assets Restricted by Enabling Legislation,* should be reported as *restricted fund balance.* Fund balance should be reported as restricted when constraints placed on the use of resources are either:
  - a. Externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or
  - b. Imposed by law through constitutional provisions or enabling legislation.

Answer #3 – Restricted Fund Balance/Net Position

- Z.54.10. ***Q***—Should the amount reported in governmental funds as restricted fund balance equal the amount reported as restricted net position for governmental activities in the government-wide statement of net position?
- ***A***—There are three reasons why those amounts will generally be different. First, the principal amount of a permanent fund is classified as nonspendable fund balance in the governmental fund financial statements but is included in restricted net position in the government-wide statement of net position. Second, reconciling items that represent basis of accounting differences may cause the amounts to be different. And, finally, internal service fund net position are generally included with governmental activities.

Answer #3 – Restricted Fund Balance/Net Position

- 7.22.9. Q—A government accrues and reports a long-term liability for accretion of interest on deep-discount (capital appreciation) debt that was issued for the construction of general governmental capital assets. Which component of net position should be reduced by the liability?
- A—Accrued interest on any capital-related debt, including deep-discount debt, generally should not be included in the computation of the *net investment in capital assets* component of net position. The amount of the "borrowing attributable to the acquisition, construction, or improvement" of a capital asset is the proceeds, rather than the total amount, including interest, that will be paid at maturity. Generally, the accrued interest liability would be included in unrestricted net position. However, if the government has established a "sinking" fund to accumulate cash to pay off the debt at maturity, the accrued interest would be included in (reduce) the same component of net position as the sinking fund resources.

Answer #3 – Restricted Fund Balance/Net Position

- Restricted Fund Balance: $1,134,994
  - Capital Assets, Net: N/A
  - Bonds & Notes Payable: N/A
  - Net Pension Liability ($250,256)
  - Deferred Outflow of Resources: $118,017
  - Deferred Inflow of Resources: ($100,595)
  - Compensated Absences: ($109,140)
  - Unavailable Revenues: $165,438
  - Unspent Debt Proceeds: ($132,365)
  - Accrued Interest Payable: ($123,114)
  - Restricted Net Position – IS Fund: $200,000
- Restricted Net Position: $902,979

Answer #3 – Restricted Fund Balance/Net Position

- 7.24.8. Q—In computing the restricted component of net position, are governments required to “close” nominal accounts into that component? That is, is it necessary to account for the change in the net position balance by adding restricted revenues and deducting expenses incurred for the specified purposes?
- A—No. Statement 34, as amended, follows a change in the *total net position* approach and does not require presentation of a statement of changes in the *components* of net position, nor does it require disclosure of the changes in restricted net position. The concept of restricted net position focuses on balances rather than transactions. **Restricted net position is composed of restricted assets, reduced by reported claims against those assets. Therefore, if a government has net position at year-end that is subject to a legally enforceable restriction on its use, that net position should be reported as restricted in the statement of net position**.

Question #4 – Capital Outlay

- Lake County had the following capital-related activity in its governmental funds (capitalization threshold is $5,000):
  - Land purchase in general fund - $350,000
  - Purchase of signage in CRA fund - $75,325
  - Donated infrastructure in general fund - $673,522
  - Acquisition of street sweeper through a noncancelable lease in street improvement fund - $130,565
  - Purchase of 15 Microsoft tablets in general fund at $400 each - $6,000
  - Street resurfacing project in progress in street improvement fund - $256,852
- What is the County’s capital outlay balance in its governmental funds? What is the total amount of capital asset additions?

Question #4 – Capital Outlay

- What about the lease on the street sweeper?
  - Lessor’s implicit rate on the lease is 6%
  - Requires no down payment and five equal annual payments of $26,113
  - Street sweepers are considered to have a 7 year life
  - Title passes to the County at the end of the lease
  - The County’s incremental borrowing rate for similar financing arrangements is 4%

Answer #4 – Capital Outlay

- GASBS 68, para 213: If at its inception a lease meets one or more of the following four criteria, the lease should be classified as a capital lease by the lessee. Otherwise, it should be classified as an operating lease.
  a. The lease transfers ownership of the property to the lessee by the end of the lease term
  b. The lease contains a bargain purchase option
  c. The lease term is equal to 75 percent or more of the estimated economic life of the leased property
  d. The present value at the beginning of the lease term of the minimum lease payments, excluding that portion of the payments representing executory costs such as insurance and maintenance to be paid by the lessor, including any gain thereon, equals or exceeds 90 percent of the excess of the fair value of the leased property to the lessor at the inception of the lease

Answer #4 – Capital Outlay

- GASBS 68, para 213: A lessee should compute the present value of the minimum lease payments using its incremental borrowing rate, unless (1) it is practicable to obtain the implicit rate computed by the lessor and (2) the implicit rate computed by the lessor is less than the lessee's incremental borrowing rate. If both of those conditions are met, the lessee should use the implicit rate.

Answer #4 – Capital Outlay

- GASB 68, para 213: A lessee should compute the present value of the minimum lease payments using its incremental borrowing rate, unless (1) it is practicable to obtain the implicit rate computed by the lessor and (2) the implicit rate computed by the lessor is less than the **lessee's incremental borrowing rate.** If both of those conditions are met, the lessee should use the implicit rate.

Answer #4 – Capital Outlay

- GASBS 68, para 217: The asset recorded under a capital lease should be amortized as follows:
  - If the lease meets the criterion of either paragraph 213a or 213b, the asset should be amortized in a manner consistent with the lessee's normal depreciation policy for owned assets
  - If the lease does not meet either criterion 213a or 213b, the asset should be amortized in a manner consistent with the lessee's normal depreciation policy except that the period of amortization should be the lease term. The asset should be amortized to its expected value, if any, to the lessee at the end of the lease term.

Answer #4 – Capital Outlay

- To summarize, at the inception of a capital lease, the capital asset and lease liability recorded by the lessee are the same. A two-part computation is required:
  - The present value of minimum lease payments scheduled during the lease term is computed using the lower of the lessee's incremental borrowing rate or, if known, the implicit rate computed by the lessor.
    - The present value of minimum lease payments is compared with the fair value of the leased asset at the inception of the lease, and the lower amount is used to record the asset and liability.

Answer #4 – Capital Outlay

- 7.9.8. Q—Should a government's capitalization policy be applied only to individual assets or can it be applied to a group of assets acquired together? Consider a government that has established a capitalization threshold of $5,000 for equipment. If the government purchases 100 computers costing $1,500 each, should the computers be capitalized?
- A—Authoritative pronouncements do not address the manner in which a capitalization policy should be established and applied. Capitalization policies adopted by governments include many considerations such as finding an appropriate balance between ensuring that all significant capital assets, collectively, are capitalized and minimizing the cost of record keeping for capital assets. It may be appropriate for a government to establish a capitalization policy that would require capitalization of certain types of assets whose individual acquisition costs are less than the threshold for an individual asset. Computers, classroom furniture, and library books are assets that may not meet the capitalization policy on an individual basis, yet might be considered material collectively.

Answer #4 – Capital Outlay

Year	Annual Payment	Principal	Interest (4%)	Unpaid Balance
2015	26,113	21,463	4,650	116,250
2016	26,113	22,322	3,791	94,787
2017	26,113	23,214	2,899	72,465
2018	26,113	24,143	1,970	49,251
2019	26,113	25,109	1,004	25,108
		116,251	14,314	(1)

Year	Annual Payment	Principal	Interest (6%)	Unpaid Balance
2015	26,113	19,513	6,600	109,998
2016	26,113	20,684	5,429	90,485
2017	26,113	21,925	4,188	69,801
2018	26,113	23,240	2,873	47,876
2019	26,113	24,635	1,478	24,636
		109,997	20,568	1

Answer #4 – Capital Outlay

- Entry in general fund (or in debt service fund, if required by legal or contractual mandate):
  - DR: Expenditure – debt service principal $21,463
  - DR: Expenditure – debt service interest $4,650
  - CR: Cash $26,113
- Entry in general capital assets ledger:
  - DR: Vehicle – street sweeper $116,250
  - CR: Capital lease obligation $116,250

Answer #4 – Capital Outlay

UNIFORM
ACCOUNTING
SYSTEM MANUAL
2014 EDITION

For Florida Local Governments

Answer #4 – Capital Outlay

Object & Sub-Object Classification Introduction

The eleventh and twelfth digits of the expenditure account designate the object classification. The object code is made up of sub-object codes that may be used at the budgetary level.

Example:

Organizational Unit Department ID / Division ID

Object/ Sub-Object Code

101 – 21 32 – 521 . 31

Fund Identifier

Expenditure Account Code

101 = Special Revenue Fund

521 = Law Enforcement

31 = Operating Expenditures/Expenses – Professional Services

30 = Operations – Reported on **AFR**

All reporting entities are required to use the object codes as outlined below when reporting the AFR to the Department of Financial Services:

10	**Personnel Services** Includes Sub-Object Codes 11 - 29
30	**Operating Expenditures/Expenses** Includes Sub-Object Codes 31 - 59
60	**Capital Outlay** Includes Sub-Object Codes 61 - 68
70	**Debt Service** Includes Sub-Object Codes 71 - 73
80	**Grants and Aids** Includes Sub-Object Codes 81 - 83
90	**Other Uses** Includes Sub-Object Codes 91 - 99

Answer #4 – Capital Outlay

60 CAPITAL OUTLAY

Includes 61 through 68

Outlays for the acquisition of or addition to fixed assets.

61 LAND

Land acquisition cost, easements and right-of-way.

62 BUILDINGS

Office buildings, firehouses, garages, jails, zoos, and parks and recreational buildings.

63 INFRASTRUCTURE

Structures and facilities other than buildings such as roads, bridges, curbs, gutters, docks, wharves, fences, landscaping, lighting systems, parking areas, storm drains, athletic fields, etc.

64 MACHINERY AND EQUIPMENT

Includes motor vehicles, heavy equipment - transportation, other heavy equipment, office furniture and equipment, and other machinery and equipment. Also includes court recording, duplicating, and transcribing equipment.

65 CONSTRUCTION IN PROGRESS

Used to account for undistributed work in progress on construction projects.

Answer #4 – Capital Outlay

30 **OPERATING EXPENDITURE/EXPENSES**

Includes 31 through 59

Includes expenditures for goods and services, which primarily benefit the current period, and are not defined as Personnel services or capital outlays.

46 **REPAIR AND MAINTENANCE SERVICES**

This account code should include costs incurred for the repair and maintenance of buildings, vehicles, and equipment including all maintenance and service contracts as well as non-capital renovation. Do not include custodial or janitorial services, which are recorded under object code 34. Do not include communications maintenance (phone systems, etc.), which are recorded under object code 41.

51 **OFFICE SUPPLIES**

This object includes materials and supplies such as stationery, preprinted forms, paper, charts, and maps.

52 **OPERATING SUPPLIES**

All types of supplies consumed in the conduct of operations. This category may include food, fuel, lubricants, chemicals, laboratory supplies, household items, institutional supplies, computer software, uniforms and other clothing. Also includes recording tapes and transcript production supplies. Does not include materials and supplies unique to construction or repair of roads and bridges.

53 **ROAD MATERIALS AND SUPPLIES**

Those materials and supplies used exclusively in the repair and reconstruction of roads and bridges.

Answer #4 – Capital Outlay

- Capital outlay computation:
- Gov't Activities Capital Asset Additions = $350,000 land purchase + $75,325 signage purchase + $673,522 donated infrastructure + $116,250 street sweeper capital lease + $0 Microsoft tablets + $256,852 CIP project
- Less: Reconciling Items
  - (673,522) donated infrastructure
  - (116,250) capital lease
- Total Capital Outlay – Governmental Funds $682,177

Question #5 – Property Tax Revenues

- Orange County taxpayers may choose to pay their taxes through a quarterly Installment Payment Plan. To qualify for the plan, the taxpayer must be current on their taxes and their prior year taxes must exceed $100.00. Taxpayers must complete and return the Installment Payment Plan Application no later than May 1.

Question #5 – Property Tax Revenues

- The first and second installments are based on ¼ of the previous year's taxes. The third and four installments are ½ of the remaining actual tax liability for the current year.
  - **1st Installment** – ¼ of the total estimated taxes discounted at 6%. Payment due June 30.
  - **2nd Installment** – ¼ of the total estimated taxes discounted at 4.5%. Payment due September 30.
  - **3rd Installment** – ¼ of the total estimated taxes plus ½ of the adjustment for actual tax liability discounted at 3%. Payment due December 31st.
  - **4th Installment** – ¼ of the total estimated taxes plus ½ of the adjustment for actual tax liability. Payment due March 31st.

Question #5 – Property Tax Revenues

- Orange County Tax Collector remitted $431,250 to the City of Orlando on 11/10/16 relating to June 2016 and September 2016 installment payments.
- What if TC remitted this amount to City of Orlando in by September 30, 2016?
- Also, Orange County Tax Collector distributed excess fees to the City totaling $162,558 on 11/25/16.
- How should these transactions be accounted for?

Answer #5 – Property Tax Revenues

- **GASB 33**: Revenue Recognition - Imposed non-exchange transactions
  - Report as revenue when *resources are required to be used* or first period that use is permitted
  - Report deferred inflows of resources for resources received or reported as a receivable before such period
  - Under modified accrual basis of accounting, report deferred inflows of resources for resources that do not meet the availability criteria

Answer #5 – Property Tax Revenues

- Tax Collector commissions are expenses rather than adjustments to revenues. Excess fee distributions represent adjustments to those commission expenses.

QUESTIONS?

I hope you enjoyed another rendition of Best of Accounting Complexities for the FGFOA Nature's Coast Chapter

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