SECTION III--ACCOUNTING RECORDS

BOOKS OF FINAL ENTRY

Books of final entry are the principal accounting records from which financial and management reports are prepared. The books of final entry are composed in a manner that classifies information according to the chart of accounts. The books of original entry (journal/registers) are totaled and summarized monthly. These monthly totals are then posted to the books of final entry (ledgers) and include:

General Ledger

When transactions are recorded in the books of original entry (journals) each item of the transaction is coded with a specific account number. It would be quite cumbersome to post each of these transactions individually to a monthly or annual financial report. The purpose of the journal is to record the individual transactions, summarize each account number into a monthly total and post this total to an account. An account is a form of record used to record the summary of all coded transactions affecting that account number. For example, all cash receipts and cash disbursements affect the "Cash" account. Accounts are set up for the various assets, liabilities, equity, revenues and expenditures related to a specific fund. This group of related accounts is referred to as a "Ledger." The ledger contains the summary of the total of transactions to date that affect that particular group of accounts. Once the ledger has been totally posted and closed out its main purpose is to facilitate the completion of the year-end financial reports.

Within the general ledger there are control accounts (i.e., revenues and expenditures). These accounts contain the summary of all revenues and expenditures against that fund to date. The

detail for the revenues is kept in a subsidiary ledger known as the "Revenue Budget Record" and the expenditure detail is kept in a subsidiary ledger known as the "Expenditure Budget Record." At any point in time the control account in the general ledger must equal the total of the detail in these subsidiary ledgers.

A general ledger should be established for each fund. A sample general ledger format is shown as Illustration 10.

The subsidiary ledgers to be maintained by schools are as follows:

Revenue Budget Record

The revenue budget record is to record the summary of each revenue source recognized in the general journal or recorded in the cash receipts journal. The total of this record should equal the revenue control account in the general ledger.

A revenue budget record should be established for each budgeted fund. This record is constructed from the estimated revenue worksheets which were prepared for the provisional and annual budgets. Each worksheet will provide a basis for each fund's revenue budget record. The revenue budget record will provide a comparison of budgeted revenue with actual revenue and will provide a running total of revenues collected to date and will provide projections for future cash flow. An example of the form to be used is shown on Illustration 11.

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Expenditure Budget Record

The expenditure budget record is to record the summary of each object level expenditure classification from the budget expense journal, general journal or voucher register. The total of this record should equal the expenditure control account in the general ledger. An expenditure budget record should be established for each fund. This record is constructed by taking the departmental budget request (by activity) and providing a separate page(s) in the expenditure budget record for each activity within the fund. The expenditure budget record will serve three purposes. It will show a comparison of budgeted expenditures with actual expenditures and a running total of actual expenditures made to date. The third purpose which this record will serve will be as an appropriation control. An example of the form to be used is shown on Illustration 12.

Capital Assets

Schools have a substantial investment of tax dollars in the various lands, buildings, equipment and other assets owned by them. The responsibility of stewardship involved in safeguarding such a large investment is of the utmost importance to sound financial administration. The protective custody of these assets can only be accomplished through adequate accounting procedures and records. In addition to stewardship or protective custody of a governmental unit's property, a good system of **capital** asset accounting permits the fixation of responsibility for custody and proper use of specific **capital assets** on individual public officials.

Initially, the school board should develop and prescribe accounting policies governing **capital asset** accounting. These policies should address:

(a) the person(s) responsible for maintaining **capital asset** control records;
(b) the minimum values for classes of **capital assets** required to be accounted for; (capitalization policy)
(c) estimated useful lives;
(d) whether an accounting for public domain or "infrastructure" **capital assets** is required; e.g., roads, bridges, sidewalks and similar assets.

From a generally accepted accounting principles (AGAPE) standpoint, a **capital assets** is an asset which possesses three attributes:

1. tangible in nature
2. a life longer than the current fiscal year
3. a significant value

Capitalization Policy - A capitalization policy is a policy set by each district to establish a dollar threshold(s) for WHEN to call an item a capital asset. Different dollar amounts may be established in the policy for different classes of capital assets. For example, buildings might be capitalized as capital assets when the amount exceeds $50,000 while items that are smaller in value and more numerous, such as equipment, might be capitalized if the amount exceeds $5,000.

How high should the equipment capitalization policy be? Federal regulations have established a maximum of $5,000, so it is recommended not to exceed that level. The focus for setting your capitalization policy should be less on accountability (a deterrent to theft) and more on financial statement presentation.

Financial statement presentation is impacted by the use of depreciation to feather the cost of an asset over its useful life. A higher capitalization threshold results in more expenses being absorbed in the current year.

As a deterrent to theft, high risk assets such as computers, cameras and tools may be tracked through the use of alternative listings. These listings may be much simpler in design then a standard capital asset listing since it would be focused on description and location instead of cost, useful life or depreciation expense.

It is advisable to consult with your insurance carrier to determine the extent of documentation needed in case of a disaster. The results of this consultation will then affect the extent and detail of the capital asset records maintained. A backup copy of all inventory listings should be stored offsite.

Personal Property Listings - SDCL 5-24 requires the school's personnel to file a property inventory with the business manager around the end of each year. By law this list should include all equipment over $5,000 in original cost but may include smaller items to coincide with your capitalization policy or the needs of your insurance carrier. It is a good chance to verify or update your capital asset listings when the personal property listings are filed once a year from the various departments.

Why keep track of capital assets at all??? Following are a few of the reasons why:

> **Accountability -** Tracking capital assets is a surefire deterrent to theft. Without records, capital assets could be taken and not detected.
>
> **Grants -** Certain grant programs require the maintenance of capital asset records.
>
> **Decision Making** - When a governing board is adopting their budget they may ask for lists of similar assets to get a feel for quantity or age of an item.
>
> **Full Costing** - Are your food service rates adequate to cover the total cost of the food service operation. One of the larger expenses on an enterprise fund's operating statement is depreciation. Therefor, the first step in providing an accurate financial statement is a completed capital asset record.

The <u>general capital assets</u>, representing the assets of general government, are reported in their own separate set of self-balancing accounts. Under GASB 34, general fixed assets will be called general capital assets. Also, reference to the "general fixed asset account group" will be phased out under GASB 34, but I still encourage the maintenance of this account group on your accounting system to act as a central place to aggregate values for reporting purposes.

Capital assets of <u>enterprise</u> funds are reported within each enterprise fund. That means that each school will have an equipment account for the Food Service Fund and an equipment account for the general capital assets.

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How are values established for capital assets and secondly how do I document these values? Accounting principles indicate that capital assets should be recorded at **original cost** or an estimate thereof. Estimated costs should be recorded when it is not feasible to locate the original cost of a capital asset. Donated capital assets should be recorded using the fair market value at time of acquisition. The following comments will provide ideas in researching capital asset costs:

> **Land** - Try locating deeds in safety deposit boxes, vaults, etc... As a last resort you may go to the register of deeds office at the court house to obtain copies of deeds. Document the legal description (lot, block and subdivision) to facilitate referencing specific properties.

> **Buildings** – Try to approximate the year the building or addition was built by talking with officials or looking at the cornerstone or plaque to obtain the year the building was built. Then go to the minutes of that year to secure the bid amounts. **Maintenance** vs. **capitalizing.** Capitalize only when the useful life is extended and/or dollar amount is significant. Painting, tuckpointing, carpeting and minor repairs are all considered maintenance and do NOT increase the capital asset value.

> **Improvements Other Than Buildings** – Values should be obtained from the original vouchers or values may be estimated for work performed on athletic complexes, parking lots and sidewalks of the school district.

> **Equipment/Vehicles** - Go back several years securing the original costs of equipment and vehicles. Document these costs obtained by making copies of the purchase invoices. You may go back even further in the minutes to obtain bids of larger vehicles. Photocopy the page of the minutes to document the cost. Estimate the smaller/older items using a committee or other approach.

Researching these values is a lot of work, but if it is done right, it only needs to be done once. Document, document, document. If you find the original cost in the minutes or locate the voucher make a photocopy of it. Place these copies into a file folder or three ring binder. Provide page numbers for these copies. Then when the capital asset listing is created on the computer, a column can be established that references back to the page number of the supporting documentation.

Costs such as freight, installation, architect fees and engineering costs are referred to as ancillary costs and should be added to the capital asset values that are recorded.

Estimating Costs – Estimates of the original cost of smaller assets may be determined by researching old catalogues or consulting with individuals that have worked in that field for a number of years. Larger assets may be estimated by using a CPI (consumer price index) approach. The CPI approach is initiated by first establishing the current cost of the item. Then CPI charts are obtained to provide the "deflation" percent per year. The current cost is then deflated to arrive at the estimated original cost.

For example, the CPI tables (found on the legislative audit WEB site) have a factor of 177 for the year 2000 and 112.3 for the year 1990. So if a building currently costs $100 per square foot in 2000, then a new building built in 1990 would be estimated to cost $63.45 per square foot. ($100 divided by the current factor of 177 and that result taken times the 1990 factor of 112.3) The estimated cost per square foot as of 1990 would then be taken times the square footage of the building in question.

Documentation of the process is critical of all items that are estimated. Who was consulted? Where was the current cost obtained? What CPI deflation factors were used?

Groupings - Groups of common assets may be viewed individually or as a group. For example, if a school had 400 chairs at $20 each in an auditorium, I would probably lean towards recording them as a group because they were probably all purchased at the same time AND they will always be in that particular location. Individual chairs in various offices would not need to be grouped together and therefor probably would not be recorded. (They would be individually under the capitalization policy)

A computer workstation could include a printer, computer, keyboard, and monitor. If they are always going to be in the same grouping, a business manager could list them together as one item. If your school has many computers and swaps pieces back and forth constantly, then you may want to track individual items or consider them separately when comparing to your capitalization policy. With the recent decreases in the cost of computers, schools may no longer consider computers as a capital asset.

Depreciation - Depreciation is only required to be applied to enterprise capital assets (the Food Service Fund). Under GASB 34, the General Capital Assets will also be depreciated so it would be wise to set up those capital asset listings in a manner to allow them to be depreciated. The simple approach is suggested which is to apply depreciation using the straight line method. Suggested useful lives of various capital assets are listed in Section II, Appendix A of this School Accounting Manual. Schools may deviate from the suggested useful life if local practices support such a decision. Caution should be exercised, in that assets should not be depreciated beyond their useful life.

Pursuant to food service regulations all food service capital assets are depreciated on a straight-line basis over a 12 year useful life. This is a simple and uniform approach that is applied statewide.

Tagging of Assets – Tagging of assets to provide specific identification is optional. Most schools in South Dakota are of such a size making it hard to justify the extra work of tagging assets. Many assets such as vehicles and computers already have a serial number or other ID number available.

Library Books – GASB 34 suggests that library books are to be viewed as a capital asset. Rather than listing each and every book, all of the books may be listed as one asset. For example, 10,000 books at $23 per book equals $230,000. Then each year the total is updated for books purchased and discarded. For convenience, all books discarded are considered fully depreciated. Some GASB 34 specialists are suggesting that library books be considered individually and therefor are not expensive enough to be a capital asset. Our preference would be to list significant libraries as a capital asset to be depreciated over their useful life. Hardcover books, softcover books, CD's and audio tapes are all considered library capital assets if they have a useful life greater than a year.

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Software – Most software purchases are merely paying for the right to use someone else's product so they are not listed as capital assets. Only software developed by the entity's own programmers needs to be capitalized.

Capital Asset Listings – Older capital asset listings were on recipe cards, three ring binders and even columnar pads. Current capital asset listing could be set up on an excel spreadsheet. You may even purchase special software from vendors to create capital asset listings.

The column headings of a capital asset record should at a minimum include the following:

ITEM # - This column would serve as a reference from the capital asset record to the support for the value of each item listed. It could also be used to list the tag numbers if tagging is used.

G/L ACCOUNT NUMBER – This column would identify the general ledger account number for each item. For example, 201 land or 204 equipment. It will be necessary to sort this column for financial statement reporting.

FUNCTION – This column will enable a school to sort by function. GASB 34 requires that depreciation expense be reported at the functional level. For example, total depreciation expense for "instruction" or "support services". The data entered into this column may be in words "Instruction – H.S. lab" or it may be by expenditure account number "1130".

YEAR ACQUIRED – This information is essential for calculating depreciation.

ESTIMATE USEFUL LIFE – These estimates may be obtained from the useful life tables on the legislative audit WEB site or it may be obtained from other sources.

DESCRIPTION – A good description coupled with the function column may save having a column for location. Also, it is optional whether to list the serial number here or in a separate column. The words "fed" or "local" may be added to this column for food service equipment to indicate the source of funding.

COST – This should include the original cost or an estimate thereof.

ACCUMULATED DEPRECIATION – This column should reflect the depreciation accumulated from the date of purchase through the current date. The amounts in this column should support the general ledger accounts of the same name.

DEPRECIATION EXPENSE 2001 – It is recommended to calculate the depreciation expense for each item listed using the straight-line method of depreciation. The totals listed for this column should tie to the amounts reported on the operating statement. Do not depreciate an item beyond its useful life. For the sake of keeping it simple, you may have a policy of depreciating an item for a full year in the year acquired even if an item is acquired several months after the year has started.

NOTE: Proclaiming a salvage value is optional and therefore is not listed as a required element above.

A sample capital asset record and depreciation schedule is shown on Illustration No. 13.

Leases – Sometimes schools will enter into leases or lease-purchases for capital assets. Leasing is the same as renting in that the school is paying for the right to use the asset but will never own the asset. Lease-purchasing on the other hand is just a mechanism to make installment payments towards the eventual ownership of the asset.

In both leasing and lease-purchasing, an analysis must be made to determine if the contract is a <u>capital lease</u> or an <u>operating lease</u>. The contract is a capital lease if ANY one of the following conditions are met:

a. The lease transfers ownership of the property to the school by the end of the lease term. (a lease-purchase)

b. The lease contains a bargain purchase option. An option to buy the item for less than its current market value.

c. The lease term is equal to 75% or more of the estimated economic life of the leased property.

d. The sum of the principal lease payments equal 90% of the fair value of the asset. (Are your lease payments, when added together, about the same as buying the item)

If it is determined that a capital lease exists, then that item should be added to your capital asset listings. (long-term debt should also be recognized)

Works of Art and Historical Treasures – Except as discussed in this paragraph, governments should capitalize works of art, historical treasures, and similar assets at their historical cost of fair value at date of donation (estimated if necessary) whether they are held as individual items or in a collection. Governments are NOT required to capitalize a collection whether donated or purchased that meets ALL of the following conditions. The collection is:

a. Held for public exhibition, education, or research in furtherance of public service, rather than financial gain

b. Protected, kept unencumbered, cared for, and preserved

c. Subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections.

Capitalized collections or individual items that are exhaustible, such as exhibits whose useful lives are diminished by display or educational or research applications, should be depreciated over their estimated useful lives. Depreciation is not required for collections or individual items that are inexhaustible.

Inexhaustible works of art and historical treasures, if capitalized, should be reported as “Land and land rights” whereby most exhaustible treasures (ones that will be depreciated) should be recorded as “machinery and equipment”.