

Principles of Accounting II

Activity Fund Accounting For Local School Personnel

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PREFACE

The following materials have been designed for individuals who are employed by a local school education agency in an accounting, bookkeeping, or compliance checking task as part of the local school's accounting procedures management. It is intended for those individuals who are responsible for the initiation of economic transactions into the accounting system.

Course Overview

The participant will be introduced to basic accounting concepts and terminology for a fund accounting system including double-entry bookkeeping procedures; internal controls and procedures found within the local school environment; journalizing and recording activity fund economic events at the local school level; and basic financial statement reporting for local education agency under current GASB standards.

Classroom Activities

Classroom activities will include lectures, bookkeeping and accounting examples, and class exercises.

Course/Seminar Materials

Why does the course manual for such a short course contain so much printed material? Part of the answer is contained in the question. This is a short course. Accordingly, effective utilization of time is critical. Time is not used effectively if the student is struggling to take notes, copy detail from power point slides or perform clerical tasks not essential to the learning process. Furthermore, subsequent review is frequently hampered or even made impossible, if the student must first organize and interpret sketchy notes. The course manual was designed to ease some of these problems by providing a systematic record of the material covered for your post-course references.

Seminar Evaluation

An evaluation of materials and classroom instruction will be requested at the end of this seminar. Your frank and honest evaluation will help in the future development and presentation of this or similar seminars.

CHAPTER 1

REVIEW OF THE ACCOUNTING CYCLE

Review of the Accounting Cycle

Accounting can be considered a communication system because it provides the mechanism to send messages to interested parties.

The accounting function includes:

- **recording** the results of economic transactions,
- **classifying** those transactions, and
- **presenting the information in reports** that will allow investors and creditors, both current and prospective, to evaluate the entity for purposes of making economic resource allocation decisions.

The objective of any accounting system is to identify events that directly affect the financial position of the governmental entity and capture the effect of these events by recording those events. The accounting equation guides the process used in recording the effect of these economic transactions.

$$\text{Assets} = \text{Liabilities} + \text{Equity}$$

This model serves as the basis for the double entry system of bookkeeping. As financial transactions occur, the elements within the balance sheet model will change but the equality of the equation (left side = right side) will be maintained. There will be several types of transactions that will increase and decrease the assets and liabilities of the entity. Likewise, there will be several types of transactions that will change the residual interest in the entity (equity).

THE BALANCE SHEET

Assets
Liabilities
Equity

A Balance Sheet (or Statement of Net Position as it is known in the government financial management environment) is a **statement of financial condition**. It is a financial picture of the fund or the organization **at one point in time**. The balance sheet reports the organization's assets, liabilities, and equity (GASB Concept Statement #4). The elements of the balance sheet (like one shown below)¹ are:

Assets - are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events. Assets can be classified as Current Assets, Investments, Property Plant and Equipment, and Intangibles.

Liabilities - are probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events. Liabilities can be classified as Current or Long-Term.

Net Position - is the residual interest in the assets of an entity that remains after deducting its liabilities. Contributed Equity is the amount of net assets contributed to the organization from the start of the organization to the current date. Retained Earnings (or Net Position as it is known in the government financial management environment) is the amount of net assets accumulated and kept from operating activities from the start of the organization to the current date.

CLASSY COMPANY Balance Sheet December 31, 20X3					
Assets			Liabilities		
Current assets			Current liabilities		
Cash	\$100,000		Accounts payable	\$ 80,000	
Short-term investments	50,000		Salaries payable	10,000	
Accounts receivable	75,000		Interest payable	15,000	
Inventories	200,000		Taxes payable	5,000	
Prepaid insurance	<u>25,000</u>	\$450,000	Current portion of note	<u>40,000</u>	\$150,000
Long-term investments			Long-term liabilities		
Stock investments	\$ 40,000		Notes payable	\$110,000	
Cash value of insurance	<u>10,000</u>	50,000	Bank Loan	35,000	
Property, plant & equip.			Mortgage obligation	75,000	
Land	\$ 25,000		Deferred income taxes	<u>80,000</u>	<u>300,000</u>
Buildings and equipment	\$150,000		Total liabilities		\$450,000
Less: Accum. depreciation	<u>(50,000)</u>	<u>100,000</u>			
		125,000	Stockholders' equity		
Intangible assets			Capital stock	\$300,000	
Goodwill		275,000	Retained earnings	<u>160,000</u>	
Other assets			Total stockholders' equity		<u>460,000</u>
Receivable from employee		<u>10,000</u>	Total liabilities and equity		<u>\$910,000</u>
Total assets		<u>\$910,000</u>			

¹ Retrieved from www.principlesofaccounting.com

THE OPERATING STATEMENT

Revenues
Expenses
Gains
Losses

The operating statement for a period of time is called the Income Statement in the for-profit environment (or Statement of Activities as it is known in the government financial management environment). The financial statement elements to be reported in the operating statement, like one shown below², are defined (SFAC #3 and SGAS #1) as:

Revenues - are inflows or other enhancements of assets of an entity or settlements of its liabilities (or a combination of both) during a period from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations. In recent for-profit standards, the concept of recognizing revenue is when the entity satisfies a performance obligation – a promise to transfer goods or services.

Expenses- are outflows or other using up of assets or incurrence of liabilities (or a combination of both) during a period from delivering or producing goods, rendering services, or carrying out other activities that constitute the entity's ongoing major or central operations.

Gains - are increases in equity (net position) from peripheral or incidental transactions of an entity and from all other transactions and other events and circumstances affecting the entity during a period except those that result from revenues or investments by owners.

Losses - are decreases in equity (net position) from peripheral or incidental transactions of an entity and from all other transactions and other events and circumstances affecting the entity during a period except those that result from expenses or distributions to owners.

QUARTZ CORPORATION		
Income Statement		
For the Year Ending December 31, 20X9		
Revenues		
Services to customers	\$750,000	
Interest revenue	<u>15,000</u>	
Total revenues		\$765,000
Expenses		
Salaries	\$235,000	
Rent	115,000	
Other operating expenses	<u>300,000</u>	
Total expenses		<u>650,000</u>
Net income		<u>\$115,000</u>

² Retrieved from www.principlesofaccounting.com

During the fiscal year, there are clearly definite procedures that are followed to ensure the operation of the accounting system. These procedures, in sequential order are:

THE ACCOUNTING CYCLE

1. Analyze the financial transactions (economic events).
2. Enter the transaction into the accounting system (journal entries posted to the ledger accounts).
3. Prepare a trial balance.
4. Prepare and enter (journalize and post) adjusting entries into the accounting system.
5. Prepare adjusted trial balance.
6. Prepare basic financial statements.
7. Journalize and post year end closing entries.
8. Prepare post-closing trial balance.

The events, processes or conditions which bring about changes +/- to an asset, liability, equity, revenue, expenditure or expense item is called a **financial transaction**. This "transaction" must be recorded by the accounting entity or fund. This is done through recording the transaction in a journal (paper) or software program (computer). After recording, the information is transferred to the individual accounts in a process referred to as posting. Both the journal and the accounts are cross referenced to assist tracing the information when needed. The cumulative result of these transactions is then used to prepare the trial balances and financial statements.

The normal balances and changes to the accounts are derived from the accounting equation: $\text{Assets} = \text{Liabilities} + \text{Equity}$. Remember, the accounting equation is an algebraic model. As the financial transactions occur, the changes are recorded in the accounts in a manner that will maintain the equality of the equation. Therefore, for every financial transaction, two or more accounts will be affected so that the total right changes (debits) will equal the total left changes (credits). The complete account structure can be illustrated using “T” accounts:

Assets		=	Liabilities		+	Equities			
Debit	Credit		Debit	Credit		Debit		Credit	
+	-		-	+		-		+	
						Expenses		Revenues	
						Debit	Credit	Debit	Credit
						+	-	-	+
						Losses		Gains	
						Debit	Credit	Debit	Credit
						+	-	-	+

After all financial transactions have been entered into the accounting system, a trial balance is prepared. The trial balance is a list of all the accounts in the ledger and their current balance. The trial balance column totals are checked for equality. After all transactions have been analyzed, journalized, and posted to the appropriate ledger accounts, some account balances will require adjustments in order to report all account balances according to GAAP. These adjustments can be classified as an accrued revenue, accrued expense, prepaid revenue, prepaid expense, and/or valuation adjustment.

Accrued Revenue - revenue that has been earned but not recorded. An example would be goods or services provided to students at the end of the period, but no payment has been received and no transaction has been recorded.

Accrued Expense - expense that has been incurred but not yet recorded. An example would be two days wages earned by employees since the last pay period that will be paid in the next fiscal year. The salary expense for the current year must be recorded and a payable set up to pay the employee on the next pay period.

Prepaid Revenue - is revenue that has not yet been earned but has already been collected and recorded. Unearned revenue is a liability for the organization that will

perform services or deliver products in the future. An example would be student tickets sold and recorded as revenue for an event to occur at the end of the semester.

Prepaid Expense - is an expense that has been paid for but has not been used. The organization making the payment should recognize an asset for the services or goods it will receive. The adjusting entry will allocate the amount used to expense and the amount of benefits still available to asset. An example would be annual insurance premiums paid and recorded as an asset that should be allocated each month to expense as the risk coverage expires.

Valuation Adjustments - adjustments are changes made to the carrying values of assets and liabilities that impact the operating statement. There are certain types of assets that are necessary for the organization to carry out its purpose, rendering services or selling products. Land, buildings, equipment, machinery, or vehicles are examples of long-lived assets used in operations. Except for land, these assets have limited useful lives and service benefits. As those service benefits are consumed, the unrecoverable cost of the asset is allocated to expense.

After all adjusting entries have been made, another trial balance is prepared. The adjusted trial balance is used to once again check the equality of the debits and credits and the normalcy of the account balances. Then, either the financial statements will be prepared, or the closing entries will be prepared. The order of these last two steps of the accounting cycle will depend on the most immediate need of management.

Exercise 1.1 - For review, complete both the Income Statement and Balance Sheet financial statements on the next two pages from the Trial Balance below for Sally's School Supplies, a for-profit entity, as of December 31, 2020.

Sally's School Supplies		
Trial Balance		
12/31/2020		
	Dr.	Cr.
Cash	\$35,575	
Supplies Inventory	24,500	
Prepaid Rent for Copier	150	
Prepaid Insurance	480	
Equipment	18,000	
Building	110,000	
Accounts Payable		\$16,090
Notes Payable		2,000
Contributed Equity		150,000
Retained Earnings		
Sales Revenue		52,565
Rent Expense	500	
Cost of Goods Sold	28,200	
Utilities Expense	1,625	
Insurance Expense	300	
Supplies Expense	<u>1,325</u>	<u> </u>
Totals	<u>\$220,655</u>	<u>\$220,655</u>

**Sally's School Supplies
Income Statement**

At the end of the fiscal year, the balances in the temporary retained earnings accounts are transferred to the permanent retained earnings account. This process is called "closing the books." Closing is necessary so that the operating results and other changes to equity for the current year do not get commingled with operating results of the subsequent year. To close an account means to bring the balance to zero.

Example of Closing Entry:	<u>dr.</u>	<u>cr.</u>
Revenues	XXX	
Retained Earnings		XXX*
Expenses		XXX

*The amount credited to Retained Earnings would be equal to the net income figure shown on the Income Statement. If an entity incurred a loss, then a debit to Retained Earnings would be shown in that amount. After all temporary accounts have been closed (brought to a zero balance), a final trial balance is prepared. This post closing trial balance (example shown below) is a final check to see if

- The ledger is in balance (debits = credits)
- The accounts are carrying normal balance, and
- No temporary accounts have been left open (carrying a balance forward)

Sally's School Supplies		
Post-Closing Trial Balance		
12/31/2020		
Cash	\$35,575	
Supplies Inventory	24,500	
Prepaid Rent for Copier	150	
Prepaid Insurance	480	
Equipment	18,000	
Building	110,000	
Accounts Payable		\$16,090
Notes Payable		2,000
Contributed Equity		150,000
Retained Earnings	<u>0</u>	<u>20,615</u>
Totals	<u>\$188,705</u>	<u>\$188,705</u>



CHAPTER 2

FUND ACCOUNTING

THE FUND ACCOUNTING SYSTEM

The accounting system in government is known as a fund accounting system. GASB Statement No. 1 as modified by GASB Statement No. 34 provides the foundation for a fund accounting system. Within this statement, the GASB explains the nature and characteristics of fund accounting through the 13 governmental accounting and financial reporting (**GAFR**) principles followed by state and local governments.

The principles require generally accepted accounting principles (GAAP) be followed for governmental financial reporting as well as defined the prescribed unique governmental accounting system known as fund accounting. The principles also establish the basis of accounting for the different fund types; the formal recognition and use of budgetary accounting; and define the minimum contents of annual financial reports.

Adherence to GAAP for financial reporting is extremely important to state and local governments. An accounting system is used to record, classify, and summarize all the economic events that affect the reporting entity. As stated earlier in the review of the accounting cycle, this system is based on an algebraic model that reports the entity's assets, liabilities, and net position.

ACCOUNTING EQUATION

$$\text{Assets} = \text{Equities}$$

BUSINESS MODEL

$$\text{Assets} = \text{Liabilities} + \text{Owners' Equity}$$

GOVERNMENT MODEL

$$\text{Assets} = \text{Liabilities} + \text{Fund Equity}$$

FUNDS

In the governmental environment, there is no business concept of ownership. Therefore, the net position is called fund equity, the residual balance of assets over liabilities. Accountability for the net position in government is maintained by purpose of activity in separate "funds". The government model, $\text{Assets} = \text{Liabilities} + \text{Fund Equity}$, applies to the individual fund. Because there are many specific activities within a government unit, there could be many separate funds within a single government unit.

A fiscal entity is an accounting entity in which operating activities are recorded such as revenues and expenses or expenditures. Each fund carries on specific activities to attain certain objectives in accordance with the law, special regulations, restrictions, and limitations. An accounting entity is nothing more than a self-balancing set of accounts. This concept of a fund accounting system is really the essence of governmental accounting. It is one of two techniques that are used to control the use of economic resources and provide accountability for taxpayers and other resource providers, such as other governments and private foundations.

There are three types of funds in a governmental fund accounting system: governmental types, proprietary types, and fiduciary types. Each of the governmental, proprietary, and fiduciary fund types is further sub classified by purpose of activity.

Governmental Funds

Governmental type funds are expendable funds through which most government operations or activities take place. These funds account for the resources used for normal governmental operating activities and which are consumed/spent during the fiscal year. There are five subtypes of governmental funds: the general fund, the special revenue funds, the capital project funds, the debt service funds, and the permanent funds.

The **General Fund** is the primary operating fund of any government. Most government day-to-day activities are accounted for in the general fund. Some examples of the general fund activities for a local school at the system level include teacher/support salaries and benefits, utilities, and other operations and maintenance items incurred for the schools and administrative activities for the local education agency. Every government has one General Fund.

Special Revenue Funds account for proceeds of specific revenue sources that are restricted or otherwise limited to spending for specified purposes other than debt service or capital projects. Examples of special revenues are property taxes levied for education and gasoline tax earmarked for highway maintenance.

Capital Project Funds account for financial resources restricted or otherwise limited to spending for capital outlays (known as general capital assets), including facilities and other capital assets such as equipment and buses.

Debt Service Funds account for financial resources restricted or otherwise limited to spending for principal and interest on long-term debt when due.

Permanent Funds account for legally restricted resources so that only earnings from the resources (and not the principal itself) may be used to support the governmental programs. An example of a permanent fund is a scholarship trust that all 12th grade students in the district may apply for at the end of their senior year. The income from the investment funds the scholarship each academic year. The principal is not spent but retained for growth of the fund.

Proprietary Type Funds

Proprietary type funds are nonexpendable, self-sustaining funds which account for ongoing activities like governmental operation of its print shop, motor pool, hospital, golf course, or other such activity found in the private sector. There are two subtypes of proprietary funds: enterprise funds and internal service funds. The major difference between enterprise and internal service funds is the type of customer or client. Internal service funds provide services within the government unit and, on occasion, to other government units. Enterprise funds sell services primarily to the general public. Enterprise funds can also sell services to their government or to other governments.

Fiduciary Type Funds

Fiduciary type funds are those funds which account for the assets held by a governmental unit in a trustee or custodial capacity for other funds in the government, other governments or organizations, or private individuals. There are four subtypes of fiduciary funds: investment trust funds, private purpose trust funds, pension trust funds, and custodial funds.³

An investment trust fund accounts for assets, liabilities, and net position that are to be maintained and managed for purposes of fulfilling the intent of the trust agreement. A private purpose trust fund accounts for assets, liabilities, and net position that are to be maintained and managed for purposes of fulfilling the intent of the trust agreement per donor intent. Unlike the public purpose trust funds (permanent funds), the beneficiaries of private purpose trust funds are private individuals, organizations, or other governments. A pension trust fund accounts for the pension plan of government workers. Finally, the custodial fund is only an accounting entity created to account for the assets collected that belong to other funds, governments or unrelated parties. (Example: tax collection fund in which the tax billed is collected by one government, in custodial fund, but belongs to several local governments.)

³ GASB 84 – Fiduciary Activities – was issued in January 2017.

STUDENT ACTIVITY FUNDS

Activity funds are established to direct and account for monies used to support co-curricular and extra-curricular student activities. As a rule, co-curricular activities are any kinds of school-related activities outside the regular classroom that directly add value to the formal or stated curriculum. Co-curricular activities involve a wide range of student clubs and organizations. Extra-curricular activities encompass a wide variety of other district-directed activities, typified by organized sports and other non-academic interscholastic competitions. It is important to note that individual states may have their own classifications for cocurricular and extracurricular activities.

STUDENT ACTIVITY FUNDS

- **Co-Curricular** activities are any kinds of school-related activities outside the regular classroom that directly add value to the formal or stated curriculum.
- **Extra-Curricular** activities encompass a wide variety of other district-directed activities.

The nature of activity funds makes them especially vulnerable to error, misuse, and fraud. In addition, activity funds often total to large sums of money, especially when capturing the amounts that flow through an educational organization in the form of school board funds, student-generated funds, receipts, and disbursements related to athletics, and the co-curricular and extracurricular events sponsored by school districts today.⁴

Activity funds are unique to school districts. The distinction is based on the purpose of the funds, that is, the programs supported by the funds. The classifications which are commonly recognized are:

- **District activity funds**
- **Student activity funds**
- **Parent support or school related organization funds**

District activity funds are those funds that belong to the district which are used to support its co-curricular and extra-curricular activities and are administered by the school district. Disbursement of this type of funds rests only with the school board

⁴ Taken from Allison, G.S. (2015). Financial Accounting for Local and State School Systems: 2014 Edition (NCES 2015-347). U.S. Department of Education, National Center for Education Statistics. Washington, DC: U.S. Government Printing Office.

(designee). In other words, the local education agency determines how district activity fund monies are spent and the district programs that receive support.

Student activity funds are those funds that support activities that are based in student organizations. Students not only participate in the activities of the organization, but also are involved in managing and directing the organization's activities. An important distinction is that disbursing monies from the student activity fund may be subject to approval by the student organization and its sponsor, rather than by the board of education or principal.

Parent Support or School Related Organizations Funds- School districts and student groups are also increasingly benefited by affiliated organizations that support curricular, co-curricular, and extracurricular activities. Affiliated organizations include groups such as Parent-Teacher Associations (PTAs), Parent-Teacher Organizations (PTOs), school foundations, and athletic booster clubs. Contributions by these groups often include supplies, materials, equipment, and even school facilities, such as weight training rooms. Financial records may be included in the school books and classified as non-public funds or may be maintained outside the school records depending on the board's policy. Additional procedures **should** be in place for those records maintained outside the school financial reporting system.

Public and Non-Public Funds

In the State of Alabama, the funds maintained at the local schools can generally be divided into two major categories: public and non-public. Public Funds are referred to as Fund 12 and Non-Public Funds are referred to as Fund 32. Various factors must be considered in determining the proper classification, which affects the degree of expenditure restriction.⁵

Public Funds

Funds are generally classified as public funds when the **following criteria are met:**

- Money generated school-wide
- Money that can be used for all students
- Money controlled by the Principal or any school employee

⁵ Taken from Alabama State Department of Education (<https://docs.alsde.edu>). Financial Procedures for Local Schools. June 2010. pp. 1- 28.

These funds are restricted to the **same legal requirements** as the Local Education Agency (Board of Education) funds. Examples include:

- **General** – may consist of vending machine commissions, proceeds from school fundraisers (school pictures, coupon books, etc.), student parking, appropriations from the Board, interest income, and other miscellaneous revenues. Its primary purpose is to pay for the general operations of the school and is totally controlled by the Principal.
- **Library** – accounts for late charges on returned library books, funds collected for lost library books, and expenditures incurred for purchasing library books.
- **Athletic** – may consist of income from gate receipts, parking at athletic events, advertising commissions, game program sales, and donations from athletic booster clubs. Separate accounts may be established for individual sports, if desired. Expenditures include athletic uniforms, equipment, and supplies; membership dues to athletic organizations; registration fees for coaching clinics; travel and transportation; game officials, and, expenditures related to athletic events, including expenses for practicing and preparing for athletic competitions and exhibitions.
- **Concession and Student Vending** – may consist of concessions operated by the school at athletic events and vending machines or concessions for students operated at the school during the school day.
- **Fees** – school-imposed course fees for certain non-required academic courses, field trips, workbooks, and supplemental instructional materials. These funds are used to cover the costs associated with the course or purpose for which the funds are collected.
- **Locker Fees** – funds collected from students that are used to cover the costs associated with maintaining the student lockers.
- **Faculty Vending** – consists of funds collected and used for items sold in faculty lounge areas that, although not assessable to students or the public, are totally controlled by the Principal.
- **Donations** - Donations that are given for use by the entire school are considered public funds.

Allowable expenditures from public funds include:

- Professional development training.
- Refreshments expended for an open house at a school where the public would attend.
- Pregame meals for student athletes and coaches.
- Academic incentives for students.
- Athletic and band uniforms for students to participate in school activities.
- Memberships in professional organizations.
- School landscaping, maintenance, furnishings, and decorations.

Note: Funds received from public (tax) sources or used for public purposes are public funds subject to the control of the school principal.

Non-Public Funds

These funds are restricted for expenditures subject to the **intent and authorization of the organization's sponsors and officers and not used for general operations of the school**. The principal does not direct the use of these funds but **does have the authority to prohibit inappropriate expenditures**.

Funds are generally classified as non-public funds when the **following criteria** are met:

- Money generated for a particular group.
- Money used for a particular group.
- Money controlled by the students and/or a parental organization.

Examples of Non-Public Funds include:

- **Clubs and Classes** – Student organizations may have self-imposed fees but not academic course fees. The participants often impose their own fees for participation in these clubs and classes. These student organizations often conduct fund raising events. Clubs and classes include FBLA, Senior Class, Student Government, Spanish Club, Cheerleaders, Band, Show Choir, Beta Club, National Honor Society, Key Club, etc. Student organizations are self-governed by officers elected by the participants.
- **Courtesy or Flower Fund** - Money collected from faculty/staff to purchase flowers or gifts in instances such as births of co-worker's children, death of faculty or staff family member, hospitalization of faculty or staff member and so forth.

-
- **Athletic Fundraisers** - Fundraisers conducted by booster clubs usually for specific activities.
 - **Other School Related Organizations** – Parent or parent/teacher organizations can have the organization’s funds in the school accounts. These organizations are governed by officers elected by its members. PTO, PTA, Band Boosters, and various athletic booster support groups are considered school related organizations.

Some of the expenditures that are **not allowable purchases from public funds but may be allowable expenditures from non-public funds include:**⁶

- Food for social gatherings.
- Class prom entertainment.
- T-shirts for club members or faculty.
- Donations to various organizations.
- Transfers to other non-public accounts.
- Travel expenses to club events.
- Championship rings.
- Faculty appreciation gifts.
- Scholarships.
- Flowers for funerals.

NOTE: Non-public funds can become subject to the same expenditure restrictions as public funds if the accounting records do not maintain a separate account for each of the non-public funds.

⁶ State of Alabama Ethics Law (Act 2012-433) limits purchases for school employees and their families.

When Funds are BOTH Public and Non-Public Funds

Some funds may be set up as **both public and non-public funds**. This means the school system may have a Fund 12 for Donations and a Fund 32 for Donations. The determining factor in such situations is dependent upon **whom or what entity has control** over how the money is spent.

Common examples may be found in the following economic events:

- **Donations** – A letter from the donor should always be requested stating how the donation may be classified for accountability purposes.
- **Fundraisers** – It depends on which group is controlling the fundraiser – if a fundraiser is controlled by the teachers, staff, and principal of the school, proceeds should be considered public funds. If a fundraiser is controlled by the club, organization, or club, this may be considered non-public funds.
- **Athletics** – Gate receipts are always considered public funds. However, outside fundraising activities controlled by officers of the booster club may be considered non-public. Documentation of club meetings along with public-posted minutes should be kept so that organization decisions can guide the decision on whether funds were intended for public or non-public usage.

Important Points on Public and Non-Public Funds Transferability

- Public funds **cannot** be transferred to non-public accounts. If funds are transferred from public to a non-public account, then funds are considered commingled and the non-public account becomes a public account.
- Non-public funds **can be** transferred to a public account. However, once transferred, they become public funds incurring all the legal restrictions of a public fund under state law.

Summary of Activity Funds

In summary of activity funds, it is important to remember that the cornerstone of government accounting is accountability and transparency in financial resources and operations. Best practice dictates the creation of **strong controls** surrounding activity funds, including assurance that all transactions are recorded and reported in district financial records. Additionally, at a minimum, proper lines of authority combined with strong control practices, such as segregation of duties, multiple checks and balances, requirements for annual audits, and regular financial reporting, are the elements to protect against error and abuse. The next chapter will discuss common internal controls found within the local school financial management system.

EXERCISE 2.1

Identify whether the following transaction should be in a Fund 12(A) or Fund 32(B) or may be BOTH (C) in accordance with our discussion from this chapter.

- A. **Public Funds – Fund 12**
- B. **Non-Public Funds – Fund 32**
- C. **May be possible to have both Fund 12 and Fund 32 accounts**

- _____ 1. Donations for the school computer lab, theatre, and library.
- _____ 2. Donations from Sports Authority to the Athletic Department. Letter stated that the funds should be used to fund the soccer team trip to Brazil this summer as well as build a soccer field that may be used for both the soccer team as well as PE classes. Letter gave a break-out of how funds were intended to be used.
- _____ 3. Locker and parking fees were collected for the entire year from students.
- _____ 4. Concessions operated by the band booster club at athletic events.
- _____ 5. Candy fundraiser revenues received by Sue Sylvester for cheerleading squad candy sale.
- _____ 6. Money collected by principal for flowers to celebrate birth of baby triplets born to Mr. Schuester's wife.
- _____ 7. Donation by Walmart to the Glee Club to hire a music and dance coach.
- _____ 8. Parking for athletic event at school stadium.
- _____ 9. Concessions during 5K Color Run Fest for Band Boosters held on County Road 40.
- _____ 10. Sponsor signage at school baseball field.

CHAPTER 3

INTERNAL CONTROLS FOR A LOCAL SCHOOL

INTERNAL CONTROLS FOR A LOCAL SCHOOL SYSTEM

Internal controls are methods put into place to safeguard assets; ensure the accuracy and reliability of accounting data; promote operational efficiency; and encourage adherence to prescribed managerial policies found within the school district as well as within the school. The greatest protection of funds within the school system comes from effective internal control. Effective internal control comes from the presence of effective supervision, which will provide the necessary reasonable assurance that the conditions of control are adequate. Internal controls may be set by the local education agency or the school management, the Principal. Whichever method is utilized, the Principal is responsible for assuring compliance by all employees within the school as well as creating a control environment that ensures public trust and accountability.

A well-planned internal control system provides a local education agency and/or school with procedures that produce accurate and reliable financial statements as well as safeguards assets, financial resources, and the integrity of the staff entrusted with the responsibility of handling assets for the school system. From an effective internal control system, operational efficiencies will arise along with public confidence that sound financial management practices are being followed and monitored within the system.

In order to create an effective internal control environment, certain procedures must be developed at the system level to prevent errors from occurring. One of these controls is the **bookkeeping function itself**. In Chapter 1 we discussed the various accounting terms commonly used in accounting such as Assets, Revenues, and Expenses (Expenditures). Bookkeepers deal with these terms in their positions every day. Bookkeepers also analyze economic events, commonly called transactions, which affect the assets, liabilities and net position of a fund. The effects of these events must be recorded as changes in the accounting equation within the proper accounts by using debits and credits within the financial management software system commonly found in the local school systems.

The analysis of transactions normally involves answering these four questions:

1. What type of account(s) were affected – asset, liability, fund equity, revenue, expenditure?
2. What specific accounts were affected – cash, accounts payable, unreserved fund balance?
3. What is the change in the account balances – increase or decrease?
4. Does the increase or decrease in the account balance require a debit or credit entry?

Through this analysis, financial management personnel within the school utilize double-entry bookkeeping (debits and credits of accounts) to ensure that each economic event is entered into the proper accounts.

Another control is the **chart of accounts** found within the local education agency. The chart of accounts indicates the nature of the assets, liabilities, and fund equity accounts, the sources of revenue and reasons for expenditures. The uses of budgetary accounts are also both effective and efficient tools of management control ensuring that appropriations of public funds are maintained and followed.

Use and establishment of internal control procedures are basically the checks and balance system to safeguard the interest of stakeholders (students, parents, employees, taxpayers, etc.) as well as the financial integrity of the local education agency. Internal controls are important to the effective operation of the school board – the following few pages will summarize some **common internal controls** found within a local school.

Cash Receipts

There is no financial need greater than that of adequate internal control for cash receipts and disbursements. Cash receipts include all monies coming into the school. Internal controls for activity fund accounting within a school rely on a system of checks and balances between three participating members of the revenue collection process: the fund provider (student, club sponsor, teacher, etc.), the school bookkeeper, and the principal. According to the State Department of Education, audits show that the management of incoming funds in local schools as the primary weakness of internal controls for local school financial operations.⁷ Because a number of different people are often involved in the collection of school funds, establishing enforceable procedures for the variety of income sources becomes an integral part of the accountability for local school funds. Master receipts, reports of ticket sales, teacher receipts, and alternative receipt listings are all important documentation for assuring that all funds collected for the school are deposited in the school's account.

Cash is the **most liquid asset** and the **most vulnerable asset** within any accounting system. There are **several general policies** that **must be followed** when dealing with cash receipts:

- All employees responsible for handling and recording activity fund monies should be bonded by the district.

⁷ <https://docs.alsde.edu/documents/68/LocalSchoolFinancialProcedures.pdf>

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- A system for receipting cash should be adopted that includes using pre-numbered receipt forms for recording cash and other negotiable instruments received.
 - All receipts should be deposited intact. That is, all receipts should be deposited in the form in which they are collected and **should not be used** for making change or disbursements of any kind.
 - All receipts should be deposited daily. Un-deposited receipts should be well secured.
 - When monies are received, a cash receipt should be prepared, and the original is to be given to the person making the payment; the Cash Receipt Journal is to be kept on file in the school office. The person receipting the money must **never** write a receipt to his/herself.
 - One deposit slip should be prepared in duplicate, listing each check separately, by recording the issuer of the check and the amount. Both should accompany the deposit to the bank to be validated by the bank teller.
 - The bookkeeper should check the accuracy of the bank's validation **before** leaving the bank. The duplicate deposit slip should be returned to the school and used to verify the entry made in the Cash Receipt Journal.
 - Daily receipts should be totaled and should match the total of the deposit slip.
 - All money is to be deposited in a bank to the credit of one account.

It is important to note, again, that cash is the most vulnerable asset within any organization and internal controls must be established to safeguard this asset. Regardless of the method of verifying cash receipts, **if cash collected is used temporarily or permanently without first being deposited following the proper internal control policies and procedures, the purpose of the internal control system and the effectiveness of its operation are destroyed.**

Internal Control Procedures of Cash Receipts for Local Schools⁸

Master Receipts

These receipts are issued in the school office by an individual assigned by the Principal or designated by job description as responsible for collecting school funds. This is normally the School Bookkeeper. **The Master Receipt must be a pre-numbered duplicate receipt book or record.** Master Receipts should be completed and issued in numerical order at the time funds are received. Because only one Master Receipt book or record is to be in use at a time, all pre-numbered receipts in a receipt book or record should be issued before another Master Receipt book or record is put into use. Master Receipts cannot be pre-signed and must contain an original signature of the person receiving the funds.

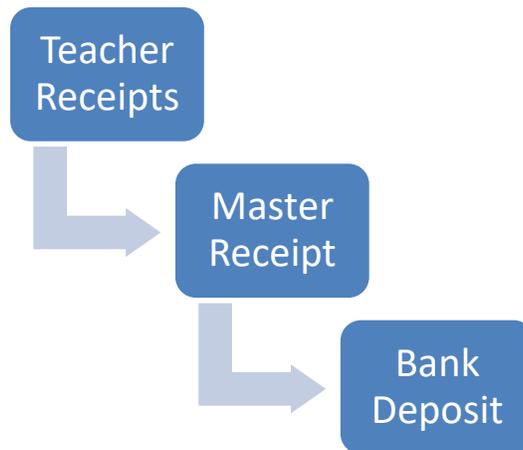
Teacher Receipts

Like the bookkeeper in the school office, teachers and staff who collect funds, **both** public and non-public, should utilize a pre-numbered duplicate receipt book. Receipt books should be secured, and a log should be maintained to track the receipt books by receipt numbers to the individual responsible for issuing the receipts. Teacher Receipts should be completed and issued in numerical order at the time funds are received. All pre-numbered receipts in a receipt book or record should be issued before another Teacher Receipt book or record is put into use. Teacher Receipts cannot be pre-signed and must contain an original signature of the person receiving the funds.

Bank Deposits

To protect the integrity of the internal control process within the school system, funds must be deposited in a timely manner. This should occur daily. If the deposit cannot be made before the bank closes, a locked night deposit bag should be used to secure the funds in the bank's night depository. In order to allow for time each day preparing the daily deposit, the Principal should establish and enforce reasonable timeframes for teachers to bring their daily collection of funds to the office and receive a Master Receipt. The purpose of the daily deposit and timelines is to provide an internal control structure to illustrate to the public that funds were deposited intact with an authorized depository (banking institution) outside of the school system.

⁸ <https://docs.alsde.edu/documents/68/LocalSchoolFinancialProcedures.pdf>



Cash Disbursements

Again, there is no financial need greater than that of adequate internal control for cash receipts and disbursements. This bears repeating within this manual because Alabama local schools make a wide variety of cash disbursements utilizing public funds. Contrary to common assumptions, fraud actually occurs more frequently in the cash disbursement cycle than in the cash receipt cycle from a national perspective.⁹ A large part of the bookkeeper's job of avoiding opportunity for fraud and safeguarding public funds functions around an orderly process by which cash disbursements are made.

All disbursements, no matter how urgent, should be made only when authorized through the official procedures and processes that have been established by the local board of education and/or the State of Alabama Department of Education. There are **several general policies that must be followed when dealing with cash disbursements:**

- Expenditures are incurred only under the authorization of the Principal.
- Expenditures will be paid by check disbursed at the local school level and supported by proper documentation.
- Purchases will be approved by the Principal (with a signed purchase order when required) before the purchase is made.
- Accounting records will be posted daily.
- The activity at the local school is summarized at the end of every month and compiled into monthly financial statements.

⁹ <http://www.osc.state.ny.us/localgov/pubs/lmgm/practiceinternalcontrols.pdf>

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- The financial statements report on transactions that affect accounts throughout the month.
 - These monthly financial statements are submitted to the Board of Education according to a scheduled date each month.

Internal Control Procedures of Cash Disbursements for Local Schools¹⁰

Purchase Orders

The Principal, as the manager of the school, should approve all expenditures that will be paid from school funds. A purchase order provides a variety of internal control checks and balances. From the principal's perspective, a purchase order allows the Principal to approve expenditures prior to purchase. From the vendor's perspective, a purchase order provides protection to the vendor for not charging Alabama sales tax on the school's purchases if the State of Alabama Department of Revenue audits the vendor's books. From the bookkeeper's perspective, a completed, pre-numbered purchase order approved by the Principal before the purchase of materials, supplies, or equipment allows the bookkeeper to show adherence to school board policies and procedures as well as maintains accountability within their job description. A purchase order register should be maintained to account for all purchase orders.

Invoices

One of the key considerations behind GAAP is **verifiability**: the ability to see how an entity arrives at a certain result from the data it provides on financial reports. A local school's accounting results are verifiable when they're reproducible, so that, given the same circumstances, another accountant outside of the school system (for example, an Examiner of Public Accounts) can reproduce the same effect on the financial statements that the bookkeeper did in the original transaction. Invoices, receipts, and documentation for receipts are key documents in assuring verifiability as well as the internal control process of any entity.

An invoice should be obtained for each purchase before payment is made.¹¹ The vendor invoice should include:

- Date of purchase
- Pre-printed or embossed name and address of the vendor listed clearly on invoice
- A description of the purchase,

¹⁰ <https://docs.alsde.edu/documents/68/LocalSchoolFinancialProcedures.pdf>

¹¹ According to ALSDE, an IRS Form W-9 should be completed and maintained on file for each individual or vendor that qualifies for IRS Form 1099 reporting.

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- Itemized listing of items purchased along with item price
 - Shipping and handling charges
 - Total amount of the purchase.

If a vendor without a pre-printed vendor invoice provides items or services, the vendor should sign an invoice containing the same information. Unless provided in another document, the school employee receiving the items purchased should sign the invoice. If the invoice is for services, the responsible school employee should sign the invoice after verification of services provided.

Before payment is made, invoices should be matched against the applicable purchase order so that documentation can be provided to the principal before checks are signed and payment is offered to the vendor.

Expenditures

Payments for school expenditures should be made from the school's checking account with the Principal acting as the maker of the check instrument. In banking terms, the maker is the authorized person to sign the check instrument which will be accepted by the banking institution as valid proof of authorized payment. If policy allows for a designee besides the Principal to sign (in their absence), this person should be someone other than the local school bookkeeper to maintain safeguarding of assets.

The following procedures are recommended from the aspect of checking accounts within the local school system:

- Never write checks to "Cash".
- Checks must be used in numerical order and any voided checks must be retained for audit purposes and clearly marked "**VOID**" on the check face in large letters.
- Checks should be filled out in their entirety including the recipient's name and amount of check before signature by the Principal.
- Invoices and supporting documents should be provided with the check to be signed and marked "**PAID**" when the check is signed and filed for accounting verifiability.
- Checks must be always secured within the bookkeeper's desk and only authorized personnel allowed access to the secure area where checks are held.

Bank Reconciliation

The preparation of a bank reconciliation is considered an internal control procedure over Cash. As mentioned earlier, Cash is the most vulnerable of assets within any economic entity, including local schools, and must have ample control procedures and processes to ensure accountability and transparency within the financial management system. The bank reconciliation reconciles as of a specific date, normally the end of the month, any differences between Cash in the funds and cash according to the bank's records.

When the school receives its bank statement, the school bookkeeper should verify that the amounts on the bank statement are consistent or compatible with the amounts in the school's Cash account in its general ledger and vice versa. Because the Principal is responsible for signing the checks for the local school, the Bookkeeper can perform the bank reconciliation which is an important internal control.

Due to timing differences, there may be a difference in the *balance on the bank statement vs. the balance in the Cash account on the school's books*. **It is also possible (perhaps likely) that neither reported balance before the bank reconciliation is the true balance.** Both balances may need adjustment in order to report the true amount of cash. However, the overarching goal is to prepare the bank reconciliation to show a common adjusted balance between the bank and the "books" of the school which should agree as well as highlight any reconciling items performed in the reconciliation.

Common terms found on a Bank Reconciliation for a Local School:

- **Deposits in Transit** - These are deposits that are in the cash per books but not in the cash per bank statement. The reason is that there is delay between when the cash gets recorded on the books and when the bank records the deposit. Deposits in transit are determined by comparing the deposits listed on the books with the deposits listed on the bank statement.
- **Outstanding Checks** - These are checks that have been deducted from the cash per the books but not the cash per the bank statement. The reason is that there is a delay between when the check gets recorded on the books and when the bank records the check. Outstanding checks are determined by comparing the check disbursements on the books with the checks listed on the bank statement.
- **Bank or Service Charges** - An expense for bank services that is listed on the bank statement but is not recorded on the school's books.

- **Non-Sufficient Fund Checks (NSF checks)** - A payment by check that has been recorded as a deposit on the books but was not collectible because of insufficient funds in the account of the person or vendor who presented the check to the school.

Common Bank Reconciliation Template for All Economic Entities

	<i>Name of School</i>	
	<i>Bank Reconciliation</i>	
	<i>Date - EOM</i>	
Bank Balance End of Month:		\$XXXX
Add: Deposit in transit		XXXX
Less: Outstanding checks		
#XXX	\$XXXX	
#XXX	\$XXXX	(XXXX)
Adjusted bank balance		<u>\$XXXX</u>
Book balance End of Month:		\$XXXX
Add: Items Shown on Bank Statement NOT in Books Yet (N/R; EFT; Errors in Books Favor) – Must List Separately on Each Line		XXXX
Less: Items Shown on Bank Statement NOT in Books Yet (Svc. Charge; NSF Checks; Errors) – List Separately on Each Line		(XXXX)
Adjusted book balance		<u>\$XXXXX</u>



Adjusted Balances Must Equal! After verifying with the Principal that the bank reconciliation is complete, the bookkeeper should do journal entries for ALL ITEMS listed under Book Balance – separately – for example, if the bank collected a payment (addition of cash example) for the school and it was deposited in the bank, the responding journal entry after the bank reconciliation would be to:

Cash		XXX	
	Revenues - xxxx		XXX

Summary of Common Internal Controls Found in Local Schools

This chapter discussed several internal controls found within local schools of Alabama. A well-planned internal accounting controls system should provide a local education agency with procedures that produce accurate, reliable, and verifiable financial statements and at the same time, safeguard the assets, financial resources and the integrity of every employee charged with the responsibility of handling public monies. Responsibility for internal controls rests at every level of authority within the school including the Principal, Assistant Principals, teachers, staff, and other employees. When an internal control procedure is used merely as a “form process” or because it has been used in the past or because it is a form provided by a governmental agency, accounting and related bookkeeping functions can become a matter of rote and not serve the purpose of the employee understanding their function and place in the internal control system. To serve a school system adequately, the purpose of each internal control should be shared with all employees and instances of fraud and abuse, where witnessed, should be reportable to the local school board.

EXERCISE 3.1

Hope High School has received its month end bank statement for October 2020. The Principal has asked you to prepare the bank reconciliation given the following information:

Balance in Bank Account, 10/31/20	\$39,010
Books Balance, 10/31/20	\$37,000

Outstanding Checks According to Analysis:

No. 1401	\$ 170
No. 1410	\$ 50
No. 1413	\$ 210
No. 1421	\$ 675
No. 1438	\$ 300
No. 1450	\$1050
No. 1456	\$1205

Cash Receipts Recorded October 31, 2020, however, deposited after 2 pm:

October 31, 2020 Deposit	\$1400
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Other Items to Note:

Bank Service Charge	\$ 25
NSF Check Returned	\$ 125

Check No. 1412 for \$650 was incorrectly recorded as \$550 in the accounting system and was issued to pay for teaching supplies. The invoice was for \$650 and the purchase order was also for \$650.

Directions:

On the following two pages, complete the bank reconciliation AND journal entries that are necessary to complete the bank reconciliation. It is recommended that you watch the presentation on the bank reconciliation before performing the journal entries.

EXERCISE 3.2

Hope High School has a new Principal and a new Bookkeeper. Ms. Sylvester has hired Trinity Tootrue to be the bookkeeper and both Ms. Sylvester and Ms. Tootrue are not aware of the various internal control procedures needed within an accounting environment to safeguard assets and maintain public trust in the accounting process. As such, when the auditor, Richard Righteous, shows up at year-end, he notes various findings found within the school's internal control procedures. Richard has asked you, a trusted bookkeeper who is knowledgeable of the internal control procedures found within the State of Alabama to look over his initial findings and note all of the internal control deficiencies you see in order to verify his own findings before he notifies the Board Superintendent of the issues found.

Receipt and Disbursement Policies Set Forth by Ms. Sylvester for Hope High School:

Ms. Sylvester told teachers at in-service training that receipt books should be maintained by both Ms. Tootrue and the teachers. A journal or notebook is ok to be used if the teacher cannot find the receipt book purchased by the school. Both Ms. Tootrue and teachers may deposit funds within the bank and must report this to Ms. Tootrue by Friday the deposit slip as well as the related receipts. Ms. Tootrue has found that it easier to do her job if she deposits fund daily and then sits down at the end of the week when it is quiet to update her receipt book. She has also found that Ms. Sylvester likes for the Assistant Principals, Lunchroom Manager, and the Glee Club Manager to have their own Master Receipt book so she sometimes has to ask for those at the end of the month before completing the financial reports for the Central Office.

Ms. Sylvester has decided it would be easier if she had a stamp made with her signature on it and distributing this stamp to all the personnel so both deposits and receipts can be made quicker to ensure efficiency of operations. Unfortunately, the Glee Club Manager has already lost the Master Receipt Book twice this year, so Ms. Sylvester has given them another receipt book but made sure it is red and noticeable in a pile of books.

Ms. Sylvester has approved the purchase of lockboxes for teachers to keep funds in their classrooms overnight in case they have to take up cash at the beginning of the day and don't have time in the lesson plan for the day to make the trip up to the office or go to the bank.

As to expenditures, Ms. Sylvester does not like to be bothered on Tuesdays and Thursdays so she has signed several blank checks to make sure that payments can be made in a timely manner. She has also suggested that to make vendors happy, payment for items in advance of receipt is ok if it is less than \$250 and done by the 25th of the month. She has also told Ms. Tootrue to make sure the bank has a signature card that allows both Ms. Sylvester and Ms. Tootrue to both sign the check in the absence of each other and teachers can bring the invoices straight to Ms. Sylvester to ensure prompt payment. The checkbook is in the top right drawer of Ms. Tootrue's desk and many teachers are aware of the location.

EXERCISE 3.3

Hope Middle School wants to raise money for a new sound system for its auditorium. The primary fundraising activity is a dance at which the famous disc jockey D.J. Sound will play tunes for the 6th and 7th graders. R.U. Kidding, the music and theatre instructor for the middle school, has been given the responsibility for coordinating the fundraising event. This is Mr. Kidding's first experience with fundraising, and he has decided that in order to teach the 7th graders responsibility, he will put them in charge of the event, and he will be a passive observer. Mr. Kidding does want to help some, so he makes 500 unnumbered tickets on the school copier to be used for the dance. He left the tickets on his desk in a box and told the 6th and 7th graders to take as many as they thought they could sell for \$5 each. In order that no extra tickets would be floating around, he told them to dispose of any unsold tickets. When the students received payment for the tickets, they were instructed to bring back the cash to Mr. Kidding and he would put the cash in a locked box in his desk drawer and turn it all in at one time. The 7th graders decided that some of the students should decorate the gym for the dance so Mr. Kidding gave each of the students a key to the money box and told them if they took money out to purchase materials, they should put a note in the box stating how much they took and what it was to be used for. After 2 weeks, the money box appeared to be getting full, so Mr. Kidding asked Perky Susie, the 7th grade class President, to count the money, prepare a deposit slip, and ask her Mom to run her by the bank after school to put in the bank account that Mr. Kidding had opened last year for another fundraiser.

The day of the dance arrived and before the dance began, the D.J., Mr. Sound, called Mr. Kidding at 4 pm and told him that he required cash up front and did not give receipts since he was not wanting to be audited by the IRS. So, knowing that they had made money, Mr. Kidding took \$400 out of the locked box and gave it to D.J. At the dance, Mr. Kidding decided it best that he mingle with the other chaperones since he had his eye on Ms. Serious, the cute new math teacher, and he put Sloppy Sam, Know It All Katie, and Kooky Keren together to work the 3 entrances, take tickets, sell tickets to those who did not have a pre-purchased ticket and gave them \$200 each and told them to give him what was left at the end of the night. As he danced with Ms. Serious, he thought that Principal Penny would be so happy with him since he counted at least 400 students there – some looked pretty old for 6th and 7th graders but he chalked that up to the fact that they asked their siblings to come so the dance was a success. At the end of the night, he received about \$500 from 2 of the gatekeeper students and couldn't find Sloppy Sam so he decided to wait until Monday to get with him over the receipts. The following Monday, after getting \$180 from Sloppy Sam who couldn't remember how he had less money than he started with, Mr. Kidding decided to close the bank account which had \$250 in it, tallied up the notes from the box for approximately \$300, and gave the \$420 left in the box to the Principal's bookkeeper. Ms. Penny called him to the office later and asked for an accounting noting that after generating approximately \$2,000 in sales, how was it that the dance only netted \$1350? Mr. Kidding was stumped. He told the Principal he was not an accountant – he was an artist – and he was only trying to help raise money for school.



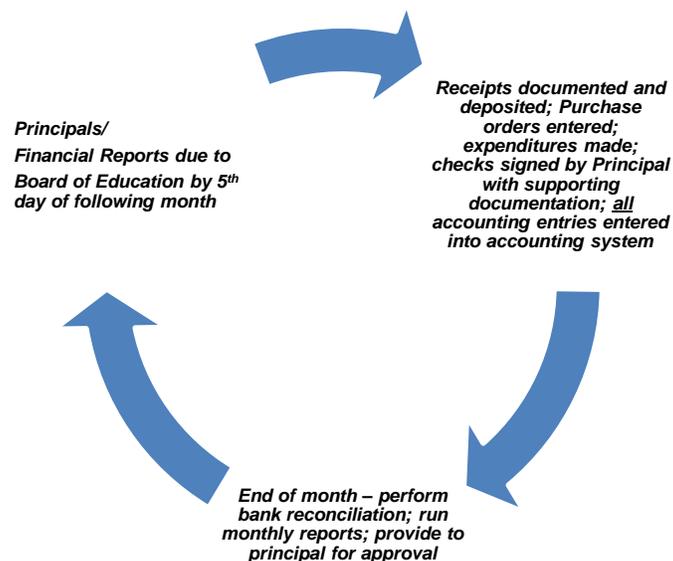
CHAPTER 4

ACCOUNTING IN THE LOCAL SCHOOLS

Alabama citizens and businesses commit a tremendous amount of its resources to fund the Alabama educational system and in return, rightfully, expect that the resources are managed **efficiently and effectively**. **Accountability and stewardship of public funds is the responsibility of every LEA and its employees**. Each school and district management leader must report, explain and justify their use of these funds.

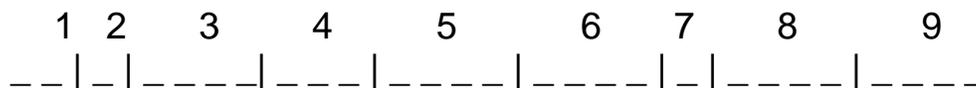
Schools must “**maintain an accounting system in accordance with generally accepted accounting principles and governmental accounting standards**” (SDE Administrative Code 290-2-5-.02(a)1. Financial accounting and bookkeeping assist management in fulfilling management’s stewardship responsibility by providing regular, complete, accurate, and detailed financial reports (on a monthly and annual basis) in an understandable and useful basis for the citizenry to assess how management allocated and used the resources.

An accounting system is the means by which financial transactions are planned, captured during the actual operation of the school system, recorded in the books of accounts, and then analyzed to produce the various reports for management, financial status and accountability.¹² **The role of the school bookkeeper is vital to achieving the above financial reporting goals**. The image below depicts the accounting cycle for the local school accounting process from the bookkeeper’s perspective.



¹² ALSDE Accounting Manual, August 13, 2019

In 1995, the Alabama Department of Education adopted a computerized accounting system that was designed to serve as a flexible tool to meet the needs of all school systems within the State of Alabama. The 27-digit code, with 9 components, provides a common means of communication to be used in planning, recording, accumulating, controlling, and reporting the financial activities of the school systems within the state. School systems should uniformly utilize this component structure in order to provide comparability between school systems.¹³



1. **FUND TYPE & ACCOUNT GROUP**
2. **ACCOUNT TYPE**
3. **ACCOUNT CODE**
4. **OBJECT**
5. **COST CENTER**
6. **FUND SOURCE**
7. **APPROPRIATION YEAR**
8. **PROGRAM**
9. **SPECIAL USE**

The following accounting transactions are normally found within the school system:

Receipts of Funds

Bookkeepers receive funds from several different sources – students, teachers, club and booster sponsors, school board, and local supporting organizations. As such, the receipting of funds is a very important function that must be recorded in a prompt and responsible manner. Also, the preparation of bank deposits, reconciling the school bank account, and providing receipts and reports to stakeholders is part of this important process.

¹³ http://www.alsde.edu/home/Sections/DocumentDownload.aspxAccounting_Manual.rtf

Expenditures of Funds

Bookkeepers also make payments from funds as part of their daily activities. As such, the disbursement of funds is a very important function that must be recorded in a prompt and responsible manner. Expenditures are the results of spending funds. Within the local schools, expenditures will be paid by check, signed by the Principal, and supported by proper documentation. Purchases will also be approved by the Principal (with a signed purchase order when required) before the purchase is made. Accounting records should be posted daily. Monthly financial reports reflecting accurate balances and activities of the accounts of the school should be reviewed and approved by the Principal as well as submitted to the Local Education Agency at the end of the month.

When a bookkeeper creates a purchase order, the bookkeeper will be inputting the following basic entry into the accounting system:

Encumbrances	XXX	
Reserved for Encumbrances		XXX

Once the order is received, this journal entry is reversed in order that the invoice may be paid.

Reserved for Encumbrances	XXX	
Encumbrances		XXX

When a bookkeeper makes a payment using a check, the bookkeeper will be inputting the following basic entry into the accounting system:

Expenditure	XXX	
Cash or Accounts Payable		XXX

If Accounts Payable is utilized, the following entry is made when the check is created for signature by the Principal:

Accounts Payable	XXX	
Cash		XXX

These economic events can be recorded either through several journal entries or one compound journal entry, however, the correct coding and funding source must be considered in order to answer which specific accounts were affected. Expenditures are more involved than Revenue Sources allowing more choice among account codes - Expenditures or Function Codes (1000-9999) in the State of Alabama Chart of Accounts¹⁵.

¹⁵ <https://www.alsde.edu/sec/leaaccount/Pages/acctman-all.aspx>

The areas are:

- Instruction (1100)
- Student Support Services (2110-2199)
- Instructional Staff Support Services (2210-2299)
- School Administrative Services (2310-2399)
- Operation & Maintenance (3100-3999)
- Student Transportation Services (4110-4199)
- Other Expenditures (9800 - 9899)
- Interfund Operating Transfers Out (9910)

When in doubt, bookkeepers should ask the Chief School Financial Officer, or a designated employee for local schools within the central office, for clarification on how to code non-routine expenditures to avoid coding edits that may affect month-end or year-end close out procedures.

Common Code Combinations for Local Schools¹⁶

Function Code	Object Code	Program Code
1100-Instruction Regular K-12	Any code directly associated with classroom instruction or dealing directly with the interaction between teachers and students	1100,1200,1500,1700,1810,1890, 4300, 4400, 4500, 2200-2900 (Sp Ed), 3700-3800 (Vocational) Pool Program: 8100
2110-2190 Instruction Support Student Support	Any code directly associated with those services or activities providing support for students and to enhance instruction	1100,1200,1500-1700,4300, 4400, 4500, 1810, 2200-2900, 3800,3500- <i>Use only with function code 2120</i> Program Pool: 8210-8219
2210-2290 Instruction Support Staff Support	Any code directly associated with those services or activities providing support for instructional staff and to enhance instruction	1100,1200,1500,1700,1810, 2200-2900 (Sp Ed) 3700-3800 (Vocational) Program Pool: 8220-8229
2310-2390 <u>School Administrative Services</u> Principal/Assistant/Office Operation Services	Any code directly associated with activities concerned with directing and managing the operations of a particular school office	1100,1200,1500,1700,1810, 2200-2900 (Sp Ed) 3600 (Vocational) Program Pool: 8230-8239
3100-3900 <u>Security,</u> <u>Operation & Maintenance Services</u>	Any code directly associated with keeping the grounds and buildings open and <u>safe</u> and equipment working	1100,1200,1500,1700,1810,4400,4500 2200-2900 (Sp Ed) 3800 (Vocational) Program Pool: 8300
4110-4190 Auxiliary Services Extra /Co-curricular Transportation	Any code directly associated with conveying students on trips to athletic events, field trips , and other "extra" school activities	1100,1200,1500-1700, 1810, 3800, 4400, 4500 <u>2200-2900 (Sp Ed) 4130 Function</u> <u>3800 (Voc) 4140 Function</u> Program Pool: 8410
7100-7900 Capital Outlay-Real Property \$50,000 or Greater Only	510-519 and 324 Use only these object codes	9100 Use only this program code
9110-9190 Continuing Education: (Extended Day/Tutoring) or Outside of K-12 students (Adult/Preschool)	Any code directly associated with providing "extra" remediation/guidance/tutoring or services for Preschool or <u>Outside</u> of Regular School Day	2200-2900 (Sp Ed) 3800 (Vocational) 4110-5900 Important: * 4300,4600,4711,4712,4800,5100
9310-9390 Community Services	Any code directly associated with providing community or civic services	Non-Instructional Programs 9510-9540
9800 Other expenditures Not associated with instruction	478-Items for Resale 699-Accomodations Exp 399-Rarely used. Only if associated with "Resale"	Please use only these program codes: 9600, 4400, 4500

¹⁶ <http://www.alsde.edu/home/Sections/DocumentDownload.aspxCommonCodeCombinLocalSchoolAcctg.rtf>

Activity Fund Accounting

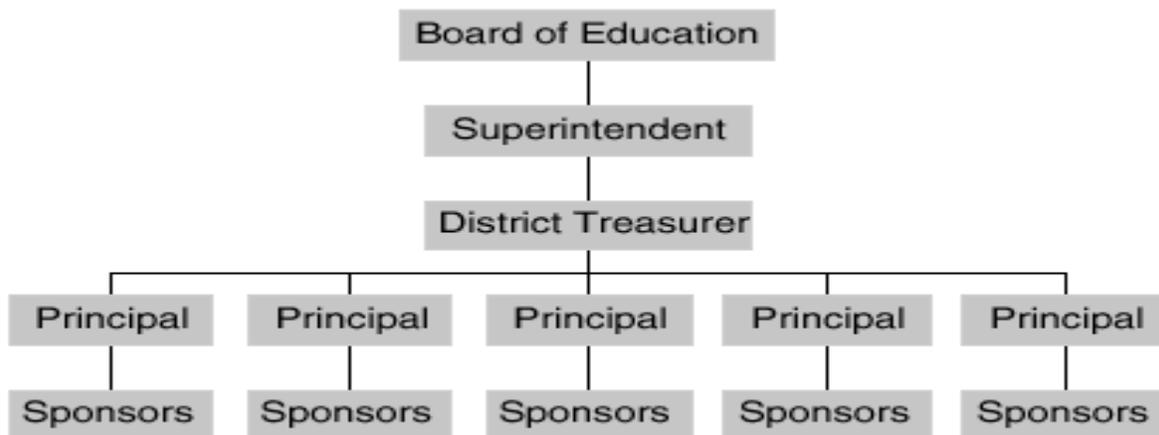
Activity funds are established to direct and account for monies used to support co-curricular and extra-curricular student activities. Policies relating to student and district activity funds **should be in writing** and distributed to all activity fund supervisors, sponsors, and accounting personnel. A useful set of general policies includes **at least** the following:

- All activity funds should be subject to sound internal control procedures.
- All activity funds should be accounted for on the same fiscal year basis as all other school district funds.
- All activity funds must be audited and subject to well-defined procedures for internal and external auditing.
- All employees responsible for handling and recording activity fund monies should be bonded by the district.
- One or more activity fund supervisors should be formally designated by the board of education.
- Depositories for student activity funds should be approved by the board of education and be further subject to the same security requirements as all other board funds.
- All activity funds should operate on a cash basis, meaning that no commitments or indebtedness may be incurred unless the fund contains sufficient cash.
- A system of purchase orders and vouchers should be applied to all activity funds that requires written authorization for payment and should be strictly enforced.
- A system for receipting cash should be adopted that includes using pre-numbered receipt forms for recording cash and other negotiable instruments received.
- All receipts should be deposited intact. That is, all receipts should be deposited in the form in which they are collected and should not be used for making change or disbursements of any kind.
- All receipts should be deposited daily. Un-deposited receipts should be well secured.

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- A system for disbursing funds that includes using pre-numbered checks and multiple original signatures (no signature stamps) should be adopted as the sole means for disbursing activity fund monies.
 - A perpetual inventory should be maintained on pre-numbered forms, receipts, and other documents to create an adequate audit trail.
 - Bank statements for activity funds should be reconciled as soon as they are received.
 - Using activity fund receipts to cash checks to accommodate individuals, to make any kind of loan, to pay any form of compensation directly to employees, or to extend credit should be strictly prohibited.
 - Monthly financial reports on all activity funds should be prepared and submitted to the administration and the board of education. A full reporting of activity funds should be included in the district's annual financial statements.
 - Student activity fund monies should benefit those students who have contributed to the accumulation of such monies.
 - A board-approved process should be specified for all fundraising activities, and any fundraising event should require advance approval.

Lines of Authority for Activity Funds

The dispersed nature of student activity funds and the multiple site collections for some district activity fund revenues dictate a need for orderly controls on all activity funds. These controls include establishing lines of authority and a set of policies to guide the operation of all activity funds. Proper control begins with the appropriate recognition of lines of authority over all monies handled by the school district. According to the National Center for Education Statistics, the local board of education should adopt a set of guidelines and regulations that includes the following lines of authority:¹⁷



Ideally, the following should be included in the lines of authority within the Alabama local schools starting with the Local Education Agency/Board of Education establishing policies to the officers of the organization:¹⁸

- **Board of Education** - The board of education should adopt policies to govern the establishment and operation of all activity funds. The district's auditors should review these policies for sound accounting and reporting principles.
- **Superintendent** - The superintendent should be directly responsible to the board of education for administering all board policies.
- **Chief School Financial Officer** - The chief school financial officer should have overall responsibility for accounting for and reporting all funds, including district and student activity funds, to the board. The chief school financial officer is also responsible for implementing and enforcing appropriate internal control procedures.

¹⁷ Allison, G.S. (2015). Financial Accounting for Local and State School Systems: 2014 Edition (NCES 2015-347). U.S. Department of Education, National Center for Education Statistics. Washington, DC: U.S. Government Printing Office.

¹⁸ Activity Fund Accounting for Local Schools, Presentation made to ASBO – September 2013

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- **Principal** - The Principal at each school site should be designated the activity fund supervisor for that school building. The activity fund supervisor has overall responsibility for the operation of all activity funds, including collecting and depositing activity fund monies; approving disbursements of student activity fund monies; and adequately supervising all bookkeeping responsibilities. The activity fund supervisor should be a signatory to all disbursements, including checks drawn on the activity fund.
 - **Sponsors** - The sponsor of each student organization is responsible for supervising all activities of the organization, including approving student activity fund transactions. Sponsors should be employees of the district and under the direct control of the activity fund supervisor.
 - **Parent Support Organization Officers** -The officers of each support organization are responsible for the activities of the organization and assurances they follow their bylaws and established laws, regulations and board policies for the operations of the organization.

Board of Education

Adopt policies to govern the establishment and operation of all activity funds.

Superintendent of Board of Education

Directly responsible for administering all Board Policies.

Chief Financial Officer

Overall responsibility for accounting for and reporting all funds, including district and student activity funds, to the Board.
Also responsible for implementing and enforcing appropriate internal control procedures.

Principal

Activity Fund supervisor for that school. Overall responsibility for the operation of all activity funds, including collecting and depositing activity fund monies; approving disbursements of student activity fund monies; and adequately supervising all bookkeeping responsibilities.
Should be a signatory of all disbursement, including checks drawn on the activity fund.

Sponsors

Responsible for supervising all activities of the organization including approving student activity fund transactions.
Should be employees of the district and under the direct control of the Principal.

Parent Support Organization Officers

Responsible for the activities of the organization and assurances they follow their bylaws and established laws, regulations and board policies for the operations of the organization.

Common Accounting Procedures Using Activity Funds

Depending on the local school, the volume of activity fund transactions and the amounts on deposit can be substantial. Internal control procedures must be followed due to a significant amount of activity fund cash receipts are collected as currency, not checks normally. The school bookkeeper normally collects the receipts and disburses the funds for activity funds if the funds are kept within the school books and records. Bookkeepers must have a thorough understanding of what the funds are for and how they should be accounted for in order to do their jobs properly. Principals, sponsors, and parent support organization officers must play a role in this communication of understanding as well as the Chief School Financial Officer and others at the central office.

Fundraisers, ticket sales, concessions, and commissions are all examples of activity fund accounting that takes place with all local schools in the State of Alabama.¹⁹ Each of these economic events and their proper accounting procedures will be discussed in the following pages as well as examples worked to ensure an understanding of the accounting processes that must be followed for these activity fund economic events.

Accounting for Ticket Sales

Wherever admission is charged, tickets should be sold for admission to the school-related event including football, basketball, baseball, softball, volleyball, soccer, wrestling, swimming, track, and other athletic events, as well as, beauty pageants, dances, theatrical performances, talent shows, carnivals, festivals, and other school-related events.

The use of tickets for admission events is an internal control procedure that assures that entrants to events paid the same admission fee and more importantly, from an accounting perspective, that all admission revenues are deposited in the school's bank account. Pre-numbered tickets may be printed for a specific event or may be sold from a roll of generic tickets. If generic tickets are sold for seasonal events, such as football or basketball games, ticket colors should be alternated.

A report of ticket sales form must be issued for everyone selling the tickets at the time the tickets are provided to them for the event. The report of ticket sales form should contain the following information:

1. Name of the event.
2. Date of the event.

¹⁹ <https://docs.alsde.edu/documents/68/LocalSchoolFinancialProcedures.pdf>

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3. A line for the name or signature of the person receiving the tickets for sale.
 4. The beginning and ending ticket numbers of the tickets issued.
 5. The beginning and ending ticket numbers of the tickets not sold.
 6. A line for the signature of the person receiving the unsold tickets and cash collected.
 7. A space for reconciling collections based on ticket sales to actual cash returned.

It is important to note that bookkeepers take a part in this process from issuing Master Receipts as well as depositing the funds from these events. A Master Receipt should be issued to an individual (organization's treasurer) for the cash collected from ticket sales. A separate Master Receipt should be issued for Change Cash. All cash collected must be deposited intact. **Individuals must not use cash collected or change cash to cash any checks, including school checks issued for officiating, security, ticket sellers, or ticket collectors.**

Accounting for Fundraising

Normally school-sponsored fundraisers are conducted by the school in order to generate a profit and provide supplemental revenue for the school public funds within the general fund or an individual club or class account. A fundraiser is considered to include ANY activity involving the sale of items to individuals that has the POTENTIAL to make a profit. These fundraising activities could include vending operations, bookstores, pictures, concessions, carnivals, book sales, candy sales, magazine sales, walk-a-thons, car washes, bake sales, or more involved outside activities such as golf tournaments. Fundraising activities do not include membership dues, fees, fines, ticket sales for sanctioned athletic events, activity fees, and similar fees.

No matter what the purpose of the fundraising activity within the school, accountability is necessary from the inception of the activity to the end of the activity. The Principal must approve each school fundraising activity conducted by students, teachers, school employees, or school-related organizations.²⁰ A form requesting authorization for a fundraising activity must be approved by the Principal prior to the start of the fundraising activity and should contain the following information:

1. Date of the request.
2. Name of the individual making the request.

²⁰ The local school board may exempt school-related organizations from this requirement if the activity of the organization is not under the control of the Principal.

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3. Activity account to receive proceeds from fundraiser.
 4. Class, club, or organization that will conduct activity, if applicable.
 5. Name of fundraising project.
 6. Beginning and ending dates of fundraiser.
 7. Description of fundraising activity, such as: name of company supplying items for sale; description of items for sale; estimated cost of items for sale; sales price of items; description and estimated cost of related fundraiser expenses; description of method of sales and collections; estimated profit from fundraiser; and purpose of fundraiser.

Bookkeepers again play a vital role in the accounting side of the fundraiser from receipt of funds to the deposit of funds. Approved fundraising activities must comply with financial procedures for school funds, including: all funds collected must be delivered to the Principal's office for a Master Receipt in the form received by the fundraising activity; any income from fundraisers must be accounted for and deposited on a timely basis using the proper forms; all fundraising expenses, including sales awards to students, must be presented to the Principal for payment by check; and within a reasonable time after completion of the fundraising activity, a form should be submitted to the Principal that documents the result of activity.

For **Exercise 4.1**, the Hope High School Varsity Cheer Boosters, a non-public fund, has elected to host a Golf Tournament to raise funds for their Nationals cheer camp and competition they hope to attend next June. The fundraiser has been authorized by Principal Sylvester for August 1, 2020 through September 30, 2020 with the Golf Tournament to occur on September 29, 2020 at the Robert Trent Jones Trail – Oxmoor Golf Course. This fundraiser helps raise money for the squad to attend the National High School Cheerleading Competition in Orlando, Florida. The entrance cost is \$60.00 per player. The cash prizes will consist of \$500 for the first-place team and \$250 for the second-place team. These funds will come out of the Varsity Cheer fund. Green and cart fees will be \$20.00 per participant. Also, cheerleaders are expected to raise \$400 from “Hole Sponsors” who will display their advertisements at each hole. The teacher who is responsible for the Cheer Boosters is Ms. Glee Spirit. Ms. Spirit brought these to you, the bookkeeper, on September 30, 2020 for deposit and reconciliation.

Following is a list of accounting transactions for **Exercise 4.1**:

- 64 golfers signed up and paid their fees (Cash collected on day of tournament – Teacher/Sponsor Receipt No. 13519) – Master Receipt No. 1252
- 18-hole sponsors were obtained and paid their fees (Teacher/Sponsor Receipts No. 13501 – 13518) – Master Receipt No. 1242
- Prizes were given as planned to 1st place and 2nd place team (Check No. 9525 to Ms. Glee Spirit).
- Donations from area bank who did not wish to sponsor received in amount of \$500 (Teacher/Sponsor Receipt No. 13500) – Master Receipt No. 1243
- Other costs for the tournament:
 - Paid Robert Trent Jones Trail – Oxmoor Golf Course for the costs per player (Check No. 9526)
 - Paid \$120 to Sign and Banner for the 18-hole sponsors signage (Check No. 9516)
 - Paid \$40 in postage for the invitations to be mailed to the 100 top area golfers (Check No. 9500)
 - Paid Alley Photocopy \$50.00 for photocopying for sponsorship flyers and tournament rules, etc. (Check No. 9510)

Backup information was received in good format. From these transactions, please fill out the next 3 pages (pages 54 – 56) in the proper format making sure to reconcile the amounts. Also, answer the questions at the end of the exercise on the next steps needed in the accounting process. Please note any internal controls that need to be observed.

Monthly Financial Reporting Found Within Local Schools

The activity at the local school is summarized at the end of every month and compiled into monthly financial statements. The financial statements report on transactions that affect all local school accounts throughout the month. These monthly financial statements are submitted to the Board of Education according to a scheduled date each month, normally at the beginning of the month, for the previous month financial transactions. The monthly financial reports serve as the source of information necessary for the Principals to properly manage the schools. Because accounting records are the basis of the monthly financial reports, it is essential that each school's records are accurate, current, and they exhibit the true financial position of the school funds. Below is a discussion of common monthly reports found in local school accounting.

Trial Balance

A trial balance is a list of all the ledger accounts with their respective balances at a point in time. At the end of each month, after all transactions have been recorded, a trial balance should be prepared to determine if general ledger debit and credit balances are equal. If the totals of the debit and credit columns are equal, the ledger from which the figures were taken is said to be "in balance." The trial balance is normally used to verify the accuracy of posting and is the first step in the preparation of financial statements and reports.

Monthly Financial Reports to Principal and Central Office

The School Fiscal Accountability Act (No. 2006-196) requires local boards of education to post monthly financial reports and annual school budgets on the board of education's website. The required monthly reports should be presented to the local board of education before posting to the website within 45 days after the end of the reporting month. As a rule, bookkeepers should prepare monthly reports for the Principal and the central office to include fund status of both receipts and expenditures along with the corresponding variance between budget vs. actual expenditures to date for the fiscal period. Here is a sample of some of the monthly reports that would be submitted to the central office:

- Copy of bank statements signed by Principal.
- Return check form signed by Principal.
- Bank Reconciliation Report signed by Principal.
- Savings Account Bank Reconciliation Report signed by Principal.
- Journal Entry Listing for Fixed Assets Reports
- Fixed Asset Inventory Cards
- Monthly Financial Report signed by Principal
- Open Purchase Order Report.
- Copies of checks (and supporting documentation)
- Copies of student refund checks

Activity Fund Reports²¹

A monthly report of cash receipts and disbursements to the activity fund should be prepared and reviewed by the activity fund supervisor and submitted to the school district office. Column headings should include the following:

- Beginning cash balance, which should agree with the ending cash balance on the prior month's report
- Cash receipts
- Cash disbursements
- Ending cash balance
- Unpaid purchase orders
- Unencumbered cash

The school bookkeeper also should prepare a monthly financial report for each student organization, showing the organization's cash receipts and disbursements. These reports should be reviewed by the activity fund supervisor and submitted to the student organization's sponsor. Each sponsor should then compare the report prepared by the activity fund bookkeeper with the sponsor's records. Any discrepancies should be resolved immediately. Additionally, the school finance office should periodically perform internal audits of the reports and supporting records.

As governments increasingly respond to the demands for fiscal and operational accountability, best practice dictates the creation of strong controls over activity funds, including assurances that all transactions are recorded and reported in district financial records. Additionally, at a minimum, proper lines of authority combined with strong control practices—such as segregation of duties, multiple checks and balances, requirements for annual audits, and regular financial reporting—are the elements needed to protect against error and abuse.

²¹ Allison, G.S. (2015). *Financial Accounting for Local and State School Systems: 2014 Edition (NCES 2015-347)*. U.S. Department of Education, National Center for Education Statistics. Washington, DC: U.S. Government Printing Office.

CHAPTER 5

FINANCIAL REPORTING FOR THE LOCAL EDUCATION AGENCY/SCHOOL BOARD

FINANCIAL REPORTING FOR THE INDEPENDENT SCHOOL DISTRICT

An entity's financial statements are an important element in conveying the current state, financial health, and future viability of the organization. Financial statements, regardless of the industry, report on several similar components, including assets, liabilities, and equity (i.e., fund balances or net position). School districts and other governmental agencies are no exception.

The GASB is the oversight body responsible for establishing the governmental reporting criteria, including the level of detail, format, and required contents of external financial statements. GASB provides much guidance in the proper interpretation and implementation of these requirements. GASB's mission was to establish and improve standards of financial reporting by state and local governments. Why is there such a concern about financial reporting? Consider the role that financial reporting has played:

<u>FINANCIAL REPORTING</u>	
1.	Demonstrates Accountability
2.	Provides Information to Assess Accountability
3.	Basis for Decision Making

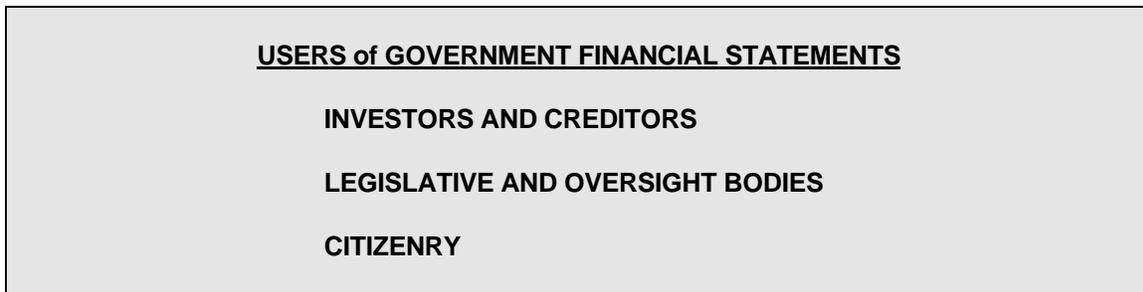
Financial reporting fulfills government's duty to be publicly accountable. It provides information for citizens to assess the accountability of government. And, financial reporting provides information for citizens and others to use as a basis for making economic, social, and political decisions.

Financial reporting is a recognized medium of communication. It is GASB's responsibility to ensure that quality reporting is done by state and local governments. The Governmental Accounting Standards Board consists of seven board members, and several professional and administrative staff. Board members are appointed for a five-year term which can be renewed. The work of the GASB is conducted through due process. Due process requires the GASB to follow certain procedures in the standard setting process. The procedures include dissemination of written proposals and public forums open to the affected parties. This ensures that fairness prevails in the setting of standards.

The unique characteristics of state and local government financial statements, as they are currently prepared, are supported by the GASB Accounting Concept Statement No. 1, *Objectives of Financial Reporting*. The Statement recognized that financial report

users need a variety of information to assess accountability and make resource allocation, investment, social, political, and other decisions affecting the governmental reporting entity.

Financial report users represent a diverse, multiple constituency including investors and creditors, legislative and oversight bodies, and the citizenry.

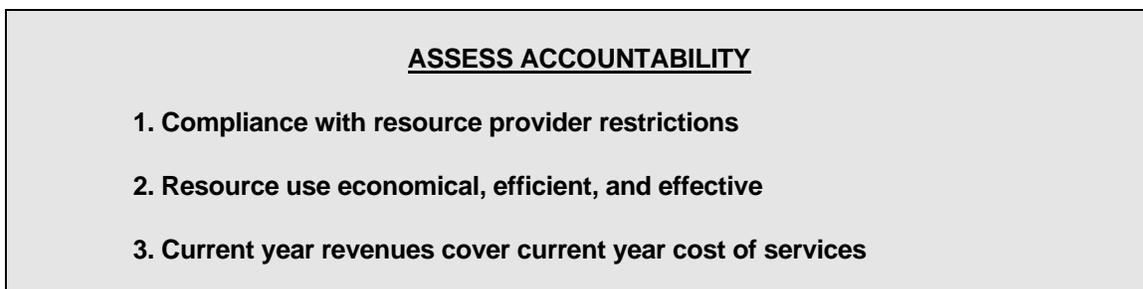


These users each have specific needs and wants regarding information from the reporting entity. They also have specific information needs that are common to each other. Common information needs should be provided in the government's financial statements.

Objectives of Financial Reporting

Common information would facilitate the users' decisions regarding the entity's accountability, operating results, operating capacity, and its solvency.

To assess accountability, the user needs to know if the government was in compliance with resource restrictions imposed by the legally adopted budget and other contractual agreements. The Statement of Revenues, Expenditures, and Changes in Fund Balances -Budget to Actual presents actual operating results on a comparative basis with the legal budget to demonstrate compliance. In addition, classifications on the Balance Sheet such as restricted, designated, and unrestricted provide disclosure regarding information about the government's assets.



Statement users also want to know how government resources were managed. Did they achieve government goals in the most economical, efficient, and effective way? Reports on the economical, efficient, and effective use of resources is provided through performance reports and through voluntary data provided in the statistical section of the year end reports.

Users also want to know if current year revenues were sufficient to pay for current year costs. The concept that current-year revenues should be sufficient to pay for current year services is called **interperiod equity**. Governments should be able to generate current revenues to obtain currently needed services. Or put another way, current services can only be provided if sufficient revenues are generated during the current year. There is a belief that governments should not use up reserves nor incur general obligation debt to cover daily operating costs. To do so, would jeopardize the financial security of future generations.

Governments, including local education agencies, issue financial statements prepared according to generally accepted accounting principles (GAAP) to meet the objectives of financial reporting. Financial statement users rely on the information in the GAAP statements to present fairly the financial position and operating results of the government. This will be valid if an adequate accounting system and internal controls are in place. Therefore, good accounting and bookkeeping procedures are essential for accurate financial reporting.

GASB 34

In June, 1999, GASB issued GASB 34 – *Basic Financial Statements – and Management’s Discussion and Analysis - for State and Local Governments*.²² This Statement established financial reporting standards for state and local governments, including states, cities, towns, villages, and special-purpose governments such as **school districts** and public utilities. It established that the basic financial statements and required supplementary information (RSI) for general purpose governments should consist of:

- **Management’s discussion and analysis (MD&A).** MD&A should introduce the basic financial statements and provide an analytical overview of the government’s financial activities. MD&A should be provided at the beginning of the report so the financial statement reader can gain a perspective from management as to the financial strengths and weaknesses of the government for the fiscal period report.
- **Government-wide financial statements – including Statement of Net Position and a Statement of Activities:** These financial reports are prepared using the economic resources measurement focus and the accrual basis of

²² www.gasb.org

accounting, these statements should report all of the assets, liabilities, revenues, expenses, and gains and losses of the government. Each statement should distinguish between the governmental and business-type activities of the primary government and between the total primary government and its discretely presented component units by reporting each in separate columns. Fiduciary activities, whose resources are not available to finance the government's programs, should be excluded from the government-wide statements.

- **Fund financial statements** which are financial statements that focus on the government's major governmental and enterprise funds, including its blended component units. Fund financial statements should report information about a government's fiduciary funds and component units that are fiduciary in nature. Governmental fund financial statements (including financial data for the general fund and special revenue, capital projects, debt service, and permanent funds) should be prepared using the current financial resources measurement focus and the modified accrual basis of accounting. Proprietary fund financial statements (including financial data for enterprise and internal service funds) and fiduciary fund financial statements (including financial data for fiduciary funds and similar component units) should be prepared using the economic resources measurement focus and the accrual basis of accounting.
- **Notes to the financial statements** consist of notes that provide information that is essential to a user's understanding of the basic financial statements.

GOVERNMENTAL AND BUSINESS ACTIVITIES

Currently, two distinct bases of accounting are used in government - accrual basis of accounting and modified accrual basis of accounting. When the measurement focus of the fiscal entity is economic resources, the accounting basis required is full accrual. When the measurement focus in the fiscal entity is financial resources, the accounting basis required is modified accrual.

<u>MEASUREMENT FOCUS</u>	<u>ACCOUNTING BASIS</u>
Economic Resources	Full Accrual
Financial Resources	Modified Accrual

Therefore, business activities are measured using accrual accounting and governmental activities are measured using modified accrual accounting.

Modified accrual differs from accrual in that revenues must not only be measurable but available for spending during the fiscal year or shortly after the fiscal year end to record a REVENUE. Also, modified accrual recognizes expenditures, not expenses, when incurred.

According to accrual accounting, REVENUES will be recognized in the period when earned and measurable; EXPENSES will be recognized in the period incurred if measurable.

TRANSFERS of resources between funds are recognized during the accounting period in which the interfund receivable and payable arise.

	<u>ACCOUNTING BASIS</u>	
	<u>FULL ACCRUAL</u>	<u>MODIFIED ACCRUAL</u>
REVENUE	Earned	Earned & Available
EXPENSE	Incurred	-----
EXPENDITURE	-----	Incurred
TRANSFERS	During the period in which the interfund receivable and payable arises.	During the period in which the interfund receivable and payable arises.

There are two significant differences in these accounting bases. First, revenues are recognized when earned under accrual accounting regardless of when they are received. Under modified accrual accounting, however, revenues are recognized only if available. Available means during the year or soon enough after the end of the fiscal period to pay the liabilities incurred within the fiscal period. There is no authoritative definition of "when available," but practice has commonly used a 60-day period following the end of the fiscal year.

The following statements are examples of financial statements that are found at the district level for a local education agency in Alabama for the fiscal year 2007.

A local education agency's (otherwise known as the Board) basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the basic financial statements.

LEA BASIC FINANCIAL STATEMENTS

- 1) government-wide financial statements
- 2) fund financial statements
- 3) notes to the basic financial statements

Government-wide financial statements - The *government-wide financial statements for a school board* are designed to provide readers with a broad overview of the Board's finances as a whole instead of on an individual fund basis, in a manner similar to a private-sector business, indicating both long-term and short-term information about the Board's overall financial status. It is important to note that all of the activities of the Board reported in the *government-wide financial statements* are classified as governmental activities. These activities include, but are not limited to, student transportation, school food services, facility maintenance, local school public funds, interest and fiscal charges on long-term debt, and student instruction. *Government-wide financial statements* report the capitalization of capital assets and depreciation of all exhaustible capital assets and the outstanding balances of long-term debt and other obligations. These statements report all assets and liabilities perpetuated by these activities using the accrual basis of accounting. The accrual basis considers all of the Board's current year revenues and expenses regardless of when received or paid. This approach moves the financial reporting method for governmental entities closer to the financial reporting methods used in the private sector. The following *government-wide financial statements* report on all of the governmental activities of the Board as a whole.

The **Statement of Net Position** (example shown on page 68 of this manual) is most closely related to a balance sheet. It presents information on all of the Board's assets (what it owns) and liabilities (what it owes), with the difference between the two reported as net position. The net position reported in this statement represent the accumulation of changes in net assets for the current fiscal year and all fiscal years in the past combined. Over time, the increases or decreases in net position reported in this statement may serve as a useful indicator of whether the financial position of the school board is improving or deteriorating.

The **Statement of Activities** (shown on page 69 of this manual) is most closely related to an income statement. It presents information showing how the Board's net position changed during the current fiscal year only. All of the current year's revenues and expenses are accounted for in the *statement of activities* regardless of when cash is received or paid. This statement shows gross expenses and offsetting program revenues to arrive at net cost

information for each major expense function or activity of the Board. By showing the change in net position for the year, the reader may be able to determine whether the Board's financial position has improved or deteriorated over the course of the current fiscal year. The change in net position may be financial or non-financial in nature. Non-financial factors which may have an impact on the Board's financial condition include age and condition of facilities, mandated educational programs for which little or no funding is provided, and increases or decreases in funding from state and federal governments, to name a few.

Fund financial statements – Recall that a fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Board uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Board can be classified into two categories: governmental funds and fiduciary funds.

Governmental Funds - Governmental *financial statements* begin on page 70. These statements account for basically the same governmental activities reported in the *government-wide financial statements*. The *financial statements* presented herein display information on each of the Board's most important governmental funds or *major funds*. This is required in order to better assess the Board's accountability for significant governmental programs or certain dedicated revenue. The Board's *major funds* are the General Fund and the Capital Projects Fund.

The *fund financial statements* are measured on the modified-accrual basis of accounting, where revenues and expenditures are recorded when they become measurable and available. As a result, the *financial statements* focus more on the near-term use and availability of spendable resources. The information provided in these statements is useful in determining the Board's immediate financial needs. This contrasts with the accrual-based *government-wide financial statements*, which focus more on overall long-term availability of spendable resources. The relationship between governmental activities reported in the *government-wide financial statements* and the governmental funds reported in the *fund financial statements* are reconciled after the financial statements. These reconciliations are useful to readers in understanding the long-term impact of the Board's short-term financing decisions.

Fiduciary Funds - Fiduciary funds are used to account for assets held by the Board in a trustee capacity or as an agent for others. Activities from fiduciary funds are not included in the government-wide financial statements because the Board cannot use these assets for its operations. Fiduciary funds of the Board, consisting of custodial funds and a private-purpose trust fund, are reported in the *Statement of Fiduciary Net Position* using an accrual basis of accounting. Custodial funds held by the Board involve only the receipt,

temporary investment, and remittance of resources to individuals, private organizations, or other governments in a purely custodial capacity (assets equal liabilities). The custodial funds reported by the Board consist of student organization accounts such as clubs and classes. Private-purpose trust funds - also reported in a *Statement of Changes in Fiduciary Net Position* - report all trust agreements under which principal and income benefit individuals, private organizations, or other governments. The private-purpose trust fund reported by the Board is a scholarship fund for students.

Notes to the Basic Financial Statements - The *notes to the basic financial statements* provide additional information that is essential for the statements to fairly represent the Board's financial position and its operations. The notes contain important information that is not part of the basic financial statements. However, the notes are an integral part of the statements, not an appendage to them.

After the presentation of the basic financial statements, additional supplemental information is required to be presented following the *notes to the basic financial statements*. The required supplemental information provides a comparison of the original adopted budget to the final amended budget of the Board's General Fund, which is then further compared to the actual operating results for the fiscal year. The comparison of this data allows users to assess management's ability to project and plan for its operations throughout the year.

Illustrated District-Wide Statement of Net Position

**CITY SCHOOL SYSTEM
STATEMENT OF NET POSITION
SEPTEMBER 30, XXXX**

	Governmental Activities
ASSETS	
Current assets	
Cash and cash equivalents	\$ 19,653,119
Accounts receivable, net	40,586
Property tax receivable	5,401,793
Due from other governments	817,714
Inventories	121,361
Total current assets	<u>26,034,573</u>
Capital Assets not being depreciated	
Land and improvements	8,859,215
Construction in progress	657,516
Total capital assets not being depreciated	<u>9,516,731</u>
Capital Assets	
Land improvements	3,598,969
Buildings and improvements	104,540,193
Furniture, equipment and vehicles	12,546,078
Less accumulated depreciation	<u>(34,092,923)</u>
Total depreciable capital assets, net of depreciation	<u>86,592,317</u>
Total assets	<u>122,143,621</u>
LIABILITIES	
Accounts payable	921,985
Deferred revenues	5,715,276
Salaries and benefits payable	3,746,414
Obligations under capital leases - due in less than 1 year	672,252
Obligations under capital leases - due after 1 year	1,294,377
Total liabilities	<u>12,350,304</u>
NET POSITION	
Invested in capital assets, net of related debt	94,142,419
Restricted for	
Capital projects	891,588
Other projects	1,891,565
Unrestricted	12,867,745
Total net position	<u>\$ 109,793,317</u>

**CITY SCHOOL SYSTEM
STATEMENT OF ACTIVITIES
SEPTEMBER 30, XXXX**

Functions/Programs	Expenses	Program Revenues			Net (Expenses)
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Revenues and Changes in Net Position
					Total Governmental Activities
Governmental activities					
Instruction	\$ 41,907,026	\$ 1,141,985	\$ 24,433,670	\$ 501,124	\$ (15,830,247)
Instructional support	12,273,077	422,223	5,729,013	113,887	(6,007,954)
Operation and maintenance	5,484,664	115,222	1,138,907	774,098	(3,456,437)
Auxiliary services					
Student transportation services	3,294,864	143,501	2,072,036	306,871	(772,456)
Food services	3,515,856	2,776,150	154,754	-	(584,952)
General administrative services	2,762,156	4,696	438,238	-	(2,319,222)
Other	1,047,261	749,679	296,402	-	(1,180)
Interest and fiscal charges	27,363	-	-	-	(27,363)
Total governmental activities	<u>\$ 70,312,267</u>	<u>\$ 5,353,456</u>	<u>\$ 34,263,020</u>	<u>\$ 1,695,980</u>	<u>(28,999,811)</u>
General revenues					
Taxes					
					11,349,945
					5,361,188
					523,749
					55,015
					2,080
					9,550,759
					127,803
					423,701
					<u>27,394,240</u>
					(1,605,571)
					<u>111,398,888</u>
					<u>\$ 109,793,317</u>

**CITY SCHOOL SYSTEM
BALANCE SHEET
SEPTEMBER 30, XXXX**

	<u>General Fund</u>	<u>Capital Projects Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
ASSETS				
Cash and cash equivalents	\$ 10,517,702	\$ 4,252,442	\$ 4,882,975	\$ 19,653,119
Accounts receivable, net	29,948	6,513	4,125	40,586
Due from other governments	622,599	30,677	164,438	817,714
Inventories	-	-	121,361	121,361
Total assets	<u>\$ 11,170,249</u>	<u>\$ 4,289,632</u>	<u>\$ 5,172,899</u>	<u>\$ 20,632,780</u>
LIABILITIES AND FUND BALANCES				
Liabilities				
Accounts payable	\$ 318,929	\$ 479,770	\$ 123,286	\$ 921,985
Deferred revenue	-	-	313,483	313,483
Salaries and benefits payable	3,459,381	-	287,033	3,746,414
Total liabilities	<u>3,778,310</u>	<u>479,770</u>	<u>723,802</u>	<u>4,981,882</u>
Fund balances				
Nonspendable	-	-	121,361	121,361
Restricted	-	891,588	1,770,204	2,661,792
Committed	-	-	2,701,509	2,701,509
Assigned	132,404	2,918,274	-	3,050,678
Unassigned	7,259,535	-	(143,977)	7,115,558
Total fund balances	<u>7,391,939</u>	<u>3,809,862</u>	<u>4,449,097</u>	<u>15,650,898</u>
Total liabilities and fund balances	<u>\$ 11,170,249</u>	<u>\$ 4,289,632</u>	<u>\$ 5,172,899</u>	<u>\$ 20,632,780</u>

CITY SCHOOL SYSTEM
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND
BALANCES – GOVERNMENTAL FUNDS
SEPTEMBER 30, XXXX

	General Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
REVENUES				
State	\$ 31,099,426	\$ 1,690,671	\$ 1,000	\$ 32,791,097
Federal	73,688	-	4,344,583	4,418,271
Local	27,241,993	9,597	4,092,717	31,344,307
Other	176,482	-	157,557	334,039
Total revenues	<u>58,591,589</u>	<u>1,700,268</u>	<u>8,595,857</u>	<u>68,887,714</u>
EXPENDITURES				
Current				
Instruction	36,492,694	456,299	3,816,193	40,765,186
Instructional support	10,675,629	594,745	1,036,259	12,306,633
Operation and maintenance	4,665,100	658,495	126,720	5,450,315
Auxiliary services	3,336,550	306,871	3,946,910	7,590,331
General administrative services	2,546,672	14,979	258,426	2,820,077
Other	474,244	322	792,621	1,267,187
Capital outlay	-	5,477,068	-	5,477,068
Debt services				
Principal retirement	817,553	-	-	817,553
Interest	27,365	-	-	27,365
Total expenditures	<u>59,035,807</u>	<u>7,508,779</u>	<u>9,977,129</u>	<u>76,521,715</u>
Excess (deficiency) of revenues over expenditures	<u>(444,218)</u>	<u>(5,808,511)</u>	<u>(1,381,272)</u>	<u>(7,634,001)</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	135,831	-	1,319,455	1,455,286
Proceeds from the sale of assets	13,084	-	2,165	15,249
Indirect cost	219,684	-	-	219,684
Other sources	35,533	-	1,425	36,958
Transfers out	(1,319,455)	-	(135,831)	(1,455,286)
Proceeds from the issuance of debt	1,904,630	-	-	1,904,630
Total other financing sources (uses)	<u>989,307</u>	<u>-</u>	<u>1,187,214</u>	<u>2,176,521</u>
Net changes in fund balances	545,089	(5,808,511)	(194,058)	(5,457,480)
Fund balances, beginning of year	<u>6,846,850</u>	<u>9,618,373</u>	<u>4,643,155</u>	<u>21,108,378</u>
Fund balances, end of year	<u>\$ 7,391,939</u>	<u>\$ 3,809,862</u>	<u>\$ 4,449,097</u>	<u>\$ 15,650,898</u>

Application of GASB Statement 34 to Activity Funds

GASB Statement 34 made significant changes in financial reporting for all governments, including school districts. **Remember that the purpose of the government-wide statements is to provide a broad overview of the entity.** Because fiduciary fund resources are not available for use by the government, fiduciary activities are excluded from the entity-wide financial statements. In accordance with the new reporting model, fiduciary activities, including **student activity funds, are reported only in the fund financial statements.** The impact of Statement 34 student activity funds is summarized below:

- If student activity funds are classified as fiduciary (agency – Fund 32) funds as recommended, they are **not reported in the government-wide financial statements.** Instead, these balances are **reported only** in the fund financial statements.
- District activity funds that are classified as governmental (special revenue – Fund 12) funds are consolidated with all governmental activities in the government-wide financial statements. District activity funds will also be presented in the governmental fund financial statements.
- Fiduciary funds are presented in the fund financial statements by fund type. **Student activity funds, as custodial funds, report no operating activity and are, therefore, presented only in the statement of fiduciary fund net position.**

GASB # 34 APPLICATION TO STUDENT ACTIVITY FUNDS

- **Student activity funds are classified as fiduciary (agency) funds and are not included in government wide financial statements.**
- **Student activity funds are reported only in the fund financial statement of fiduciary fund net position.**

In conclusion, **financial reporting within the local schools plays an important role in demonstrating accountability and transparency to the various stakeholders of the local education agency as well as the school.** This includes the students, parents, employees, vendors, taxpayers, and other stakeholders of the publicly funded entity. School officials and staff are in a position of public trust and should be held accountable for that trust. Through adherence to a sound internal control system, following related financial reporting policies and procedures, and ensuring personal integrity in their position, school bookkeepers play an important and vital part in ensuring that public trust.