Michigan School Accounting Manual Referent Group's
Supplemental Guidance on GASB 34
Initial Publication January 26, 2001
Revised February 2007

Introduction -

This guidance is designed to communicate information related to Michigan School Accounting Manual Referent Group's guidance to public schools implementing GASB-34 on Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments. In order to be in compliance with Generally Accepted Accounting Practices (GAAP), school districts will be required to implement GASB-34. Statement 34 establishes new requirements for the annual financial reports of state and local governments. The statement was developed to make annual reports easier to understand and more useful to the people who use governmental financial information to make decisions.

The Statement will be phased in over the course of three years depending upon a local unit of government's 1998-99 total revenues (excluding other financing sources). The first phase governments, those with $100 million or more in total revenues, will be implementing for the fiscal year ending June 30, 2002; phase two governments, those with total revenues between $10 million and $100 million, will be implementing for the fiscal year ending June 30, 2003; and phase three governments, those with less than $10 million in total revenues, will be implementing for the fiscal year ending June 30, 2004.

The Michigan School Accounting Manual Referent Group has developed guidance for Michigan public school districts. It was designed to supplement (not replace) Governmental Accounting Standards Board's *Guide to Implementation of GASB Statement 34 on Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments and the Association of School Business Officials GASB Statement No. 34 Implementation Recommendations for School Districts*. We strongly recommend that in addition to this guidance, each school district obtain copies of the GASB and ASBO documents. The GASB Implementation Guide may be obtained at the following address:

GASB
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116
Phone Number 1-800-748-0659

In addition there is a recently released GASB manual titled, *What you Should Know-About Your School District's Finances - A Guide to Financial Statements*. It is also available at the address listed above.

The ASBO implementation guide may be obtained from:

ASBO International
11401 North Shore Dr.
Reston, VA 20190-4200
Phone: (703)478-0405
website: www.asbointl.org
ISBN No. 0-910170-81-9

The Michigan guidance follows the Table of Contents found in the ASBO guide. Issues will be numbered by chapter and then by order of action; for example, the second issue resolved from Chapter One would be labeled Issue I-2. We anticipate that issues will continue to emerge as districts begin to implement the new standard. In addition, some of our early recommendations may be modified, as better information becomes available. For this reason, each issue and recommendation will be labeled with the date the most recent information was added.

The website for the MDE supplemental guidance is:

www.state.mi.us/mde/off/stateaid/gasb34.htm

Chapter One - Management′s Discussion and Analysis (MD&A)

The MD&A will provide an analysis of the school district′s overall financial position and operating results. Its purpose is to help financial statement users assess if the district's financial position has improved or deteriorated. The analysis must include a comparison of the current year to prior year based on the district-wide financial information about assets, liabilities, revenues, and EXPENSES. In addition, the analysis will explain significant variations in fund-based financial results and budgetary information and will describe capital asset and long-term debt activity during the year. The MD&A will include a description of currently known facts, decisions, or conditions expected to have a significant effect on the future financial position and results of operations of the school districts.

The following guidance is for clarification of specific issues for Michigan School Districts regarding MD&A.

<u>ISSUE I-1</u> Comparison Data In Year 1 (Date Updated 12/31/00)

GASB #34 requires comparative financial data be included in the MD&A in the year of implementation, comparative data for the prior year does not readily exist, but GASB encourages the inclusion of this data.

<u>RECOMMENDATION I-1</u> (Date Updated 12/31/00)

The committee recommends that Districts not devote the time and effort to establish prior year data in the year of implementation. A statement to the effect that prior year data is not available but will be provided in subsequent years must be included in the MD&A in the first year of implementation.

Chapter Two - District-wide Financial Statements

... Perhaps the most notable feature of the new model is the requirement for district-wide financial statements. The focus is on the school district as a whole rather than on individual funds. The district-wide statements must be prepared on an ACCRUAL basis of accounting for all the activities of the district. Under the accrual basis, all revenues and costs of providing services are reported, not just those received or paid in the current year or soon thereafter. This approach moves governmental accounting closer to financial reporting in the private sector…

The following guidance is for clarification of specific issues for Michigan School Districts regarding district-wide financial statements:

<u>ISSUE II-1</u> Level of Detail for Statement of Activities (Date Updated 12/31/00)

One of the objectives to be accomplished by GASB-34 implementation is to display program or activity reporting. GASB guidance was primarily established by looking at municipalities that perform more than one function as an entity. For example, municipalities may provide water/sewage functions, public safety, parks and recreation, etc. School districts are different in that they basically have one primary function, to educate children.

<u>RECOMMENDATION II-1</u> (Date Updated 12/31/00)

At this point in time, the committee believes that program reporting is not a feasible option. Data collected at that level would be inconsistent and inaccurate for most districts. For this reason, the referent group recommends the Statement of Activities display minimum reporting by major function area (instruction, support services, food services, etc.) rather than by program area (special education, Title I, etc.) This merely establishes the <u>minimum</u> level of reporting required of Michigan public school districts. It does not prohibit districts from providing more detailed program level information in their reports.

See Figure 2-2 Sample Statement of Activities

<u>ISSUE II-2</u> Allocation of Indirect Expenses (Date Updated 12/31/00)

GASB-34 allows for extensive allocation of indirect expenses. ASBO recommends not doing this since it may serve to confuse rather than aid the reader.

<u>RECOMMENDATION II-2</u> (Date Updated 12/31/00)

The referent group recommends adopting the ASBO recommendation. We do not encourage indirect expense allocation.

ISSUE II-3 Allocation of Depreciation (Date Updated 12/31/00)

GASB-34 requires allocation of depreciation whenever the capital asset can be identified as being associated with a specific function. When the asset is associated with multiple functions, allocation of depreciation by function is allowed or reported as part of a separate line entitled "UNALLOCATED Depreciation." ASBO recommends using the "UNALLOCATED Depreciation" line whenever possible.

RECOMMENDATION II-3 (Date Updated 12/31/00)

The referent group encourages districts to allocate depreciation to functions whenever possible. If an asset is truly multi-functional, to the extent it is not reasonable to allocate the portion of depreciation attributable to a given function, districts should adopt the ASBO recommendation to use the Unallocated Depreciation line. To be exempt from allocation, the capital asset must be truly multi-functional.

See Discussion on Page 45 of ASBO Guide for further clarification.

See Chapter 4 - Issue IV-3 for a discussion on the allocation of depreciation expense.

Practical Tip Remember that GASB #34 requires that depreciation for single purpose assets must be allocated to the appropriate function. The district's capital asset footnote disclosure will disclose the allocation by function. So, care must be taken to identify those assets (for example - depreciation on classroom equipment - allocated to instruction) where it is clear that they are not multi-purpose.

ISSUE II-4 Should the Balance Sheet be classified as Current and Non Current or in the liquidity format? (Date Updated 12/31/00)

GASB-34 allows both formats. ASBO recommends the classified format.

RECOMMENDATION II-4 (Date Updated 12/31/00)

The referent group encourages districts to adopt the ASBO recommendation to use the classified format; however MDE will accept either format.

See figure 2-1 - Sample Statement of Net Assets

<u>ISSUE II-5</u> What are the typical items for Michigan districts that would be treated as Restricted Net Assets? (Date Updated 12/31/00)

GASB-34 requires the use of the caption Restricted Net Assets. This is not the same as reserved/designated. What should be shown in this section?

<u>RECOMMENDATION II-5</u> (Date Updated 12/31/00)

Net Assets should be reported as restricted when constraints placed on net asset use are EXTERNALLY imposed by creditors, grantors, contributors or law or regulations of OTHER governments. Examples of restricted net assets are as follow:

Net Assets Attributed to:	Generally Restricted	Generally Not Restricted
Debt Levies	X	
Bond Issues (including Durant Bonds)	X	
Board Designations for Future Plans		X
Bequests and Gifts	X	

<u>ISSUE II-6</u> For a Michigan district what are program revenues vs. general revenues? (Date Updated 12/31/00)

GASB-34 requires revenues to be identified by program (i.e., federal aid, state categorical aid, etc.) It also states that property taxes are almost always general revenue. What happens with Act 18 (County Special Education) tax revenue at the K-12 level? What other revenues for Michigan districts will need clarification as to their source as Program or General?

<u>RECOMMENDATION II-6</u> (Date Updated 12/31/00)

The ASBO guide has an excellent table to assist with the answer to this question. See ASBO Figure 2-3 on page 25 of the guide.

Payments from the State are reflected on the Monthly State Aid Status Report. It is the intention of the MDE to indicate the category " General Revenue or Program Revenue " on the status report for each revenue item paid by the State.

Payments of Federal Government Grant Revenue must be reviewed individually to determine the specific nature of the grant. In almost all cases, Federal Grant Revenue will be program revenue. See Issue II-7 for a discussion of how to allocate Federal program revenue between functions.

The following table is designed to assist Michigan districts identify other program and general revenues:

Reference	Revenue Source	Program Revenue	General Revenue
	County Special Ed Tax Levies (Act 18)	Generally	Potentially
	County Vocational Ed Tax Levies	Generally	Potentially
	Food Service Sales	Always	
	User Fees (Gate Receipts, Community Ed, Daycare)	Always	
	Other Local Revenue Such As Library Revenue	Always	

ISSUE II-7 Once a federal grant revenue is identified as a program revenue, how is it allocated by function? (Date Updated 12/31/00)

Most federal grant revenues will be identified as program revenues rather than general revenues. This program revenue must be allocated between Instruction, Support Services, Community Services, Food Service and Athletics, if these functions are shown separately.

RECOMMENDATION II-7 (Date Updated 12/31/00)

There appears to be no rule of thumb or chart that will tell the district how to allocate federal grant revenue by function. Each district will have to review each grant and determine the specific allocation by function.

Practical Tip   The federal grant budget will classify the expenditures by function (100's, 200's, etc.) The revenue can be allocated the exact same way.

Practical Tip   At the time the federal grant is applied for, the allocation of revenue by function can be determined. If the district modifies its chart of accounts to capture the revenue amounts by function, no further allocation efforts should be necessary at year-end.

<u>ISSUE II-8</u> How are transfers to other governmental units handled on the Government Wide financial statements? (Date Updated 12/31/00)

While it is clear that interfund transfers are eliminated on the Government Wide Statement of Activities, there remains the question of how to classify such items as County Special Education payments which have historically been considered as "transfers" by the MDE.

<u>RECOMMENDATION II-8</u> (Date Updated 12/31/00)

Discussions with the GASB staff confirms there are basically no transfers reflected on the Government Wide Statement of Activities. Transactions such as the County Special Education payments are treated as "intergovernmental revenue" at the K-12 level (either as program or general revenue based on applying the criteria on a case by case basis) and as program expense at the ISD level. There really is no difference in the nature of revenue received from the County, State or Federal government.

<u>ISSUE II-9</u> Should principal and Interest related to the school bond loan fund be included in the computation of investment in capital assets, net of related debt? (Date Updated 1/14/02)

<u>RECOMMENDATION II-9</u> (Date Updated 02/26/07)

The MDE 1996 *Michigan School Audit Manual*, Section E discussed the accounting for school bond loan transactions. The conclusion, after consultation with GASB at that time, was as follows:

We do not believe it is appropriate to recognize accrued interest expenditures (offset by an other financing source) in a flow of current financial resources operating statement. The amounts so recognized are neither increases nor decreases in expendable available financial resources. Further, this reporting results in double counting of interest, once when annually accrued and again when actually paid. Finally, under current generally accepted accounting principles, interest on general long-term debt is usually required to be reported as an expenditure when payment is due. Because repayment is not based on any definitive, established due dates, but rather on the availability of whatever excess property taxes remain after satisfaction of bonded debt service, we believe interest is best recognized when payment is made.

Therefore, we believe the preferable method of reporting accrued interest on school bond loans is to report the annual accruals as a GLTDAG liability. This accounting is comparable to accounting for deep-discount or capital appreciation debt.

So it has previously been established that School Bond Loan Debt is treated like capital appreciation bonds and therefore it is logical to include this debt in the computation of “investment in capital assets, net of related debt.”

This issue was also discussed recently with GASB. They believe the school bond loan fund was part of the original financing plan of the district and therefore believe the preferable method of reporting is to include the principal and accrued interest in the computation of *investment in capital assets, net of related debt.* See question number 87 of the GASB implementation guide for further guidance to this issue.

Practical tip: This may result in a negative balance where the debt and accrued interest is greater than the net capital assets.

Question number 87 of the GASB implementation guide answer was changed. It is now 7.124 as reported below:

7.124. *Q*— A government accrues and reports a long-term liability for accretion of interest on deep-discount (capital appreciation) debt that was issued for the construction of general governmental capital assets. Which component of net assets should be reduced by the liability? (87)

A—Accrued interest on any capital-related debt, including deep-discount debt, generally should not be included in the computation of the *invested in capital assets, net of related debt* component of net assets. The amount of the “borrowing attributable to the acquisition, construction, or improvement” of a capital asset is the proceeds, rather than the total amount, including interest, that will be paid at maturity. Generally, the accrued interest liability would be included in unrestricted net assets. However, if the government has established a “sinking” fund to accumulate cash to pay off the debt at maturity, the accrued interest would be included in (reduce) the same component of net assets as the sinking fund resources.

Based on this change in answer by the GASB, the committee believes interest on the school bond loan fund should be treated the same as accretion of interest on deep-discount (capital appreciation) bonds.

The second question to be considered is what type of debt is the actual principal outstanding of the school bond debt?

The committee believes there are two options now concerning the outstanding principal of the school bond loan fund debt.

The first is to consider the school bond loan debt as <u>not</u> capital related debt.

The second consideration is to treat the amount of school bond loan debt outstanding which replaces the original capital related debt, as capital related debt up to the amount of the original debt issue, similar to how an advance refunding of debt would be recorded.

The committee recommends that the districts disclose in the footnotes how school bond loans were treated in the calculation of net assets.

Chapter Three - Fund Financial Statements

...Because the users of financial information continue to assess compliance with finance-related laws, rules, and regulations, Statement 34 requires districts to continue to present financial statements with information about funds. The focus of these fund-based statements has been sharpened, however, by requiring districts to report information about their most important or *major* funds, including the district's general fund. Districts will continue to provide budgetary comparison information in their annual reports. An important change, however, is a requirement to add the district's original budget to the current comparison of final budget-to-actual results.

The following guidance is for clarification of specific issues for Michigan school districts regarding Fund Financial Statements.

<u>ISSUE III-1</u> Reporting Major/Non-Major Funds (Date Updated 12/31/00)

The examples on page 28 & 29 of the guide (Figures 3-1 & 3-2) show a column for other governmental funds.

<u>RECOMMENDATION III-1</u> (Date Updated 12/31/00)

It is recommended combining schedules of the other governmental funds not meeting the definition of a major fund, be included in the annual report.

<u>Practical Tip</u>:
The Michigan Department of Education (MDE) knows certain funds, by GASB 34 definition, may go from major to non-major (or vice versa) from year to year. An example of this could be a capital projects fund. During the initial year, the fund may be a major fund, subsequent years activity may not be significant enough to qualify as a major program. For various reasons, providing the individual capital project fund detail in annual reports as a major fund each year could be very helpful. Page 28 of the ASBO guide also permits this. The guide refers to chapter 6 for further guidance.

<u>ISSUE III-2</u> Business Type Activity Reporting (Date Updated 12/31/00)

The guide shows adult education and food service as business-type activities.

<u>RECOMMENDATION III-2</u> (Date Updated 12/31/00)

It is generally understood in Michigan that adult education, latch key, and food service programs do not meet the proprietary fund definition as included on page 32 of the guide. The use of business type activities will be rare for local public schools. Intermediate school districts may have business type activities. For statewide consistency, the definition on page 32 should be used in making this decision. Please keep in mind the costs of depreciation and debt service need to be included in this decision making process.

<u>ISSUE III-3</u> Budgetary comparisons (Date Updated 06/06/03)

The guide requires budgets for the general fund and major special revenue funds.

<u>RECOMMENDATION III-3</u> (Date Updated 06/06/03)

Districts are required to follow current state budgeting requirements as cited in MCL 141.422a. This requires local school boards to adopt a budget for the general fund and all special revenue funds. Following GAAP, districts that have not implemented GASB-34 are required to report in their annual financial statements budget to actual comparisons for the general fund and all special revenue funds. Districts that have implemented GASB-34 are required to report budget to actual comparisons for the general fund and ONLY major special revenue funds.

<u>ISSUE III-4</u> GASB #33 Impact on Fund Level Revenue Recognition (Date Updated 1/14/02)

GASB #33 "Accounting and Financial Reporting for Non-exchange Transactions" eliminates the revenue recognition rule for grants established in NCGA Statement #2. This revenue recognition rule stated that revenue should be recorded at the time of the expenditure- without regard to consideration of when received. GASB #33 is effective for FYE 6/30/01 and after.

<u>RECOMMENDATION III- 4</u> (Date Update 1/14/02)

With the elimination of the revenue recognition rule for grants (NCGA Statement #2), all nonexchange revenue at the fund level is recognized in the accounting period when it becomes available and measurable. Available is defined as "collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period."

This revenue recognition rule (available and measurable) has previously existed for all nonexchange revenue except for grant revenue. Therefore, the district currently has a policy in place that defines availability. GASB #33 simply makes grant revenue fall under the same definition.

Practical Tip - GASB #38 (footnotes) will require the district to disclose their definition of Aavailable in the footnotes.

Practical Tip - To assure that certain grant funds meet the "availability" criteria, we suggest that the districts promptly request reimbursement of funds as they are expended.

<u>ISSUE III-5</u> Interpretation #6 Impact on Fund Level Liability Recognition (Date Updated 8/8/03)

Interpretation #6 - Recognition and measurement of certain liabilities and expenditures in Governmental Fund Financial Statements is effective at the same time a District is required to implement GASB #34. One of the provisions of Interpretation #6 covers Governmental Fund liabilities and expenditures for claims and judgments, compensated absences and special termination benefits. It states these liabilities should be recognized in a governmental fund to the extent the liabilities are "Normally expected to be liquidated with expendable available financial resources." In general, Districts are normally expected to liquidate liabilities with expendable available financial resources to the extent that the liabilities <u>Mature</u> (come due for payment) each period.

<u>RECOMMENDATION III-5</u> (Date Updated 08/08/03)

In all cases, the criterion for modified accrual recognition of a liability in a Governmental Fund is whether and to what extent the liability has matured, independent of the method and timing of resource accumulation.

The purpose of an interpretation is to clarify previously issued pronouncements. Districts should review, along with their auditor, their policy for recording these liabilities in their governmental funds as they implement GASB #34. . See Section II, Accounting Issue E.01 of the *Michigan Public School Accounting Manual* for further guidance on accounting for various liabilities.

ISSUE III-6 Accounting for Trust and Agency Funds Under GASB Statement #34 (Date Updated 5/7/03)
GASB-34 has made changes in the treatment of Trust Funds.
Background- Trust and Agency Funds are treated under GASB #34 as follows:
Guidance GASB #34, Paragraph 65 and 72- Implementation Guide question 172.

Type of Fund	Old Rules	New Rules	B1022 Fund Number
Student Activity	Fiduciary Fund/Agency Fund	Fiduciary Fund/Agency Fund	61-69
Expendable Trust – Not Used to Support Operations/Programs	Fiduciary Fund/Trust Fund	Fiduciary Fund/Private Purpose Fund-The consensus of the B1022 Committee was in most instances "expendable trust funds do not support the district's activities and would be reported as private purpose funds."	51-59
Expendable Trust – Used to Support Operations/Programs	Fiduciary Fund/Trust Fund	Special Revenue Fund- GASB Statement #4 paragraph 72 states that private purpose trust funds should be used to report all other trust arrangements under which principal and income benefit individuals, private organizations, or other governments. In situations where the district believes their activities do support the district, question #172 of the AICPA implementation guide would allow these activities to be reported in a special revenue fund. (Usually do not support operations.)	28
Non-Expendable Trust Fund Used to Support Operations/Programs	Fiduciary Fund/Trust Fund	Permanent Fund – This is a new fund. An example of an activity which supports the district's programs is as follows: A band fund tracks investments donated by a local resident who stipulates that only the earnings of the investments may be used to purchase musical instruments for the district. Permanent funds are considered governmental funds.	51-59
Non-Expendable Trust Fund Not Used to Support Operations/Programs	Fiduciary Fund/Trust Fund	Fiduciary Fund/Private Purpose Fund. The consensus of the 1022 committee was non-expendable trust funds which only use investment earnings for scholarships or other external activities do not support district activities and therefore should be reported as private purpose funds per paragraph #65 of GASB Statement #34.	51-59

RECOMMENDATION III-6 (Date Updated 5/7/03)

Student Activity funds- Agency Funds (Use Fund Codes 61-69.)
Required Reports:
Statement of Fiduciary Net Assets
Practical Consideration- Many districts record immaterial trust funds in their agency funds. Consult with your auditor to see if this will be permissible in the future.

Expendable Trust Funds that generally do not support district operations
Private Purpose Trust Funds (Use Fund Codes 51-59)
Required Reports:
Statement of Fiduciary Net Assets
Statement of Changes in Fiduciary Net Assets

Expendable Trust Funds that generally do support district operations

Alternative- Special Revenue Fund (Fund Coder 28) when activities support district operations. Under GASB #34 the term *expendable trust* is no longer used.

Not Supporting Operations-

Private Purpose Trust Funds (Fund Codes 51-59)
Required Reports:
Statement of Fiduciary Net Assets
Statement of Changes in Fiduciary Net Assets

Non-Expendable Trust Funds-
Supporting Operations/Programs

Permanent Fund which is a governmental fund (Fund Codes 51-59)
Note: Under GASB #34 the term *non-expendable* trust is no longer used.
Required Reports:
Fund level Balance Sheet- likely non-major and part of the combining non-major statement in additional information section of the reports.
Fund level Revenue/Expenditure Statement-likely non-major and part of the combining non-major statement in additional information section of the reports.

Chapter Four - Capital Assets and Depreciation

Background:

Prior to GASB-34, many school districts did not maintain a general fixed asset account group (GFAAG). In lieu of maintaining GFAAG, districts chose to have a qualified opinion issued by their auditors.

GASB-34 does away with GFAAG. Instead of GFAAG, districts will have to maintain an accounting for capital assets. In addition, districts will have to calculate annual depreciation expense, maintain a record of accumulated depreciation for capital assets and calculate the gain/loss on the sale of capital assets.

Under GASB-34 it is highly improbable that the district's auditors will accept the omission of capital assets, annual depreciation expense, accumulated depreciation and gain/loss on sale of capital assets as being immaterial to the financial statements taken as a whole. As a result, districts run the risk of an adverse opinion from their auditors. In other words, a district which chooses NOT to comply with GASB-34 requirements for maintaining capital assets, annual depreciation expense and accumulated depreciation expense will likely receive an auditor's opinion with language similar to the following:

> ...the financial statements do NOT present fairly, in all material respects, the financial position of the XXX School District at June 30, 20XX...

In addition, a letter dated October 26, 2000 from Elaine Madigan Mills of the Michigan Department of Education states:

> MDE will require financial statements received from public schools to follow GASB-34 requirements.

<u>ISSUE IV-1</u> Capital Asset Valuation (Date Updated 12/31/00)

What do I need to do to get ready for GASB-34 as it relates to capital assets, accumulated depreciation, etc.?

<u>RECOMMENDATION IV-1</u> (Date Updated 12/31/00)

The ASBO Guide on pages 39 and 40 provides nine steps for compliance with GASB-34. The referent group recognizes that for many districts these nine steps may be the most costly of all steps needed to implement GASB-34. The referent group recommends that districts plan carefully how they will implement these requirements of GASB-34. Districts may have to budget additional district resources to meet the GASB-34 requirements during the first year of implementation.

ISSUE IV-2   Which assets should be capitalized? (Date Updated 12/31/00)

RECOMMENDATION IV-2 (Date Updated 12/31/00)

A universal definition of a capital asset is an asset that has an estimated useful life of greater than one (year). Per the ASBO Guide, assets that are consumed, used up, habitually lost or worn out in one year or less should not be capitalized. The asset cost will also be used in determining whether or not to capitalize an asset. ASBO recommends that school districts establish a capitalization threshold that ensures that at least 80 percent of the value of assets (with useful lives greater than one year) is reported; however, the threshold should not be greater than $5,000 (the federal threshold). The ASBO Guide further states that even for the smallest districts a capitalization threshold of $1,000 should provide the district with at least 80 percent coverage.

The Referent Group advised districts to consider the following:

The lower the capitalization threshold the greater the cost to:

a) Construct initial capital asset records (i.e., the more assets that need to be counted, the greater the cost to count)
b) Maintain ongoing depreciation and accumulated depreciation records (i.e., the more assets that are counted, the more assets that will have to be depreciated)
c) Keep accurate records of gain or loss on sale of capital assets

The capitalization threshold for GASB-34 financial reporting purposes may also impact the district′s fund statements, fund budgeting process and insurance records as well as the district′s government wide financial statements.

Further considerations include:

a) Uniform capitalization policy for government wide statements, fund level statements and budgeting.

Some districts may wish to use the same capitalization threshold for reporting and budgeting for capital assets in the general, special revenues or capital project funds.

Advantages: Consistency for all reporting. Simplicity.

Disadvantages: Impact on fund budgets and financial reporting. A change in the capitalization policy may impact a district′s budget, e.g., requiring more/less budget for capital outlay and more/less budget for supplies and materials or non-capital equipment lines.

b) Multi-tier capitalization policies

Alternatively, districts may wish to maintain more detailed records for insurance and fund reporting purposes than is required or recommended for GASB-34 government wide financial reporting purposes.

The following table is the recommended capitalization threshold for Michigan School Districts for both accounting (GASB 34) and asset inventory/control purposes:

GASB-34 Reporting Requirements (Accounting)

Impacts the following:

> Government-wide financial statements. Capital assets recorded at actual or estimated cost. Capital assets are depreciated and reported net of accumulated depreciation.
>
> Fund Budgeting. For example: general fund, special revenue funds, budgets and financial reports and capital outlay fund financial reports.

Capital assets are recorded at cost.

GASB 34 Compliance Assets Capitalized for:	Large District (Greater than $10 Million Annual Revenue)	Small District (Less than or equal to $10 Million Annual Revenue)
Construction/Buildings/Additions Furniture & Fixtures/Equipment	$ 5,000 Threshold	$1,000 Threshold

For insurance and inventory control reporting purposes, capital assets and other equipment should be identified at their replacement value.

<table>
<tr><td>Insurance, Accountability, and Control</td><td>Large District
(Greater than $10 Million Annually Budgeted)</td><td>Small District
Less than or equal to $10 Million Annually Budgeted</td></tr>
<tr><td>Construction/Buildings/Additions
Furniture & Fixtures/Equipment</td><td>$ 5,000 Threshold</td><td>$1,000 Threshold</td></tr>
<tr><td>Equipment with a replacement cost less than $5,000/$1,000</td><td colspan="2">For insurance purposes, large and small districts should maintain adequate records of all capital assets as well as many other assets that are of significant value and may be subject to theft or loss, e.g., computers, peripheral equipment and other electronic equipment (i.e.: not formally capitalized, but still inventoried)</td></tr>
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ISSUE IV-3 Reporting Depreciation Expense (Date Updated 12/31/00)

How is depreciation expense and accumulated depreciation reported on the government wide financial statements? (Page 45 of ASBO Guide)

Background:

GASB-34 paragraph 44 states: Depreciation expense for capital assets that can specifically be identified with a function should be included in its direct expense. However, the same paragraph of GASB-34 further states: Depreciation expense for capital assets... that serve all functions is not required to be included in the direct expenses of the various functions. How much detail a district chooses to report on its government wide financial statements will impact how much it should attempt to allocate depreciation.

RECOMMENDATION IV-3 (Date Updated 12/31/00)

The ASBO Guide ...recommends not allocating the depreciation expense of a building that serves multiple (that is more than just a few) functions. The referent group concurs that it would be impractical to allocate depreciation to the various functions that may be housed in a typical school. For example, a high school may house classroom instruction (function 113), counselors (function 212), principals (function 241), librarians (function 222) and other staff such as custodians, central administrators, athletics and community or adult education.

ISSUE IV-4 What should be included in the Management Discussion and Analysis regarding Capital Assets?

RECOMMENDATION IV-4 Management Discussion and Analysis (Date Updated 12/31/00)

1. Minimum requirements per GASB-34 paragraph 11
   a. Description of Significant Capital Assets
   b. Illustrate changes, net of depreciation, by asset type
   c. Disclose any other currently known facts that could have a significant impact on capital assets. Such as a material gain or loss on a sale (Yes, for the GASB-34 financials you do need to keep track of gains and losses.)

ISSUE IV-5 What Should Be Included In General Disclosure Requirements (i.e., Footnotes After Financial Statements) regarding Capital Assets?

RECOMMENDATION IV-5 (Date Updated 12/31/00)

Fixed asset capitalization policy
Disclose amount of depreciation allocated to function codes
Discussion of construction in progress
Future Capital Asset spending plans
Disclose material capital acquisitions, sales or other dispositions
a. Including gains and losses
b. Discussion of construction in progress
c. Future Capital Asset spending plans

ISSUE IV-6 Asset Lives (Date Updated 12/31/00)

GASB-34 states in paragraph 21 that Capital assets should be depreciated over their estimated useful lives. Paragraph 161 states: For estimated useful lives, districts may use: general guidelines obtained from professional or industry organizations, information for comparable assets of other governments or internal information.

The *GASB Guide to Implementation of GASB Statement 34 on Basic Financial Statements* in question 47 further states:

> Useful lives should be based upon the government's own experience and plans for the assets. Although comparison with other governments or other organizations may provide some guidance, property management practices, asset usage, and other variables (such as weather) may vary significantly between governments. In determining useful life, a (district) also should consider an asset's present condition and how long it is expected to meet service demands.

The ASBO Guide provides a chart on page 42 on suggested asset lives. For instance, the ASBO Guide estimates the useful life of a school building as 50 years.

Districts which spend more or are more efficient than average on maintenance, upkeep and improvements may be able to justify a longer useful life than 50 years. Districts which spend less or are less efficient than average in these areas may find their useful lives for school buildings to be less than 50 years.

<u>RECOMMENDATION IV-6</u>: (Date Updated 12/31/00)

Use the ASBO Guide, however the Referent Group recognizes that useful asset lives may vary from the ASBO recommendations. Districts which vary from the ASBO recommendations should be prepared to justify their rationale to citizens, auditors and others. In particular, those districts who choose asset lives + 20% of those listed in ASBO should be prepared for scrutiny of their decisions on asset lives.

<u>ISSUE IV-7</u> Residual Values (Date Updated 12/31/00)

The ASBO guide does not address residual values of assets. The GASB Guide to Implementation of GASB Statement 34 on Basic Financial Statements states in paragraph 45:

Residual value is the estimated fair value of a capital asset remaining at the conclusion of its estimated useful life.

<u>RECOMMENDATION IV-7</u> (Date Updated 12/31/00)

The Referent Group recommends that districts choose a simple method for determining residual values. For instance, all assets have a residual value of 10%. Alternatively, all buildings may have a 15% residual value, all computers may have a 5% residual value, etc. This approach would be less complicated than determining residual values asset by asset. In terms of materiality, it may be more cost effective and as reliable than the asset by asset approach.

Chapter Five - Notes to the Financial Statement

No issues to date. This section may be updated as issues arise.

Chapter Six - The Comprehensive Annual Financial Report

No issues to date. This section may be updated as issues arise.

Other Related Topics

Form B- MDE′s current perspective is that all Form B financial reporting will continue at the fund, function, and object level using the modified accrual basis of accounting. This will be the case until the federal government changes its reporting structure for collecting financial information from the states.

Definition of Deficit District - MDE will continue to look at the information reported on the Form B to determine districts in violation of the State School Aid Act, Section 102(1). Currently a district is determined to have a deficit fund balance if; 1) its general fund balance before reserves is negative, or 2) Other funds have a negative balances that are greater than the general fund balance before reserves. As mentioned above, the Form B will continue to be reported at a fund level with a modified accrual basis of accounting.

Figure 2-1

Sample School District
Statement of Net Assets
June 30, 2002

	GOVERNMENT ACTIVITIES	BUSINESS TYPE ACTIVITIES *	TOTAL
ASSETS			
Current Assets:			
Cash & Cash Equivalents	$62,005		$62,005
Investments	100,000		100,000
Property Tax Receivables, Net	3,717,026		3,717,026
Other Government Receivables	3,800,000		3,800,00
Inventories	83,697		83,697
Total Current Assets	$7,762,728	$0	$7,762,728
Non Current Assets:			
Capital Assets, Net of Accumulated Depreciation	$34,759,986	$0	$34,759,986
Total Assets	$42,522,714	$0	$42,522,714
Liabilities			
Current Liabilities:			
Account Payable	$1,469,066		$1,469,066
Deposits & Deferred Revenue	38,911		38,911
Current Portion of Long Term Obligations	1,426,639		1,426,639
Total Current Liabilities	$2,934,616		$2,934,616
Non Current Liabilities:			
Non Current Portion of Long Term Obligations	$22,437,349		$22,437,349
Total Liabilities	$25,371,965	$0	$25,371,965
Net Assets			
Invested In Capital Assets Net of Related Debt	$12,921,592		$12,921,592
Restricted for Capital Projects	442,345		442,345
Restricted for Debt Service	50,100		50,100
Unrestricted	3,736,712		3,736,712
Total Net Assets	$17,150,749	$0	$17,150,749

*Will be rare for a Michigan District B See Chapter III B Issue III-2

Figure 2-2

Sample Michigan Public School District
Statement of Activities for the Year Ended June 30, 2002

		Program Revenues		Net (Expense) Revenue and Changes in Net Assets		
	Expenses	Charges for Services	Operating Grants	Government Type Activities	Business Type Activities *	Total
Instruction	$16,924,321	$147,739	$2,825,109	-$13,951,473		-$13,951,473
Support Services	$7,972,559	$300	$751,711	-$7,220,548		-$7,220,548
Community Services	$117,773	$2,866		-$114,907		-$114,907
Food Services	$908,263	$541,383	$344,124	-$22,756		-$22,756
Athletics	$545,440	$17,514	$12,102	-$515,824		-$515,824
* Business Type Activities	$0					$0
Interest on Long Term Debt	$546,382			-$546,382		-$546,382
Unallocated Depreciation	$4,171,760			-$4,171,760		-$4,171,760
Total	$31,186,498	$709,802	$3,933,046	-$26,543,650	$0	-$26,543,650

General Purpose Revenues:			
Property Tax	$6,176,108		$6,176,108
State School Aid - Unrestricted	$21,893,273		$21,893,273
Unrestricted Contributions	$285,600		$285,600
Investment Earnings	$667,742		$667,742
Miscellaneous	$19,950		$19,950
Total General Purpose Revenues	$29,042,673		$29,042,673
Excess (Deficiency) of Revenues over Expenses	$2,499,023	$0	$2,499,023
Net Assets - Beginning	$14,651,726		$14,651,726
Net Assets - Ending	$17,150,749	$0	$17,150,749

* Business Type Activities will be rare in Michigan Public School Districts. See Issue III-2.