1135

Problems in Accounting

Dr. Jerry Farley
Current Operating Topics

Learning Objectives

Upon completion of these materials, you will be able to:

- Comprehend the reporting and recognition guidance for information included in public and private colleges and universities financial reports
- Introduce the accounting standards that are significant to public and private colleges and universities
- Explain the need and use of Fund Accounting
Dead or Alive?

Business Officers Debate the Future of Fund Accounting

Fund Accounting Is Dead
Let this complex system rest in peace
By Joe Smith

Fund Accounting Lives
Changes will not kill valuable management tool
By Jerry G. Farley

The only real change brought about by SFAA
No. 117 among the new institutions report changes in financial reporting do not necessarily affect the way business officials account for transactions.
Why Fund Accounting?

- Focus on Stewardship
- Resources with Strings Attached
- Accountability to Resource Providers
- Management

Fund Accounting versus Fund Reporting

FASB ASC 958 – 205 (SFAS #117)
GASB S-34/35/63

Financial Reporting Model

- Reporting Model DOES NOT Change Institutions Financial Management
- Model ONLY Changes Reporting Format Of Results
- Institutions Report In Different Formats For A Variety Of Different Purposes/Users

FUND ACCOUNTING LIVES !!!!!!!!
### GASB Model

- **Business-Type Activity**
  - Fees Charged for Service
  - Full Accrual Accounting --- Depreciation
- **Required Supplemental: MD & A**
  - Management's Discussion and Analysis
- **Three Required Statements**
  - Statement of Position
  - Statement of Revenues, Expenses, and Changes
  - Statement of Cash Flows

### FASB Reporting Model

- **Three Required Statements**
  - Statement of Financial Position
  - Statement of Activities
  - Statement of Cash Flows

No MD&A YET!

### Asset Classification

- **GASB Categories**
  - Capital Assets Net of Debt/Depreciation
  - Restricted
    - Nonexpendable
    - Expendable
  - Unrestricted
- **FASB Net Asset Categories**
  - Unrestricted
  - Temporarily Restricted
  - Permanently Restricted
Current Operations

Current Operating Topics

Learning Objectives

- Recognize judgment involved in interpreting restrictions
- Make the entries to recognize and report Pell Grants and explain the concept of Discounts and Allowances
- Recognize the accounting treatment similarities between compensated absences/defined benefit retirement/OPEB

Resources -- Classification

- Unrestricted
- Restricted
  - Must Be Externally Imposed
  - Purpose/Principal/Period (Time)
Resource Classification - Restricted

- Private Institution
  - Temporarily Restricted
  - Permanently Restricted
- Public Institution
  - Restricted Expendable
  - Restricted Nonexpendable

Can Any Resource Really Be Restricted?

* Revenue Issues *

- Pell Grants
- Scholarships/Discounts and Allowances
Pell Grants

- GASB
  - S-24
  - Revenue
  - Used For Tuition
    - Discount
  - Disburse To Students
    - Expense
  - Non-Operating

Pell Grants

- FASB
  - No Recognition of Revenue Or Expense
  - Agency Account

SCHOLARSHIP/DISCOUNTS AND ALLOWANCES

- NACUBO Advisory Report:
  - Publics 2000-05
  - Privates 1997-01
  - Preferred industry practice
    - Unless future guidance by FASB/GASB/AICPA
REPORTING SCHOLARSHIP DISCOUNTS AND ALLOWANCE

Definition
- A Scholarship Allowance Is:
  - Difference Between Stated Charge And The Amount Billed To Student/Others

REPORTING

- Amounts received for tuition/fees will be reported as revenue only ONCE i.e. fees, gifts, federal grants (Pell - for Publics), investment income
- Only amounts received from students/others for tuition/fees, room/board, or bookstore payments will be reported as revenue

REPORTING

- Institutional resources provided to students as financial aid will be recorded as scholarship allowances in amounts up to and equal to amounts owed by the student
- When aid exceeds the tuition/fees/housing/ or meals, the excess of aid should be treated as an expense
REPORTING

- Income on investments established to provide financial aid will be reported as income from investments:
  - When used to cover forgone tuition, revenue should not be recognized a second time as gross tuition and then as financial aid expense
  - The entry should be to record a discount to tuition to reflect the waiver

DISPLAY

- Tuition/fee revenue may be reported net as a single line
- Scholarship allowances may be reported parenthetically to Tuition and Fees line
- Gross revenue permitted if allowance displayed immediately beneath as reduction
- Same reporting for all types of revenue—tuition, housing, food service, etc.

Contributions

- GASB S – 33
- FASB ASC 958 – 605
- (SFAS # 116)
Contributions

Voluntary Non-reciprocal (Non-Exchange)
Transfers To/From Non-owners
   Unconditional
   Conditional

- Conditional Contribution
  - Specifies Future Uncertain Event
  - Differs From Restriction
  - Disclosed In Notes
  - Funds In Hand ----- Unearned
  - Privates-- Do Not Recognized As Revenue Until Condition Met
  - Publics-- Not Recognized Until Eligible To Use

Contributions --- Time

- Publics – Time Creates Condition (An Eligibility Requirement)
- Privates – Time Creates A Restriction -- Is Recognized Immediately As A Restricted Net Asset
Unconditional Contributions

- Unconditional (Voluntary Non-exchange)
- Gifts (Cash or Fair Value of Asset)
- Promise to Give (Pledge)

Unconditional Promise to Give (Pledge) Public

- Recognize When:
  - Verifiable
  - Measurable and Probable of Collection
  - Eligible to Use
- Publics – If Cannot Be Used Until Future Period, Do Not Report Until Then
  - Promise to Give an Endowment Not Recorded Until Funds May Be Invested As Endowment
  - Reimbursement Basis – ALLOWABLE AS EXPENDITURES ARE MADE

Eligibility Example (Publics)

- The Art Dep’t receives a Cash gift of $10K for faculty art exhibit this year --- next year.
- Would the entries change if the gift was a pledge rather than cash?
Eligibility Example

¬ The University received an endowment
  Pledge of $10M  Debit ..... Credit

¬ The University receives a gift for a new
  building ..... Record all or Fair Value

Unconditional Promise to Give
(Pledge) Private

¬ Privates – Report As Restricted Upon Receipt
  • Temporarily (Time Creates Restriction)
  • Permanently
  • Record Present Value of Future Cash Flows
¬ Difference Between Discounted Value and Future
  Receipts—Additional Contribution Revenue
¬ Allowance For Uncollectible Pledges
¬ Ambiguous Stipulations ……. Conditional

Pledges @ Fair Value

¬ Pledge = $100,000 Over 5 yrs. (@0K/Yr.  
  Discount Rate 4%/ PV $90K, Discount by 
  Yr.—$3K/$2.5K/$2K/$1.5K/$1K
¬ Year 1 ——Record Pledge
  Dr. Receivable  $90K
  Cr. Gift $90K
¬ Year 2 —— Record Payment
  Dr. Cash $20K
  Cr. Pledge Receivable $17K
  Cr. Gift $3K
Contribution --- Example

In 2014, University received a copy of Mr. Fried’s will. He died in 2017. In 2018 the will is declared valid and $10K will be disbursed to the University in 2019.

Would you record an unconditional promise to give? If so when?

Contribution --- Example

In 2019 Mrs. Morton promised to give the Athletic Dep’t $400K for a new practice facility, if the school will raise $600K. Mrs. Morton gives the $400k immediately so planning may begin while the $600K is raised. Is the $400K a contribution? How would the school record the $400K?

Contributed Services --- Public

No specific Guidance --- May Use Similar Definitions as Privates
Contributed Services

If Relevant/Measurable and Cost Effective … Recorded as Contribution Revenues and Expense
If A Non-Financial Asset Is Created ….. Capitalize the Asset

FASB ASC 958-205-25/30

Contributed Services

Private Institutions Recognize if:
• Create/Enhance Assets
• Requires Special Skills
• Provider Has Skills
• Would otherwise purchase

Contributed Services

➢ Footnote Disclosures
  • Nature/Extent of Services
  • Amounts Recognized
  • Services Received ….. Not Recognized
Contributed Services

- Private Institutions
  - If Services Provided To Affiliated NFP ... NFP Must Recognize At Actual Cost of Provider (ASU 2013 – 06)

Special Collections

- Works of Art/Treasures Need Not Be Recognized OR Capitalized If Addition to Collections Held And Maintained For:
  - Exhibition
  - Education
  - Research

Special Collections

- Disclosures
  - Description
  - Amount Bought/Sold
  - Cared For
  - If Sold … Buy Other Collection Items
### Realized and Unrealized Investment Gains/Losses

- Recognized by Publics and Privates
  - FASB ASC
    - 958 – 205 – 45
    - 958 – 320 – 45
    - 958 – 225 – 45
  - GASB S - 31

### Gains/Losses (Privates)

- Temporarily Restricted Net Assets Unless Explicitly Permanently Restricted
- Unspent Gains May Be Continually Invested To Protect Future Purchasing Power of Endowment
- Unrestricted Net Assets
  - Board Can “Appropriate” For Use Based on Spending Policy

### Gains/Losses (Publics)

- Based on spending policy
  - Portion of gains in Current Fund (non operating revenue) and balance of gain in Endowment Fund (Non operating revenue – Restricted Expendable) – Unspent Gains May Be Used to Protect Future Spending Power Of Endowment
Expenditures

- Current Operations vs Capital
- Classification ....Financial Reporting
  - Natural (object class)
  - Functional Designation

Natural Classification

- Salaries and Wages
- Benefits
- Utilities
- Supplies and Other Services
- Depreciation

Categorized As on Stmt of Cash Flows

Traditional Functional Classification

- Instruction
- Research
- Public Service
- Academic Support
- Student Services
- Institutional Support
- Operations and Maintenance of Plant
- Auxiliary
- Hospital
- Independent Operation
### Private Institutions Expenditure Classification

- If Natural on Face – Function In Notes
- If Function On Face – Natural
- Classification Not Required In Notes
- Allocate To Functions
  - Depreciation
  - Operations and Maintenance
  - Interest Expense

### Public Institutions Expenditure Classification

- If Function On Face – Natural Not Required In Notes
- If Natural On Face – Function In MD&A
- Report Depreciation As Functional Category
- Allocations Not Required for Financials
  - Depreciation/Interest/Operations and Maintenance
- Allocations Required for IPEDS

### Expenditure Issues

- Compensated Absences/Retirement/Other Post Employment Benefits
- Payments To Be Made In Future Based On Past Service
- Benefits “Earned” and Obligations “Accrue” During Employment
- Payments Of Benefits Occur After Employment
- Record Systematically During Employment
Compensated Absences

- FASB ASC 710 – 10 – 25 (SFAS # 43)
- GASB S-16
- Very Similar Requirements

Compensated Absences

- Paid Absences
  - Vacation
  - Sabbatical If No Future Service
  - Not Sick Leave Unless Paid at Termination

Compensated Absences

- Accrue Liability as Earned
  - Based on Past Service
  - Payment Must be Probable
  - Use Current Rates of Pay Including Benefits
  - No Provisions for Future Salary Increases
  - No Provision for Actuarial Discount
  - Covers Sabbaticals ..... If No Future Service
Compensated Absences

Sick Leave
Record Only if Results In Termination Payments
- Accrue as Earned or;
- Measure those Currently And Those Expected To Be Eligible

Compensated Absences

✓ Many Institutions Do Not Budget for Compensated Absences
✓ Pay-As-You-Go
  - Leave Departing Person On Payroll
  - Do Not Fill Position Immediately
✓ Only An Operational Impact If Going Out Of Business
  - Will Be Paid From Liquidation Of Assets

Compensated Absences

Compensated Absences

Compensated Absences

Other Post Employment Benefits (OPEB)

✓ FASB 715 (SFAS#106/#158)
✓ GASB S – 45/57
✓ GASB S – 75 (applicable FY18)
✓ OPEB Includes:
  - Healthcare *******
  - Life Insurance/Long-Term Care/Free Tickets/Parking/Etc.
✓ Actuarial Methodology Differences
OPEB (Publics)

- Applies to employers and non-employer contributing entities that have a legal obligation to make contributions directly to an OPEB plan or to make benefit payments as those payments come due.
- A liability will be reported whether the benefits are through the state or employer.
- If the plan is “pay as you go” and no assets to offset liability, Big balance sheet issue.

Retirement Benefits

- FASB ASC 715 – 20 (SFAS#87/#158)
- GASB S – 5/25/27/67/68

- Defined Contribution Plans
- Defined Benefit Plans

Retirement Benefits

- Defined Contribution Plans
  - Public and Private
  - Most Used
- Defined Benefit Plans
  - Few Private University Plans Remain
  - Often Multi-Employer State Plans
    - (Public Employer Retirement System {PERS})
Defined Contribution

- Fixed Amount To Retiree (Usually A % Of Salary)
- Used To Purchase A Mutual Fund (403[b]) On Behalf Of Employee
- Employee Responsible For Investment Choices And Thus Retirement Income
- Ends Employer Obligation
- Retirement Plan Is “Funded”
- Debit: Expense ---- Credit: Cash

Defined Benefit

- Employer Promises Employee A “Defined” Amount of Retirement Income
- Based On Mathematical Formula:
  - Average 3 or 5 Year or High Salary
  - Multiple By % (1-2-3)
  - Multiple By Years Of Service
- Income For Life Fixed At Retirement
  - Possible Future Increases To Offset Inflation
  - Employer Responsible For Investments
  - Debit: Expense .... Credit: Liability

WHERE IS THE CASH???????
### Defined Benefit

- Without Cash To Purchase Investments And Investments To Generate Returns (Plus Corpus) To Pay Eventual Benefit
  - PLAN FAILS!!

- Must Compute Amount To Contribute (Cash) And Add Investment Returns To Pay Computed Future Retirement Income

### OPEB/Defined Benefit Retirement Plans

- All OPEB and Pensions Obligations Will Be Measured and Reported Using The Same General Approach
- Accrue Expenses/Liability As Earned From Start Of Employment Till Full Eligibility
- Actuarial Computation
- Publics: Projection Of Future Salary Increases Or Additional Service Credits

### OPEB

- GASB Issue (S-68)
- Public – If A Member Of A Multi-Employer PERS:
  - Record Proportionate Share Of Obligation (Liability)
### Actuarial Computation Issues

- Of Employees Who Start Work, How Many Will Reach Eligibility
- How Long Will Retirees Or Dependents Receive Benefits
- What Will Be The Cost of Future OPEB Benefits (Present Value)

### Actuarial Computation Issues

- How To Attribute Cost To Service Periods
  - Allocated As A % Of Payroll
- How To Value Plan Assets
  - Fair Market Value
  - Actuarial Value
  - Discount Rate

### GASB Pension Reporting (S-68)

- Moves From A Funding Approach to an Accounting Approach
- Requires Immediate Recognition of Overall Pension Obligation
- Measurement of Liability Will Be Determined on funding Status, Discount Rate
GASB Pension Reporting

- Liabilities to Employees for Pensions
  - Net Pension Liability (NPL) = Total Pension Liability (TPL), Net of Pension Plan’s Fiduciary Net Position (Investment Assets)
  - Cost Sharing Employers Recognize Proportionate Shares of Collective NPL

GASB Pension Reporting --- Changes in NPL

- Recognized as Expense Immediately:
  Service Cost, Interest on the TPL, Changes in Benefit Terms, Projected Investment Earnings
- Recognized as Expense Over Time:
  Changes in Assumptions, Difference Between Assumed and Actual Demographic /Economic Factors, Differences in Projected and Actual Investment Earnings.

GASB Pension Reporting --- Cost Sharing

- Determining Employer’s Proportionate Share of the Collective Net Pension Liability
  - Basis for Proportion Consistent with the Manner in Which Contributions Are Determined
  - Different Contribution Rates Are Assessed Based on Separate Relationships
  - Not Necessarily One Size Fits All
Other Pension Issues

- Actuarial Accrued Liability (AAL)
- Actuarial Value Of Plan Assets
- Do You Fund?
- UAAL (AAL Less Plan Assets)
- Funded Ratio
- Ratio Of UAAL To Covered Payroll

OPEB: GASB Issues

- Implicit Rate Subsidies -- GASB Issue
  - When Current Employees and Retirees Are In Same Group ---- Costs For Retirees Generally Significantly Higher
  - Therefore, Retirees That Pay For The Cost Of Healthcare Benefits Through A Blended (With Current Employees) Premium May Not Be Actually Paying The Actual Costs Of Their Benefits

FASB Defined Benefit Issues

- FASB ASC 715 (SFAS #158)
  - Requires The Net over (Asset) Or Under (liability) Funded To Be Recorded On The Balance Sheet
  - Applies To Both Pension and OPEB
  - Recognize Changes In Funded Status In Unrestricted Net Assets
  - Year Changes Occur
FASB Defined Benefit Issues

- FASB ASC 715 (SFAS# 158)
- Fair Value Of Plan Assets Less:
  - Pensions … Measure Against Projected Benefit Obligation (PBO)
  - OPEB …. Measure Against Accumulated Postretirement Benefit Obligation (APBO)
- Measure On Balance Sheet Date

Expiration of Restrictions – Privates

- At Time Restriction Met/Time Expires Temporarily Restricted Reclassified To Unrestricted
- Decrease: Temporarily Restricted
- Increase: Unrestricted
- If Expense Incurred For A Purpose For Which Both UR and TR Available, TR Released To Extent Of Expense

Deemed Spent

IF YOU COULD OF …..
YOU SHOULD OF
Expiration Of Restriction -- Publics

- Tracks Each Gift
- Specific Identification Of Expense As Either Restricted Or Unrestricted

Endowment and Similar Funds

Endowment Fund Learning Objectives

- Introduce relevant legal concepts governing endowments and funds functioning as endowments
- Discuss Uniform Prudent Management of Institution Funds Act (UPMIFA)
- Review accounting standards that apply to endowments and funds functioning as endowment
Endowment Fund Learning Objectives Cont.

- Describe Annuity Funds, Split Interest Agreements, Pooled Income Funds, and Charitable Remainder Trusts
- Discuss issues related to management of endowment funds

ENDOWMENT FUND TYPE

- True/Pure
- Funds Functioning As Endowment/Quasi
- Term

TRUE/PURE ENDOWMENT

- Invest Corpus/Principal In Perpetuity
- Spend Only Earnings
- What is “Earnings”? -- Income
- -- Dividends
- -- Rents
**True Endowment**

- What About Appreciation?
- Is Principal – Non-expendable?
- Is Principal – Expendable?
- Legal Issue
  - Trust Law
  - Charitable Corporations

**Trust Law**

- Trustee -- Beneficiary - Remainderman
- Appreciation Is Principal
- Co-mingling Forbidden
- Investment Management May Not Be Delegated

**Laws Governing Charitable Corporations**

- Hold Endowment For Own Benefit
- Absolute Ownership
- Appreciation May Still Be Principal
- Delegation - Maybe
Uniform Management of Institutional Funds Act (UMIFA)

- Permitted Prudent Use of Appreciation
- Allowed Delegation
- Prescribed Standard of Care/Prudence
- Established “Historic Dollar Value”
- Original Gift/Subsequent Additions
- Appreciation: Excess of Historic Dollar Value

NOW!!! Uniform Prudent Management Of Institutional Funds Act

UPMIFA Highlights

- Abolishes Historic Dollar Value
- Comprehensive Prudence Standards
- Portfolio Managers Not Limited To Kinds of Assets
- Cost Must Be Managed Prudently
- Rebuttable Presumption Of Imprudence If Spending Greater Than 7%
- Total Return Expressly Authorized
UPMIFA HIGHLIGHTS

Continues Concept Of Spending
Prudent Amount of Appreciation

Continues Concept of Protecting
Future Purchasing Power Against
Ravages Of Inflation

UPMIFA

Without Concept Of Historic Dollar Value:
• What is Permanently Restricted?
• How Are Amounts Retained To Protect
  Purchasing Power Classified?

FASB ACS 958 – 205 – 45
(SFAS # 117 – 1)

Historic Dollar Value
• Permanently Restricted
• Remainder of Fund
  • Temporarily
  • Unrestricted
UPMIFA FASB (FSP) Disclosure

- Net Asset Classification
- Net Asset Composition
- Net Changes in Composition
- Spending Policy
- Investment Policy

Total Return Concept

- Investing for Total Return
  - Invest In Variety Of Instruments (Diversify) To Maximize (Optimize) Total Return

Protect Purchasing Power

- Spending Policy
  - Spend Income (Yield)
    - Interest
    - Dividends
    - Rents
- Spend Appreciation
- Spend “Earnings”
  - Income Plus Prudent Amount Of Appreciation
**Underwater Endowment**

- Concept Of Underwater Endowment
  - Losses Bring Fund Below Historic Dollar Value

- Charge Losses To Temporarily Restricted Or Unrestricted Net Assets

  FASB ASC 958-205
  FASB ASC 958-320

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**“Underwater” Endowments Private**

- Year 1: $50,000 Endowment For Library
  $3,000 Investment Gain
- Year 2: $5,000 Investment Loss
- Year 3: $3,000 Investment Gain

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<tr>
<td>Year 3 - gain $2,000</td>
<td>$1,000</td>
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**“Underwater” Endowment Private**

- Spend Funds From Underwater Endowment If It Has No TRNA
  - What Does State Law Say … UPMIFA
  - Use Unrestricted Resources To Cover Payment
  - Board Concerns ….. Prudence
  - Donor Concerns

- Changes Coming!!
GASB Underwater Endowments

Investments Are Recorded At Fair Market Value
Gains/Losses Reported On Financial Statement

Funds Functioning As Endowment

Term Endowment

Funds Functioning As Endowment

- Funds “Designated” By Board To Be Treated Like An Endowment ..Retained And Invested
- Board May Authorize Expending Principal
- Normally For A Stipulated Period
- QUASI
### Term Endowment

- Similar To True Endowment
- Except:
  - After Stated Period Or Specified Event …. All Or Portion Of Principal May Be Spent
- Used To “Jump Start” Programs
- Popular Sixty Years Ago By Private Foundations

### Endowment Examples

- The School of Nursing Receives a Large bequest to be Invested for the General Benefit of the School.
- How Would You Classify?
- ----to the School
- ---- to the University

### Endowment Example

- Silverton College Received an Unexpected Bequest of $500K. The Regents Voted to Place 75% in the Endowment and the Balance to be Used for Student Services.
- How would You Classify the Gift?
Endowment Example

The Chair of the English Department Requests an Endowment Fund Be Established to Generate Income to be Restricted to Support of Lectures in Creative Writing. The Funds Came From the Sale of Publications, Principally a Creative Writing Magazine.

How would you classify?

Endowment Example

You have Received a Bequest Containing the Following Provisions: “I Direct My Residuary Estate be Paid to the Veterinary College to be Used for Research and the Study of Equine Diseases. The Funds of This Trust Shall be Used for Direct Scientific Equine Research and Shall be Known as the Jones Equine Research Foundation.”

How Would You Classify?

Annuity Funds and Other Split Interest Agreements.
Annuity

- Pay Stipulated Amount Periodically To Donor
- Payments Terminate at Specified Time
- Principal Balance Belongs to Institution

Annuity

- Assets When Received
- Income Payments Based On:
  - Life of Beneficiary
  - Earnings Rate Promised
  - Administrative Expenses
- Residual

Annuity Accounting

- Assets At Fair Value
- Liability For PV Of Expected Payments
- Difference Is Net Asset
- Changes In Liability
  - Income On Assets
  - Payments
- Amortization Of PV Discount And Changes In Life Are Income
- Balance To Institution
Split Interest Agreements

- Pooled Income Contracts
- Perpetual Trust
- Charitable Lead Trust
- Charitable Remainder Trust
- Charitable Remainder Unitrust

- Assets .... Contributions At Fair Value
- Liabilities And Net Assets:
  - Charitable Lead Agreement ... PV Of Estimated future Distributions = Gift
  - Remainder Interest Agreement ... Value Of The Assets Contributed less PV Of The Payments To Be Made To Beneficiaries = Gift
  - Pooled Life Income Agreement ... Value Of The Assets Contributed, Discounted Until Donor’s Death = Gift

Funds Held in Trust by Others

- Trust Assets Held by Third Party
- Institution has Irrevocable Right to Income
- Never Receives Assets
Funds Held in Trust by Others

**Privates**
- Recorded As Present Value Of Estimated Future Cash Receipts From Trust Assets

**Publics**
- Asset Recorded At Fair Value
- Deferred Inflow (Same as Fair Value)
- Changes In Fair Value Reflected As Deferred Inflow

**Income**
- Public/Privates
  - Revenue when received (unrestricted or restricted or temporarily restricted)
- Publics – Contribution Revenue – Non Operating
- Privates – Investment Income

Management

**Who Classifies Gifts and Interprets Restrictions**
- Development
- Legal
- College/Department
- Financial

Gift Stipulations

**Precatory Declaration**
**Cy Pres**
**Changed Condition**
Deeds of Gifts

- Documentation
- Centralize
- Update

Investment Issues

- Separately Invested
- Pool Concept

Investment Pools

- Spread Risk
- More Flexibility
- Minimize Uninvested Cash
- Easier to Liquidate
Multiple Pools

- Active Vs/ Index
- Fixed Income Vs/ Equities
- International Vs/ Domestic
- Large Cap Vs/ Mid Or Small
- Growth Vs/ Value
- Alternatives
  - Private Equity/Hedge/Emerging Markets/Real Estate

Investment Pool

- Basic Principles:
  - Identity Of Each Fund At Book Value
  - Participation In Pool Identified By Number Of Units
  - Market Value Of Pool Determined Periodically
  - Additions/Withdrawals Made At CURRENT Market
  - Income Distributed Based On Units

Investment Pools (Continued)

- Realized Gains And Losses Accumulated In Separate Account.
- Withdrawals Based On Unit Market Value At Time Of Withdrawal. Gain/Loss From Withdrawal Considered Realized Gain/Loss Of Pool
Investment Policies

Distribution/Diversity Should Reflect Spending Policy

Spending Rate

- Begin With Earnings/Investment Performance
- Offset Inflation and Protect Purchasing Power
- Administrative Cost
- Consistency Year to Year
- Smooth Based On Market Value Over 12 – 16 – 20 Rolling Quarters

Spending Policies

- All Earned
- % Over Prior Year
- % Of Moving Market Value
- Review Periodically
- Balance Current Income Demands vs. Protection of Purchasing Power
Capital Issues

Identify the Elements (revenues/expenditures) of transactions in the following areas:
- Construction/acquisitions
- Renovations
- Debt Service
- Capitalized Assets

Learning Objectives Cont.

Explain and discuss the concept of depreciation and how depreciation contributes to funding asset replacement
Learning Objectives Cont.

- Recognize the elements and how to record transactions resulting from the following special problems:
  - Bond premium/discounts
  - Capitalized interest
  - Capital leases
  - Extinguishment of debt

Fund Accounting
Plant Funds

- Unexpended
- Renewals and Replacements
- Retirement of Indebtedness
- Investment in Plant

Plant Funds

- C & U No Longer Report By the Various Plant Fund Categories
- The Capital Transactions Reported Still Occur
Fund Accounting
Plant Funds

Accounts For Similar Types Of Transactions:
- Construction In Progress
- Renovations

Funds To Retire Indebtedness
Capital Accounts
- Buildings And Equipment
- Land Improvements And Infrastructure (Public)

Capital Reporting

Capital Transactions
- Acquisitions Are Balance Sheet Transactions -- Exchange Cash For Asset
- Debt Is Liability ---Associated With Capital Asset
- Principal Payment Is Balance Sheet Transaction

Transactions

Expenditures for Construction Renovations Principal Payment

Creates Balance Sheet Transactions
Revenue Available for Capital Additions/Acquisitions

Earmarked External Resources

- Student Fees
- Government Appropriations
- Private Gifts
- Investment Gains

Gift for Building

- A cash gift is received to construct a new science building
- Is the gift restricted?
- How is restriction met?
- If the building is “restricted”, could it be converted to a building occupied by History?
<table>
<thead>
<tr>
<th>Internally Available Resources</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unrestricted Net Assets</td>
</tr>
<tr>
<td>Current Funds/Other</td>
</tr>
<tr>
<td>• Annual Operations</td>
</tr>
<tr>
<td>• Resources Functioning as Endowment</td>
</tr>
<tr>
<td>• Reserves</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Borrowing</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Internal Advances</td>
</tr>
<tr>
<td>• Temporary</td>
</tr>
<tr>
<td>• Long Term</td>
</tr>
<tr>
<td>• External Indebtedness</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction In Progress</td>
</tr>
<tr>
<td>• Architecture Fees</td>
</tr>
<tr>
<td>• Site Work</td>
</tr>
<tr>
<td>• Construction</td>
</tr>
<tr>
<td>• Fixed/Movable Equipment</td>
</tr>
<tr>
<td>• Interest During Construction</td>
</tr>
</tbody>
</table>
Other Expenditures

• Acquisitions
• Investment Losses

Project: Solar Panels

_installed solar panels to existing building:
Cost $783,000
_capitalize: Yes…… No…… If yes, where?
_does source of funds: current, quasi, plant determine where to capitalize?

**Panels cost $715,000 -- Installation by physical plant $68,000**
_capitalize:__
_panels….
_physical plant cost: Yes…. No….____
_what if portion of physical plant cost was institution overhead?**
Local utility company has a solar project rebate program
Institution received $700,000 rebate
How recorded? Reduce capitalized amount?
Yes…No… If no: how – where recorded?
Debit ______
Credit ______

What if rebate was provided by manufacturer at the time of purchase?

Science Building

Institution intends to construct a science building.
When – What to capitalize – (planning team):
 development, academic department, physical plant, University architect, accounting
Engage external architect
Fundraising stalls – one year – two years – five years
Capitalize – Yes? No?
How reported?

Project revitalized – proceeds
Building occupied – stop capitalization – when?

Contingency reserve remains and department spends for physical improvements the next two years
Capitalize – Yes? No?
Renovation Expenditures

- Extraordinary Repairs-Improvements
  - Capitalize If: Increase Capacity, Efficiency, Useful Life --- Benefits Future
- Ordinary Repairs – Maintenance
  - Expense
  - Typically Current Operations

To Capitalize or Not

- Established capitalization policy above $50,000
- Oldest campus building needs extensive repairs, especially external painting. Legislature provided “capital project” funding, $200,000 for painting.

- Does the project meet the criteria for capitalization?
- Would the cost of painting be capitalized?
Renovation Expenditures (Con’t)

- Replacements
  - Capitalize
  - Remove Replaced Assets from Inventory

---

Roof Replacement

- After twelve years, the roof on our newest building failed and had to be replaced.
- Should the new roof be capitalized or expensed? Why?
- Should the undepreciated cost of the old roof be removed?
- How computed?
- Would component depreciation help?

---

External Resources
To Retire Debt

- Earmarked – External
  - Student Fees
  - Gifts
  - Investment Gains
<table>
<thead>
<tr>
<th>Internal Resources To Retire Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>➢ Current Operations</td>
</tr>
<tr>
<td>➢ Reserves</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Debt Related Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>➢ Interest</td>
</tr>
<tr>
<td>➢ Trustee Fees</td>
</tr>
<tr>
<td>➢ Investment Losses</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Payment Of Principal</th>
</tr>
</thead>
<tbody>
<tr>
<td>➢ Balance Sheet Transaction</td>
</tr>
</tbody>
</table>
Capitalized Assets

- Donated Capital Assets
- Acquisitions
  - Current Operations
  - Construction
  - Renovation
  - Purchase
  - Construction In Progress

Capital Assets

- Real Property
  - Land/Buildings/Other Improvements
  - Construction In Progress
  - Infrastructure (Publics)
- Personal Property
  - Equipment/Library Books/Museums
  - Art Collections/Livestock
- Depreciable Capital Assets
  - Accumulated Depreciation

Infrastructure  Land Improvement

- Street/Road
- Sidewalks
- Traffic Lights
- Street Signage
- Bridges
- Tunnels
- Distribution Systems
  - Water/Sewer/Electrical
  - Steam/Chilled Water
- Landscaping
- Tennis Courts
- Bleachers
- Athletic Fields
- Golf Courses
- Pools Fountains
- Fencing Parking Lots
Capitalization Policy

- Acquisition Value In Excess of Stated Dollar Amount
- Expected Useful Life In Excess of Stated Number of Years
- Identity Does Not Change Over Time

Funding Asset Replacement

Do Not Confuse Funding Asset Replacement With Depreciation
Depreciation
Concept of Capital Maintenance

Capital Maintenance
- Measures economic wealth/performance
- Did revenues exceed expenses
- Were payments to owners - Return of Capital
  or
  Return on Capital

Two Concepts
- Maintenance of
  - Financial Capital
  - Physical Capital
Maintenance of Financial Capital

- Accrual Accounting
- Depreciation of Fixed Assets
  Based on Cost

Depreciation

- Matches Expense with Revenue
- Indirect Means of Asset Replacement
- Measurement of Reduction of Capital
Maintenance of Physical Capital Expense Based on Current/Future Asset Value

Depreciation Required For Private And Public Institutions

Depreciation

► Expense for Period
► Accumulated Depreciation
► Balances of Major Asset Classes
► Describe Computational Method
Does Depreciation Provide For Asset Replacement?

Jerry’s Juice Company ::::Operations

<table>
<thead>
<tr>
<th></th>
<th>Year One</th>
<th>Year Two</th>
<th>Year Three</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>25</td>
<td>35</td>
<td>45</td>
</tr>
<tr>
<td>Sales</td>
<td>25</td>
<td>35</td>
<td>45</td>
</tr>
<tr>
<td>Expenses</td>
<td>25</td>
<td>25</td>
<td>25</td>
</tr>
<tr>
<td>Cash</td>
<td>25</td>
<td>25</td>
<td>25</td>
</tr>
<tr>
<td>Depreciation Expense</td>
<td>10</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Accumulated Depreciation</td>
<td>10</td>
<td>10</td>
<td>10</td>
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</table>

Jerry’s Juice Company

Income Statement

<table>
<thead>
<tr>
<th></th>
<th>Year One</th>
<th>Year Two</th>
<th>Year Three</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>25</td>
<td>35</td>
<td>45</td>
</tr>
<tr>
<td>Expenses (Cash)</td>
<td>&lt;25&gt;</td>
<td>&lt;25&gt;</td>
<td>&lt;25&gt;</td>
</tr>
<tr>
<td>Depreciation</td>
<td>&lt;10&gt;</td>
<td>&lt;10&gt;</td>
<td>&lt;10&gt;</td>
</tr>
<tr>
<td>Profit/Loss</td>
<td>&lt;10&gt;</td>
<td>-0-</td>
<td>10</td>
</tr>
</tbody>
</table>
### Jerry’s Juice Company
### Balance Sheet

<table>
<thead>
<tr>
<th></th>
<th>Year One</th>
<th>Year Two</th>
<th>Year Three</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>10</td>
<td>30</td>
<td></td>
</tr>
<tr>
<td>Asset</td>
<td>50</td>
<td>50</td>
<td>50</td>
</tr>
<tr>
<td>Accumulated Depreciation</td>
<td>&lt;10&gt;</td>
<td>&lt;20&gt;</td>
<td>&lt;30&gt;</td>
</tr>
<tr>
<td>Total Assets</td>
<td>40</td>
<td>40</td>
<td>50</td>
</tr>
<tr>
<td>Liability</td>
<td>-0-</td>
<td>-0-</td>
<td>-0-</td>
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<tr>
<td>Equity</td>
<td>50</td>
<td>50</td>
<td>50</td>
</tr>
<tr>
<td>Operating Profit/Loss</td>
<td>&lt;10&gt;</td>
<td>&lt;10&gt;</td>
<td>0-</td>
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<tr>
<td>Total Liabilities and Equity</td>
<td>40</td>
<td>40</td>
<td>50</td>
</tr>
</tbody>
</table>

### Funding Asset Replacement

- Accumulate Resources in Operating Accounts
- Accumulate Resources in Reserve Accounts
- Invest Reserve To Offset Inflation
- May Not Reflect Designations On Stm’ts
- Reservations Of Unrestricted Net Assets
- Previously Referred To As Renewals And Replacement Accounts

### Disposal of Capital Assets

- Loss
- Retirement/Replacement
- Sale

Remove Asset Balance and Accumulated Depreciation
Special Problems

- Bond Premium Discount/Issue Cost
- Extinguishment of Debt
- Capitalization of Interest
- Capital Leases

Bond Premium/Discount

- Difference Between Cash/Face Value
  - Discount Viewed as Prepayment
  - Premiums Viewed as Advance
- Amortize to Interest Expense Over Life
  - Adjusts Effective Interest Rate
- Early Retirements

Bond Premium/Discount

- Direct Reduction From Or Addition To Face Amount Of Debt
- NOT A separate Asset Or Liability

FASB ASC 835-30-45
GASB S – 62
**Issue Cost**

- Legal
- Financial Advisor
- Printing
- Rating

**Issue Cost**

- Private
  - Amortize to Interest Expense over life of the debt
- Public
  - Period cost charged to interest expense

FASB ASC 835-30-45-3
GASB S - 65

---

**Exhibit A**

<table>
<thead>
<tr>
<th>Bond: Premiums/Discount/Issue Cost</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The Bond Issue</strong></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>9,700,000</td>
</tr>
<tr>
<td>Issue Cost</td>
<td>100,000</td>
</tr>
<tr>
<td>Discount</td>
<td>200,000</td>
</tr>
<tr>
<td>Debt</td>
<td>10,000,000</td>
</tr>
<tr>
<td>Issue 20 year debt for construction</td>
<td></td>
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</tbody>
</table>

**FINANCIAL STATEMENTS**

<table>
<thead>
<tr>
<th>Private Institutions</th>
<th>Public Institutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>9,700,000</td>
</tr>
<tr>
<td>Debt (Discount)</td>
<td>200,000</td>
</tr>
<tr>
<td>Issue Cost</td>
<td>100,000</td>
</tr>
<tr>
<td>Debt</td>
<td>10,000,000</td>
</tr>
<tr>
<td>Interest Expense</td>
<td>15,000</td>
</tr>
<tr>
<td>Non-operating</td>
<td>5,000</td>
</tr>
</tbody>
</table>
### Exhibits A-1

**Exhibit A-1**

**Bond: Premiums/Discount/Issue Cost**

Annual Amortization of Issue Cost/Discount

<table>
<thead>
<tr>
<th></th>
<th>Cash</th>
<th>Capitalized Interest</th>
<th>Debt Service Reserve</th>
<th>Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>8,100,000</td>
<td>700,000</td>
<td>1,200,000</td>
<td>10,000,000</td>
</tr>
</tbody>
</table>

**Construction in Progress Accounts**

<table>
<thead>
<tr>
<th></th>
<th>Cash</th>
<th>Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>8,100,000</td>
<td>8,100,000</td>
</tr>
<tr>
<td>Debt</td>
<td>8,100,000</td>
<td>1,900,000</td>
</tr>
</tbody>
</table>

**Debt Service Accounts**

<table>
<thead>
<tr>
<th></th>
<th>Cash - Trustee</th>
<th>Cash - Cap. Int.</th>
<th>Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>1,200,000</td>
<td>700,000</td>
<td></td>
</tr>
<tr>
<td>Debt</td>
<td>8,100,000</td>
<td>1,900,000</td>
<td></td>
</tr>
</tbody>
</table>

---

**Exhibit A-1**

**Financial Statements**

<table>
<thead>
<tr>
<th>Private Institutions</th>
<th>Public Institutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unrestricted Net Assets</td>
<td>Unrestricted Net Assets</td>
</tr>
<tr>
<td>Cash</td>
<td>Cash</td>
</tr>
<tr>
<td>Cash-Debt Service</td>
<td>Cash-Debt Service</td>
</tr>
<tr>
<td>Cash-Reserved</td>
<td>Cash-Reserved</td>
</tr>
<tr>
<td>Debt</td>
<td>Debt</td>
</tr>
</tbody>
</table>

---

---

**Extinguishment of Debt**

- Reacquisition of Debt Before Maturity
- Debt Repaid
- Legal Release
- In-Substance Defeasance
Extinguishment of Debt Guidance

- FASB ASC 405-470
  - SFAS #76
  - APB #26
  - SFAS #145 (Rescinds SFAS #4 and #64)
  - SFAS #125 (More later)
  - GASB S – 62/68

In-substance Defeasance (Advanced Refunding)

- Create Trust
- Irrevocably Fund Trust
- Trust Cash Flows Cover Debt Service

Strict Requirements

- Specified Maturities/Fixed Payments
- Irrevocable Risk Free Assets in Trust
- Future Payments - Remote
- No One May Gain Access to Assets
- May Only Refund ONCE
Callable Debt

- Call Debt When Mandatory Unless Specified at Time of Refunding
- Cannot Exercise Optional Call

Instantaneous Defeasance

- New Debt Issued
- Old Debt Immediately Extinguished
- Simultaneous Borrowing/Investing
- Related Income/Expense Recognized Overtime
- Added Option – Publics
  - University Existing Resources May Be Placed In The Trust Thus Reducing Size Of New Debt

Accounting for Extinguishments

Amount to Reacquire
Less
Net Carrying Amount
-Gain or Loss-
### Display Of Extinguishments

**Public**

- Reported As Deferred Outflows (Debits)
- Reported As Deferred Inflows (Credits)

GASB S - 65

#### Exhibit B

**FINANCIAL STATEMENTS**

<table>
<thead>
<tr>
<th>Private Universities</th>
<th>Public Universities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unrestricted Net Assets</td>
<td>Unrestricted Net Assets</td>
</tr>
<tr>
<td>Cash</td>
<td>Cash</td>
</tr>
<tr>
<td>9,700,000</td>
<td>9,700,000</td>
</tr>
<tr>
<td>Deferred Issue Cost</td>
<td>Deferred Issue Cost</td>
</tr>
<tr>
<td>100,000</td>
<td>100,000</td>
</tr>
<tr>
<td>Debt (Discount)</td>
<td>Debt (Discount)</td>
</tr>
<tr>
<td>200,000</td>
<td>200,000</td>
</tr>
<tr>
<td>Debt</td>
<td>Debt</td>
</tr>
<tr>
<td>10,000,000</td>
<td>10,000,000</td>
</tr>
<tr>
<td>Interest Expense</td>
<td>Interest Expense</td>
</tr>
<tr>
<td>15,000</td>
<td>10,000</td>
</tr>
<tr>
<td>Deferred Issue Cost</td>
<td>Deferred Issue Cost</td>
</tr>
<tr>
<td>5,000</td>
<td>Non-operating</td>
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<tr>
<td>Debt (Discount)</td>
<td>Debt (Discount)</td>
</tr>
<tr>
<td>10,000</td>
<td>10,000</td>
</tr>
<tr>
<td>CIP</td>
<td>CIP</td>
</tr>
<tr>
<td>Cash</td>
<td>Cash</td>
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<tr>
<td>9,700,000</td>
<td>9,700,000</td>
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<tr>
<td>Bridge &amp; Equipment</td>
<td>Bridge &amp; Equipment</td>
</tr>
<tr>
<td>CIP</td>
<td>CIP</td>
</tr>
<tr>
<td>9,700,000</td>
<td>9,700,000</td>
</tr>
</tbody>
</table>

#### Exhibit C

**Extinguishment of Debt**

<table>
<thead>
<tr>
<th>Issue, New Debt to Refund Old Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
</tr>
<tr>
<td>8,900,000</td>
</tr>
<tr>
<td>Issue Cost</td>
</tr>
<tr>
<td>100,000</td>
</tr>
<tr>
<td>New Debt</td>
</tr>
<tr>
<td>9,000,000</td>
</tr>
<tr>
<td>Gov't Securities w/Trustee</td>
</tr>
<tr>
<td>8,900,000</td>
</tr>
<tr>
<td>Cash Deposed w/Trustee</td>
</tr>
<tr>
<td>8,900,000</td>
</tr>
<tr>
<td>Old Debt</td>
</tr>
<tr>
<td>10,000,000</td>
</tr>
<tr>
<td>Gain</td>
</tr>
<tr>
<td>15,000</td>
</tr>
<tr>
<td>90,000</td>
</tr>
<tr>
<td>100,000</td>
</tr>
<tr>
<td>8,900,000</td>
</tr>
</tbody>
</table>
GASB S-7
GASB S-23

GASB S-7 Disclosures

- General Description of Transaction
- Difference Between Cash Flows of Old and New Debt
- Economic Gain or Loss Based on Present Value
- Report Amount of Defeased Debt Outstanding

Revised FASB Guidance
FASB ASC 405-470
(SFAS #125)
(SFAS #145)
Extinguished Liability

- Derecognize If:
  - Pay Creditor
  - Reacquisition by Debtor
  - Legally Released

SFAS #125 Disclosures

- In-substance Defeasance
  - General Description
  - Amount Extinguished
  - Nature of restrictions on assets set aside for future payments

Taxability: Advanced Refunding

- Revised IRS Section 149(d)(1) Eliminates the Exemption for Interest on Municipal Bonds Issued to Pre-Refund Outstanding Municipal Bonds
- Interest on Original Bond Remains Tax-Exempt
Capitalized Interest Guidance

- FASB ASC 835  
  (SFAS # 34/#62)  
- GASB S - 62

Capitalized Interest - FASB

- Concept - Include All Cost of Readying Asset
- Capitalization Period
- Borrowed Funds Restricted to Asset Acquisition
- Interest Capitalized
  - Actual Interest Cost Less Interest Earned

Exhibit D

Capitalization of Interest

<table>
<thead>
<tr>
<th>Construction Expenditures</th>
<th>Average during period</th>
<th>Interest Rate</th>
<th>Average T-bill rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>5,700,000</td>
<td>4,300,000</td>
<td>10%</td>
<td>7%</td>
</tr>
</tbody>
</table>

Designed Plant Accounts

<table>
<thead>
<tr>
<th>Construction in Process</th>
<th>Retirement of Indebtedness</th>
<th>Capital Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>Interest Expense 970,000</td>
<td>Buildings 970,000</td>
</tr>
<tr>
<td>Cash</td>
<td>Equity 970,000</td>
<td>Equity 970,000</td>
</tr>
<tr>
<td>Interest Income 339,500</td>
<td></td>
<td>Buildings 339,500</td>
</tr>
</tbody>
</table>

Cash 339,500
Interest Income 339,500
Interest Expense 970,000
Equity 970,000
## FINANCIAL STATEMENTS

<table>
<thead>
<tr>
<th></th>
<th>Private Universities</th>
<th>Public Universities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Unrestricted Net Assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest Expense</td>
<td>Cash</td>
<td>970,000</td>
</tr>
<tr>
<td></td>
<td>Buildings &amp; Equipment</td>
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<tr>
<td>Interest Expense</td>
<td>Interest Expense - non operating</td>
<td>970,000</td>
</tr>
<tr>
<td>Cash</td>
<td>Buildings &amp; Equipment</td>
<td>Interest Expense - non operating</td>
</tr>
<tr>
<td>Interest Income</td>
<td>Cash</td>
<td>339,500</td>
</tr>
<tr>
<td></td>
<td>Buildings &amp; Equipment</td>
<td>Interest Income - non operating</td>
</tr>
<tr>
<td>Interest Income</td>
<td>Interest Income - non operating</td>
<td>339,500</td>
</tr>
<tr>
<td>Buildings &amp; Equipment</td>
<td>Interest Income - non operating</td>
<td>339,500</td>
</tr>
</tbody>
</table>

### Capitalized Interest

**GASB S-89**

- Interest During Construction No Longer Capitalized
- Asset/Interest – Relevant/Comparable
- Asset Cost/Amount of Interest for a Period
- Reduces Complexity
- Less Costly to Compute

### Accounting For Leases

**FASB ASC 840 – 10 – 25**

(SFAS # 13/22/98)

**GASB S – 13/62**

FASB And GASB Have A Major/Multiple Year Project Underway To Increase Transparency And Comparability By Recognizing Assets And Liabilities Of A Lessee
Current Accounting for Leases

- Capital Lease
- Non-cancelable and one of:
  - Ownership Transfer
  - Bargain - Purchase Option
  - Term - 75% of Life
  - PV Payments 90% FMV

Capitalization

Record as Asset and Liability
Amortization

- Allocate Payments
  - Liability
  - Interest Expense
  - Depreciate

Amount Equal to PV Minimum Payments During Term
Exhibit E

**Accounting for Leases (1)**

**Capital Lease**

- 20 year lease agreement annual payments: $19,105.00
- Present value minimum lease payments: $19,105.38
- Present value of amount of $1 due for 20 periods at 5%: $13,085
- Amount to be capitalized: $250,000.00
- PV minimum lease payment: $250,000.00
- Less: payment on date lease consummated: $19,105.00
- Balance of Lease outstanding during first year: $230,895.00
- Discount rate: 0.05
- Interest in year two payment: $11,545.00
- Principal in year two: $7,560.00
- Annual Payment: $19,105.00

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**Designated Plant Accounts**

- **Current Unrestricted**
  - Cash: $19,105
  - Equity: $19,105
  - Int. Exp.: $11,454
  - Cash: $11,454
  - Payment-Prin.: $7,560
- **Capital Assets**
  - Leased Asset
    - Long-Term Lease Payable: $250,000
  - Interest Expense
    - Operating: $11,545
    - Cash: $11,545
  - Long-term Lease payable
    - Non-current: $7,560

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**FINANCIAL STATEMENTS**

- **Private Universities**
- **Public Universities**

- **Unrestricted Net Assets**
  - Lease Asset: $250,000
  - Long-Term Lease Payable
    - Non-current: $11,545
  - Interest Expense
    - Operating: $11,545
  - Cash: $7,560
  - Long-term Lease payable
    - Non-current: $7,560
  - Cash: $7,560
FASB And GASB Have Proposed New Lease Standards

- FASB Proposes All Leases Convey a Right-of-Use, Which Results in Both an Asset and a Liability Which Should Be Reflected on the Balance Sheet of the Lessees.
- Straight Line Amortization of the Right-of-Use Asset Will be Recognized Separately From the Lease Liability.
- Beginning After Dec. 15, 2018 (FY 20 for Most Colleges).

GASB Lease Accounting Proposal

- GASB’s Basic Premise Is That All Leases Are Financings of the Right-to-Use an Asset
- Expected Release FY 18. Effective Date FY20.