SECTION II – SPECIFIC COMPLIANCE

SCHOOL DISTRICT BOOKKEEPING

The State Board of Education has, in accordance with law, prescribed a uniform double-entry system of bookkeeping for use in all school districts and is authorized to compel its use. (*N.J.S.A.* 18A:4-14 and *N.J.A.C.* 6A:23A-16)

The Uniform Minimum Chart of Accounts for New Jersey Public School (2008 Edition) (COA) was originally published in 1992 and revised effective July 1, 2009. The revised COA is available on the website http://www.nj.gov/education/finance/fp/af/coa/.

GAAP distinguishes between funds which benefit the district (Permanent funds) and those for which the district acts as a trustee or agent, but where the resources benefit other governments, individuals, or organizations (Trust or Fiduciary funds). Governmental fund 50 should be used to record the accounting for Permanent funds. Expendable trusts that benefit the district should be included in the Special Revenue fund. The Proprietary funds use fund 60 and fund 70, and the Fiduciary funds use funds 80, 90, and 95. When the district uses the reimbursable or pay as you go method for unemployment, the Unemployment Compensation Trust would be included in fund 80. The resources and changes in net assets of a private purpose scholarship fund would also be reported here. The Fiduciary funds are not included in the accrual level statements (A - series) since they are not assets of the district.

The following is a listing of funds using the revised chart of accounts structure effective July 1, 2004:

Governmental Funds
Fund 10 (General fund)
Fund 20 (Special revenue fund)
Fund 30 (Capital projects fund)
Fund 40 (Debt service fund)
Fund 50 (Permanent fund)

Proprietary funds
Fund 60 (Enterprise fund)
Fund 70 (Internal service fund)

Fiduciary funds
Fund 80 (Trust funds)
Fund 90 (Agency funds)
Fund 95 (Student activity funds)

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<u>SECTION II – SPECIFIC COMPLIANCE</u>
<u>FUND 10 –GENERAL FUND</u>

Optional Treasurer of School Moneys

P.L. 2010, c.39, effective July 2, 2010, made the treasurer of school moneys an optional position. Upon the board's election to eliminate the treasurer's position, the law requires a shifting of internal control and internal reporting responsibilities from the treasurer to the board secretary and chief school administrator. Accordingly, Boards of Education electing to eliminate the treasurer's position must consider the impact on the district's internal controls. This law supplemented chapter 17 of Title 18A and amended various sections of the New Jersey statutes. The following is an overview of responsibilities of the board secretary when the treasurer position is eliminated. For a complete understanding of the changes, see P.L. 2010, c.39.

N.J.S.A. 18A:17-9.1 - the board secretary will receive and hold in trust all school moneys, except any moneys derived from athletic events or other activities of pupil organizations of the district.

N.J.S.A. 18A:17-9.2 - the board secretary shall keep a record of the sums received and paid out by him in accordance with the uniform system of bookkeeping prescribed by the State board.

N.J.S.A. 18A:19-9 as amended requires that payrolls must be certified by the president and secretary of the board and the chief school administrator.

N.J.S.A. 18A:19-10 as amended requires the board secretary to draw and deposit the warrants in separate bank accounts as a net payroll account and an agency account for payroll deductions and associated board contributions (agency account); authorized signatories on the payroll account must include the secretary and a board designee.

N.J.S.A. 18A:19-10 amended provides that the board secretary shall draw and deposit the warrants.

Board Secretary and (Optional) Treasurer Reports

In accordance with *N.J.S.A.* 18A:17-9(a) amended, the board secretary shall report to the board at each regular monthly meeting the amount of total appropriations and the cash receipts for each account, the amount for which warrants have been drawn against each account, the amounts of orders or contractual obligations incurred and chargeable against each account year to date, and since the date of the last report, the cash and appropriation balances for each account and fund, and the reconciled bank account balances. At the close of each fiscal year, the board secretary shall present to the board a detailed report of its financial transactions during such year and file a copy with the executive county superintendent on or before August 1st of each year.

For a district board of education that elects to maintain the treasurer's position, *N.J.S.A.* 18A:17-36 requires the treasurer to report to the board monthly a detailed account of all receipts, the amounts of all warrants signed by him/her since the date of the last report and the accounts against which the warrants were drawn, and the balance to the credit of each account. At the close of each fiscal year, the treasurer shall present an annual report showing the amounts received and disbursed for school purposes during said year and file a copy with the executive county superintendent on or before August 1st of each year.

The separate monthly board secretary and treasurer (where the board of education elects to maintain the position) reports must be reconciled on a monthly basis.

Cash Reconciliation

The cash accounts must be reconciled. *N.J.S.A.*18A:17-9 amended, provides that the chief school administrator or board designee other than the secretary must prepare the monthly reconciliations of all bank accounts prior to the completion of the secretary's monthly report. Reconciliation of payrolls and bond and interest accounts are to be made in all districts maintaining such accounts and must be permanently recorded and filed for future reference. The auditor must verify the reconciliation of all cash accounts of the school district.

Bank reconciliation statements are not required to be exhibited in the audit report. Workpapers must be available for review upon request.

Petty Cash Funds

N.J.A.C. 6A:23A-16.8 states "Pursuant to the provisions of *N.J.S.A.* 18A:19-13, a district board of education or charter school board of trustees may establish on July 1 of each year, or as needed, a cash fund or funds for the purpose of making immediate payments of comparatively small amounts."

To be in compliance with the administrative code, the board must establish the amounts authorized for each fund, and set the maximum allowable individual expenditure. The board must designate custodians for each fund and must establish the minimum time period for the custodian to report on fund activity. Petty cash accounts must be closed out at year-end and unexpended cash deposited in the bank by June 30.

Summer Payment Plans

N.J.S.A. 18A:29-3 authorizes a district board of education to establish a Summer Payment Plan which will provide for withholding 10 percent of the salary of 10-month employees during the academic year. *N.J.A.C.* 6A:23A-16.9 states "The district board of education shall ensure that the amount withheld earns interest and is available to the employee either at the end of the academic year or in installments prior to September 1."

SOC 1 Report (Service Organization Controls Report) – Formerly SAS #70 Reports

N.J.A.C. 6A:23A-16.6 requires that district boards of education which contract for electronic data processing bookkeeping services including services provided by software vendors, payroll service vendors, and other service organizations, shall annually have an audit prepared or obtain a copy of an audit of the internal controls of the service company. Such audit shall be as prescribed by Statement on Standards for Attestation Engagements (SSAE) No. 16, *Reporting on Controls at a Service Organization*. SSAE No. 16 was issued by the AICPA in April 2010 and is effective for service organization auditor reports for periods ending on or after June 15, 2011. SSAE No. 16 supersedes *Statement of Auditing Standards No. 70* (SAS 70), as amended by SAS 88, of the American Institute of Certified Public Accountants. A SOC 1 report (Service Organization Controls Report) is a report on Controls at a Service Organization which are relevant to user entities' internal control over financial reporting. Previously known as SAS #70 Reports, the SOC 1 report may be either a Type 1 or a Type 2 report.

- Type I – Report on policies and procedures placed in operation. This report may be an effective and efficient way for the district auditor to gain an understanding of the internal controls of the service organization.

- Type II – Report on policies and procedures placed in operation and tests of operating effectiveness. This report includes a description of the tests of operating effectiveness and the results of those tests. If the controls are present and operating effectively, the district's auditor may choose to assess control risk below the maximum for financial statement assertions related to the service organization transactions. This is a decision made by the district auditor.

Auditors are advised to review Chapter 4, Field Work Standards for Financial Audits, of the *Government Auditing Standards* (2007 edition) available electronically at the website http://www.gao.gov/yellowbook for further guidance on internal controls.

Third Party Disbursements

N.J.S.A. 52:27D-20.1 *Contracts for third-party disbursement services*, gives the Local Finance Board, in consultation with the Commissioner of Education, the authority to adopt regulations permitting district boards of education to contract with a third-party disbursement service organization in order to make payments and execute financial transactions for those purposes.

The rules on third party disbursements can be found in *N.J.A.C*. 5:30-17 et seq. District boards of education are advised to review the rules prior to engaging a third party disbursement service organization.

N.J.A.C. 5:30-17 et seq., Electronic Disbursement Controls for Payroll Purposes can be found at http://www.state.nj.us/dca/lgs/fiscal/generalpubs/payroll%20_agency_%20handbook_1.pdf

N.J.S.A. 18A:19-10 amended, requires districts to maintain separate bank accounts for net payroll, and for payroll deductions and associated board contributions (agency account). In a district that does not maintain the position of treasurer of school moneys, the secretary shall draw and deposit the warrants. Where the district maintains the position of treasurer of school moneys, the treasurer shall deposit the warrants.

N.J.S.A. 18A:19-10 amended, requires that authorized signatories on the payroll account must include the secretary and a board designee.

Investments

Several statutes govern permissible investment of school monies by New Jersey school districts. In a district which appoints a treasurer of school moneys, *N.J.S.A.* 18A:17-34 gives the treasurer of the school district the authority to deposit school moneys in any bank or banking institutions of this state designated as a depository of school monies. In a district that does not have a position of treasurer of school moneys, the board secretary when required by the board resolution has that authority (*N.J.S.A.* 18A:17-9.1). Under *N.J.S.A.* 17:9-41 et seq., the Governmental Unit Deposit Protection Act (GUDPA), a school district may deposit public funds in a public depository if such funds are secured in accordance with GUDPA. This statute defines a public depository as:

> "a State or federally chartered bank, savings bank or an association located in this State or a state or federally chartered bank, savings bank or an association located in another state with a branch office in this State, the deposits of which are insured by the Federal Deposit Insurance Corporation and which receives or holds public funds on deposit."

N.J.S.A. 18A:20-37 provides for the specific types of securities that the board of education can authorize to be purchased and sets forth general investment practice requirements. It also provides for the specific types of securities which may be purchased and registered in a school district's name. While the types of securities and requirements are too extensive to list, the statute includes governmental money markets funds and bonds or other obligations having a maturity date of not more than 397 days from the date of purchase, approved by the Division of Investments in the Department of Treasury for investment by school districts. The division does not publish a listing of approved investments but districts may request approval of a specific security by sending a letter to the address on the following page:

Director
Division of Investments
P.O. Box 290
Trenton, NJ 08625

The Department of Education does not have the authority to determine compliance with GUDPA or review and approve the types of securities a school district can utilize. Districts should consult with their legal counsel and direct any questions on the permissibility of a specific security pursuant to N.J.S.A. 18A:20-37 to the Division of Investments in the Department of Treasury at the above address.

Further information on GUDPA or on banking institutions may be found at the Department of Banking and Insurance website http://www.state.nj.us/dobi/division_banking/depositories/gudpa.htm. A school district which is unsure as to whether the bank/institution is certified as a depository should request from the bank/institution a copy of the "Notification of Eligibility" or may contact the Department of Banking and Insurance.

Districts were required to implement GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools," effective for fiscal year end June 30, 1998. This statement establishes fair value accounting and financial reporting standards for certain types of investments held by governmental entities other than external investment pools. This should have a limited impact on school districts. For government entities other than external investment pools, this statement establishes accounting and financial reporting standards for the following investments: participating interest-earning investment contracts, external investment pools, open-end mutual funds, debt securities, and equity securities, option contracts, stock warrants and stock rights that have readily determinable fair values.

The implementation of GASB Statement No. 31 did not supersede the required disclosures included in the CAFR in accordance with GASB Statement No. 3, "Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements." It represents a change to the method at which investments are valued for accounting and financial reporting and provides for additional disclosures regarding the valuing of investments.

GASB Statement No. 40, "Deposit and Investment Risk Disclosures, an amendment of GASB Statement No. 3" is effective for financial statements for periods beginning after June 15, 2004 and states:

> "…disclosures generally referred to as category 1 and 2 deposits and investments are eliminated. However, this Statement does not change the required disclosure of authorized investments and it maintains, with modification, the level-of-detail disclosure requirements of Statement 3." Statement 40 is designed to inform financial statement users about deposit and investment risks that could affect a government's ability to provide services and meet its obligations as they become due. The reduction of existing custodial credit risk disclosures follow from federal banking reforms adopted since the release of Statement 3.

District auditors should refer to the statement for further understanding and for illustrations of disclosures.

Revenues and Receipts

Revenues accruing to the board of education for the period under audit must be verified. Receipts for the year and accounts receivable at the close of the year must be verified as to source and disposition. Revenues must be delineated by type and recorded in the proper fund. Common revenues and the funds in which they are reported are included in *The Uniform Minimum Chart of Accounts Handbook for New Jersey Public School Districts*. The auditor must comment in detail on any irregularity in the method of handling receipts and revenues as a result of audit tests performed.

N.J.S.A. 18A:39-31 (P.L. 2010, c.121) permits boards of education to enter into contracts for the sale of advertising space on school buses. *N.J.A.C.* 6A:27-7.10, 7.11 and 7.12 have been amended to permit boards of education to enter into a contract for the sale of advertising space on the exterior sides of school buses owned or leased by the school district, subject to prohibited items in *N.J.S.A.* 18A:39-31, the aforementioned code, and any other products or services the board deems inappropriate. Prior to the June 4, 2012 effective date of the regulations, a contract for the sale of advertising space on the exterior sides of a school bus was prohibited. *N.J.S.A* 18A:39-31(b) provides that 50% of any revenue so generated be used by the board to offset the fuel costs of providing pupil transportation services and 50% of the revenue shall be used to support any programs or services deemed appropriate by the board of education.

N.J.S.A. 18A:17-9.1 provides that for a district that does not maintain the position of treasurer of school moneys, the board secretary will receive and hold moneys. *N.J.S.A.* 18A:17-9.2 provides that in a school district that does not have a treasurer of school moneys, the board secretary will keep a record of the sums received.

Extraordinary Aid

The awards for 2011-12 extraordinary aid (ExAid) were posted in the district's state aid folders on June 4, 2012. Guidance for budgeting and recording the 2011-12 ExAid award was provided to the districts within the June 4 award notification letter. The following link may be used to access the award notice: http://education.state.nj.us/broadcasts/2012/JUN/04/7123/Ex%20Aid.pdf

Extraordinary Aid awards are recorded in the general fund, account 10-3131. Since actual payment will not be made until after the end of the fiscal year districts must also establish a receivable for the appropriate amount of anticipated payment (*N.J.S.A.* 18A:7F-55c). This amount can be excluded from the June 30, 2012 excess surplus calculation only if the district can clearly document that they did not budget this additional aid during the 2011-12 fiscal year for which they filed an application.

Audit procedures, similar to the ASSA, can be found in the *State Aid/Grants Compliance Supplement* at: http://www.nj.gov/education/finance/fp/audit/1112. Extraordinary aid applications are made online, with the Department's determination of aid based on the applications submitted for each individual student. Additional information on ExAid including a Frequently Asked Questions document can be found at https://homeroom.state.nj.us/exaid.htm.

The exclusion of extraordinary aid from the audited excess surplus calculation should be documented on the "Extraordinary Aid Adjustment" line. This will also require the submission of a brief letter or memo explaining the circumstances surrounding the exclusion, and if applicable, how the exclusion relates to the appearance of the excess surplus warning message on the Audit Summary (Audsum) transmittal form.

N.J.A.C. 6A:23A-13.3(d)6 provides that a district board of education may at any time without Commissioner approval appropriate surplus generated from state revenue, such as extraordinary aid, that has been excluded from the excess surplus calculation in the prior year.

District Taxes

District taxes must be recorded in the fund for which they were voted (Type II) or were certified by the Board of School Estimate (Type I). Additional amounts certified to the county board of taxation after the issuance of tax bills by the municipality will be shown as an adjustment on the district's subsequent year's certificate and report of school taxes. These adjustments are generally the result of Commissioner restorations for budget appeals and/or additional certifications for unanticipated debt service expenditures. These additional certifications should be reported as revenue via the accrual of a tax levy receivable.

N.J.S.A. 54:4-75, as amended by P.L. 2010, c. 39, states, "The governing body of each municipality shall pay over to the board secretary or treasurer of school moneys, as appropriate, in the case of school districts in which appropriations for school purposes are made by the inhabitants of the school district, within forty days after the beginning of the school year, twenty percent (20%) of the appropriation for local school purposes, and thereafter, but prior to the last day of the school year, the balance of the moneys raised in the municipality for school purposes in such amounts as may from time to time be requested by the Board of Education, within thirty days after each request."

The auditor should comment on any uncollected taxes as of June 30 (other than the special accruals referred to above), and make a recommendation that the board of education request the remittance of the balance from the municipality.

Tuition (*N.J.A.C.* 6A:23A-17.1)

Tuition revenue is recorded in the general fund. The procedures for determining tuition rates are detailed in *N.J.A.C.* 6A:23A-17.1. Because it is "measurable and available" the entire tuition charged for the school year is revenue of the year even though part of the charge is uncollected at year-end. Tuition or program fees should not be charged for accredited Adult Education programs operating for the purposes outlined in *N.J.S.A.* 18A:50-12, since pupils enrolled in such programs are included on the Application for State School Aid. Fees collected for non-accredited Adult Education programs are miscellaneous general fund revenue, not tuition.

Local school district auditors should compare tentative tuition charges in the current fiscal year to the rate certified by the Department of Education. The auditor must comment on whether appropriate billing adjustments have been made for the differences between tentative and actual charges. In accordance with the readoption of *N.J.A.C.* 6A:23A-17.1(f), the certification of tuition rates occurs after two years, versus three. This began with the certification of 2008-09 rates and the transition to the shorter certification cycle was made during the 2010-11 budget process. In the 2010-11 budget, districts were required to include any applicable tuition adjustment for the certification of 2007-08 and 2008-09 rates. In the 2011-12 budget districts were required to include any applicable tuition adjustment for the certification of the 2009-10 rates. Consult *N.J.A.C.* 6A:23A-17.1(e). Local school district auditors should refer to *N.J.A.C.*

6A:23A-17.4 for auditing tuition rates for county vocational schools; and *N.J.A.C*. 6A:23A-17.7 for auditing rates for county special services schools when these types of LEAs are audited.

Beginning with the 2008-09 school year, a receiving district must phase-out the reduction of the “actual cost per pupil” by the amount of Abbott Parity Remedy Aid, Educational Opportunity Aid, and Discretionary Educational Opportunity Aid, pursuant to section 61 of P.L. 2007, c.260. The receiving district will reduce the actual cost per student for all grade and program categories by the total amount of the above aid received in the 2007-08 school year by .80 in the 2008-09 school year. Phase out reductions are .60 (2009-10), .40 (2010-11), and .20 (2011-12). For the 2012-2013 school year and thereafter, no reduction will be made to the “actual cost per pupil.” Auditors should refer to *N.J.A.C.* 6A:23A-8.7 for additional guidance.

Local school district auditors must perform procedures to determine that the following requirements are met and should refer to the guidance on Fund Balance Classification in Section II-10.20 of this Audit Program for reporting the tuition reserve in the CAFR and to Section III-5 for guidance on including the tuition reserve in Audsum. **There are specific lines for the opening and ending balance for each year of the reserve**.

1. The district used the Budget Software tuition worksheet (only applicable to regular districts) or another Department of Education prescribed method for estimated tuition charges (Estimated Cost Per Pupil for Tuition Purposes).

2. Receivables and/or payables are based upon uncollected tuition billed.

3. Regular tuition adjustments based upon Department of Education certification of rates are not recognized as revenue and/or expenditures until the second year after the contract year and that the tuition adjustments are correctly reflected in the amounts reported as tuition revenue (receiving district) or tuition expenditures (sending district).

4. In accordance with the readoption of NJAC 6A:23A-17.1(f), the certification of tuition rates occurs after two years, not three. This began with the certification of 2008-09 rates and the transition to the shorter certification cycle was completed during the 2010-11 budget process. In the 2010-11 budget districts were required to include any applicable tuition adjustment for the certification of 2007-08 and 2008-09 rates. In the 2011-12 budget districts were required to include any applicable tuition adjustment for the certification of 2009-10 rates.

5. If at the end of the contract year when a district board of education anticipates that a large tuition adjustment will be required in the second year following the contract year, the district board of education may restrict fund balance up to 10 percent of the estimated tuition cost in the contract year, in a reserve for tuition adjustments. The tuition reserve is available only for districts that have a sending/receiving relationship. Full appropriation shall be made in the second year. This change was first reflected in the 2010-11 budget when two years (2007-08 and 2008-09) reserves were required to be budgeted. (*N.J.A.C.* 6A:23A-17.1(f)(8)). In the 2011-12 budget districts were required to include any applicable tuition adjustment for the certification of 2009-10 rates.

6. For the 2011-12 budget year districts were permitted and required to withdraw and budget the June 30, 2010 amounts deposited in the tuition reserve account for the actual 2009-10 certified tuition rate adjustments. The money was reserved in 2009-10 based on an estimated tuition adjustment in 2011-12.

7. A district may have at June 30, 2012 a reserve for each applicable year 2010-11 and 2011-12. The tuition reserve for each year should be presented separately on the *Budgetary Comparison Schedule – General Fund* (Exhibit C-1) in the Recapitulation of Balances and on Audsum. There is no authority to increase the tuition reserve by interest earnings.

Local school district auditors must make appropriate comments and recommendations for any findings related to these procedures.

Reporting On-Behalf Payments

GASB Statement No. 24 requires that an employer government recognize revenue and expenditures for on-behalf payments for fringe benefits and salaries. On-behalf payments for fringe benefits and salaries are direct payments made by one entity (the paying entity or paying government) to a third-party recipient for the employees of another legally separate entity (the employer entity or employer government). In applying this accounting directive in New Jersey, districts are required to include in their CAFR as both a revenue and expenditure both the pension contributions made directly to the TPAF by the state on their behalf, as well as the reimbursed social security amounts related to its employees that are TPAF members. The department annually provides district information on the amounts paid on their behalf for employer contributions to the TPAF on the DOE website at http://www.nj.gov/education/finance/fp/audit/.

Districts should prepare a schedule of the amounts reimbursed by the state for the current year FICA employer contribution for its TPAF members on an accrual basis. That is, the current year amount equals total cash reimbursement received during the current year less the prior year June 30 receivable amount plus the current year June 30 receivable balance. **The on-behalf payments will be included in the CAFR as non-budgetary revenue and expenditure items, similar to the reporting of assets acquired under capital leases.** Districts are not required to include these amounts in their annual school budgets or monthly reports of the board secretary. These amounts should be excluded from the Type A programs threshold calculation. For further guidance, auditors should refer to Section II-SA, Federal and State Audit Requirements, of this Audit Program.

Compensation Reporting

N.J.S.A. 18A:23-2.1 requires that the annual audit include test measures to assure that documentation prepared for income tax related purposes complies fully with the requirements of federal and state laws and regulations regarding the compensation which is required to be reported. See the *State Aid/Compliance Supplement* available on the website: http://www.nj.gov/education/finance/fp/audit/1112 for suggested audit procedures.

The following links are provided to assist auditors and districts in complying with this law: Internal Revenue Service Governmental Entities website - www.irs.gov/govt/fslg/index.html. At that site, select "FSLG Toolkit" for a listing of several tax guides for payroll and fringe benefits (FSLG Taxable Fringe Benefits Guide).

Information on tax filings for the State of New Jersey can be obtained through the website for Department of Treasury, http://www.state.nj.us/treasury/, the Division of Revenue link for "Tax and Employer Filings and Payments" http://www.state.nj.us/treasury/revenue/, or the Division of Taxation link http://www.state.nj.us/treasury/taxation/. Generally, anything regarded as "wages" for federal withholding purposes is subject to withholding for the NJ Income Tax. See also *N.J.S.A.* 54:A1-1 et seq. Auditors are advised to contact the NJ Department of Treasury directly for technical questions regarding taxable compensation for state reporting.

N.J.S.A. 18A:17-14.4 requires the school business administrator, or any other person designated by the board of education, to certify to the Department of Treasury that all documentation prepared for income tax related purposes, in regard to superintendents of schools, assistant superintendents of schools and school business administrators, complies fully with the requirements of federal and state laws and regulations regarding the types of compensation which are required to be reported. The certification is due annually on or before March 15 for the certification year (calendar year). The first year for this filing was December 31, 2007, and was due March 15, 2008. The form and instructions for this certification are available on the Department of Treasury's website http://www.nj.gov/treasury/taxation/pdf/other_forms/misc/e_cert1.pdf.

Pensionable Wages

All defined benefit plans administered by the NJ Division of Pensions and Benefits require that employee contributions be remitted regularly to the Division. For school districts, these include the TPAF and PERS. School districts are issued a Quarterly Report of Contributions to report and reconcile employee pension information and monies each calendar quarter. Districts may only include pensionable wages as defined by the Division of Pensions and Benefits. The following discussion is provided to assist auditors when testing payroll and pensionable wages.

The Division of Pensions and Benefits defines pensionable wages or creditable compensation as the compensation of a member subject to pension and group life insurance contributions and creditable for retirement and death benefits administered by the Teachers' Pension and Annuity Fund (TPAF). Creditable compensation is limited to "base salary" which is defined under *N.J.A.C.* 17:3-4.1. Base salary means the annual compensation of a member, in accordance with contracts, ordinances, resolutions, or other established salary policies of the member's employer for all employees in the same position, or all employees covered by the same collective bargaining agreement, which is reported in regular, periodic installments in accordance with the payroll cycle of the employer. Creditable compensation does not include "extra compensation" which is defined in *N.J.A.C.* 17:3-4.1. The Board of Trustees may question the compensation of any member or retiree to determine its creditability where there is evidence that compensation reported as base pay includes extra compensation. The examples of extra compensation listed in the citation above are not meant to be all inclusive.

For the Public Employees' Retirement System (PERS), auditors should refer to *N.J.A.C.* 17:2-4.1, for a similar definition of creditable compensation.

For further guidance, refer to the Division of Pensions and Benefits Employer's Pensions and Benefits Administrative Manual at the website: http://www.state.nj.us/treasury/pensions/epbam/index.htm. Under the "Shortcuts" there is a toolbar "Employer Financial Services/Reporting Contributions." Within that link, The Quarterly Report of Contributions (ROC), column #6 defines base salary and extra compensation. The information contained in the manual should not be quoted as "law." For a ruling that involves pension law, please write to the Division of Pensions and Benefits. Inquiries may be made by email at the link in the above website or by writing to the following address:

The Division of Pensions and Benefits
Attn: EPBAM Editor
P.O. Box 295
Trenton, NJ 08625-0295

Refunds

Refunds on current year expenditures are a credit to the applicable expenditure line account. Refunds on prior year expenditures, and sales of books and manual training materials and products, are miscellaneous income, not refunds. Proceeds from the sale of land, buildings and equipment are other financing sources.

Telecommunications Act of 1996 – Universal Service Fund (E-rate)

The Schools and Libraries Universal Service Fund, known as the "E-rate" was created as part of the Telecommunications Act of 1996 to provide affordable access to modern telecommunications and information services to all eligible schools and libraries in the U.S. The School and Libraries Corporation (SLC) was established by the FCC to administer the Schools and Libraries Universal Service Fund. All public and private schools and libraries qualify for funding based on their level of economic disadvantage (based on the percentage of students eligible for the national school lunch program) and their location, rural or urban. The offset to the reduction in the expenditure is either to accounts receivable if a refund is due or to accounts payable if unpaid at June 30, 2012. Additional information is available at the Department of Education, Office of Technology website at www.state.nj.us/education/techno/toc.htm and at the School and Libraries website at www.sl.universalservice.org.

Cancellations

Cancelled prior year contractual orders and canceled prior year tuition receivables are reflected in the audit report as revenues and expenditures, respectively. Cancellations of prior year reserve for encumbrances increase the amount available for expenditure in the current year.

Travel Expenditures

N.J.S.A. 18A:.11-12 limits expenditures for travel. Travel regulations *(N.J.A.C.* 6A:23A:7.1 et seq.) provide rules on school district travel policies and procedures. District auditors can access this at http://www.state.nj.us/education/code/current/title6a/chap23a.pdf. Please note that the travel guidance is applicable to all funds. District auditors should refer to *The State Aid/Compliance Supplement* for suggested audit procedures related to travel. Commissioner approval of requests for specific conferences is posted at this website: http://www.state.nj.us/education/genfo/travel/.

Travel Regulation Circular No. 11-05-OMB effective December 16, 2010 supersedes 08-19-OMB. This circular focuses on efficiencies in travel (one bag peer flight per employee, long term parking, reduce mileage reimbursement for normal commute) and includes updated federal per diems.

Entertainment, Meals, and Refreshments Circular No. 11-09-OMB effective January 5, 2011 supersedes 06-14-OMB and allows receptions for awards, retirements, not to exceed $25 per month per agency.

Health Insurance Policies

The department issued a hotline concerning audit issues/procedures regarding certain insurance policies held by New Jersey school districts dated August 30, 1995. At that time, we were seeking an opinion from the Office of the Attorney General on questions raised regarding the custody of funds and payment of claims. In response to that request, we were advised that the enactment of Chapter 74, P.L. 1995 authorized school districts to enter into minimum premium insurance policies with insurance companies authorized to do business in the state although those policies may involve different cash management methods than those required by existing statute.

The 1995 hotline was issued after review of policy terms and discussions with both public school accountants and insurance company representatives. Based on that review, the following issues were identified:

Districts with minimum premium policies commonly have three accounts with the carrier:

1) a termination reserve account
2) a claims account
3) a premium stabilization account

The <u>termination reserve account</u> generally represents funds earmarked for the district's liability for claims which have been incurred but not reported (IBNR), also known as the "run-off" liability. The IBNR liability amount is calculated annually by the carrier's actuaries and provided to the policyholder. The <u>claims account</u> is used for the payment of claims filed. The contracted monthly premium estimate (including the employee’s contribution to medical premiums) is deposited into this account. The monthly deposit may or may not include the administrative fee paid to the carrier. In some cases, the fee is a separate remittance. The <u>premium stabilization accounts</u> are used as a mechanism to smooth insurance premium payments. Commonly, any funds remaining in the claims account at the end of the year are transferred to the premium stabilization account for use in future years in the event of "premium" increases. Premium stabilization funds are often attached to participating and fully funded policies in which rebates are based on a retrospective review of claims filed during the policy period. These funds (rebates) are maintained in an account, in the district's name, and are used to smooth future years' premium payments. Payments from these accounts for other than insurance premiums are prohibited and circumvent the budgetary process.

In the past, the aforementioned accounts may have not been reflected in the district accounting records or were inaccurately reported as fund balance. Public school accountants should review the terms of district policies and statements/monthly activity reports issued by the carrier. If the district has a minimum premium policy a confirmation should be issued to the insurance carrier regarding the following:

- The existence of and amount of June 30 balances in accounts in the district's name held on their behalf by the carrier*
- District liability for the IBNR claims at June 30
- District liability for claims that were filed but unpaid at June 30
- Composition of the accounts (what are the types of underlying investments made on the district's behalf)*
- Investment income earned during the year on district funds held by the carrier*

Auditors may wish to obtain confirmation from the carrier that the expenditures made from the claims accounts were for valid claims if direct testing is not possible from district records. Items noted with an (*) should be confirmed in situations where it appears that a premium stabilization account exists under a participating or fully funded policy.

The confirmed information as well as the balances in any accounts related to the policies that are held by the district itself should be used to determine the proper presentation in the CAFR. The assets (total of the June 30 account balances) will be compared to the related liabilities (total of the June 30 IBNR claims and claims in process at June 30). Any excess assets should be included in the amount reported as unreserved general fund surplus. If the liabilities exceed the assets, the district's unreserved general fund surplus must also be considered. The accrual made for the claims should not put the general fund into a deficit position. That is, the total liabilities should be subtracted from the total of the June 30 unreserved general fund surplus plus the total assets. The amount of liabilities in excess of the total of surplus and assets should be shown as a liability in the districtwide *Statement of Net Assets* and the June 30 general fund unreserved surplus reported as zero. For minimum premium policies, the current year expenditures reported for insurance premiums/claims should represent the total of the amount of claims and administrative fees paid in the current year related to the current year, the accrual for the unpaid claims in process, and the change in the June 30 balance in the IBNR liability between the current year and the prior year. For any type of policy, it must not include any excess premium payments transferred to a premium stabilization account.

The funds held by the district or the carrier on the district's behalf are included in the general fund balance sheet as cash, cash equivalents, or investments.

The June 30 general fund accounts payable balance should include the amount of claims in process as of that date. It should not include the IBNR liability. The IBNR liability should be reported in the general fund balance sheet an accrued liability labeled "Accrued Liability for Insurance Claims."

The notes to the financial statements should clearly disclose the terms of the policies and provide explanations of the related balance sheet accounts.

Refer to page II-90.1 of this Audit Program for audit guidance regarding employee health insurance withholding.

Sale and Lease-back Contracts

*N.J.S.A.*18A:20-4.2(h) authorizes boards of education to enter into sale and lease-back contracts on certain instructional materials (i.e. textbooks). The district can acquire through sale and lease-back textbooks and non-consumable instructional materials provided that the sale price and principal amount of the lease-back do not exceed the fair market value of the textbooks and instructional materials and that the interest rate applied in the lease-back is consistent with prevailing market rates or is less. The lease-back can be for any term not exceeding in the aggregate of five years.

Proceeds from the sale and lease-back of textbooks and non-consumable instructional materials shall not be included in the calculation of excess undesignated general fund balance during the budget year in which they are realized. A board of education may establish a reserve account in the general fund with all or part of the proceeds from the sale and lease-back provided that subsequent appropriations from the reserve account shall only be made within the original budget certified for taxes or as approved by the Commissioner for good cause.

If the board of education establishes a reserve in the year the proceeds are realized, then the calculation of excess surplus will not include the June 30 legally restricted reserve balance in that year and future years.

The exclusion of sale and lease-back funds from the audited excess surplus calculation should be documented on the "Sale and Lease-Back" line.

Required Maintenance

Beginning in ten years following enactment of P.L. 2000, c.72 (EFCFA), *N.J.S.A.* 18A:7G-9, to receive funding under EFCFA, districts will be required to demonstrate a net investment in required maintenance of at least 2 percent of the replacement cost of the related school facility (determined pursuant to subsection b. of section 7). For new construction, additions, and school facilities aided under the act, beginning in the fourth year after occupancy of the school facility, districts must demonstrate an investment in required maintenance in the prior year of at least two-tenths of 1 percent of the replacement cost of the school facility.

To support the demonstration of this requirement, districts must include a schedule of required maintenance expenditures for each year by school facility (as defined under *N.J.A.C.* 6A:26-1.2) in the CAFR. **This schedule must reflect each year beginning with June 30, 2001 up to ten years.** For reporting 2001 and 2002 required maintenance expenditures (11-000-261-xxx), a district was permitted to allocate the total to each school facility and other facilities by proration according to its gross square footage.

Districts are required to maintain their accounting records for required maintenance at the school facility level and will be required to "have available the expenditure records, detailed by school facility, for verification by the district auditor beginning in the year 2002-2003" (*N.J.A.C.* 6A:26A-2.2(c)). Auditor verification should include a review of classification of expenditures and documents to support the school level expenditures for object code 261 and random testing of purchase orders/vouchers. Auditors should be aware that salaries split between custodial and required maintenance need "task specific documentation."

A sample Schedule of Required Maintenance for School Facilities (Exhibit J-19) is included on the website http://www.nj.gov/education/finance/fp/cafr/outline/J-16toJ-20.xls. The schedule should indicate the gross square footage in the column preceding the current year expenditure. All district types should complete this schedule. If the district has no school facilities projects, the district should indicate "N/A" on the schedule.

Restricted Appropriations/Balances

There are no Commissioner tax levy cap waivers for 2011-2012. Accordingly, for 2011-12, no lines of appropriation have been increased or are transfer restricted as a result of a Commissioner waiver.

Districts that added to the waiver offset reserve (a component of legal reserves) at year end June 30, 2010 were required to withdraw the amount so reserved during the 2011-12 fiscal year. Districts that had any remaining waiver offset reserve balance at June 30, 2011 were required to budget that amount in the 2012-13 budget. Any balance remaining at June 30, 2012 should be reported as Waiver Offset Reserve – Designated for Subsequent Year.

Additional Spending Proposals

Additional spending proposals are supported by: (1) a formal board resolution, "Separate Proposal Summary," (2) an advertised description of the purpose or purposes and amount, (3) a separate ballot question or questions for the associated tax levy, (4) an itemized accounting for the appropriations, and (5) a merged final budget including the base budget and approved appropriations.

N.J.A.C. 6A:23A-12.13(a)10 requires that amounts approved by the local voters or board of school estimate shall be used exclusively for the purpose(s) contained in the associated question(s). Additionally, each question must contain sufficient funds to carry out the specific purpose or purposes contained therein and no funds shall be included in the base budget for implementing such purposes.
Budgeted appropriations are deemed restricted when associated with an additional spending proposal (*N.J.A.C.* 6A:23A-12.13(a)11).

The district board of education is required to maintain a separate accounting of expenditures for each question. Approved amounts that remain unexpended or unencumbered at the end of the school year shall either be anticipated as a part of the designated general fund balance of the subsequent school year budget or reserved and designated in the second subsequent school year budget.

N.J.A.C. 6A:23A-12.13(a)9 requires that a district board of education may not modify the base budget to execute proposed expenditures that have been rejected by the local voters, or board of school estimate, except as specified in *N.J.A.C.* 6A:23A-12.13(a)13, through a donation or contribution from an external source, only if such implementation will not require funding by the district board of education in subsequent budget years.

When a reservation of fund balance is established for unexpended or unencumbered funds pursuant to an additional spending proposal, the annual independent audit shall contain a note to the financial statements indicating the reserved fund balance amount, source and the fiscal year in which it will be appropriated. The financial statements should include the amount of the reserve in general fund equity account in the "Restricted Fund Balance" category (GASBS 54): ***reserved fund balance-legally restricted appropriations***.

Capital Reserve Account - General Fund

The capital reserve account (*N.J.A.C.* 6A:23A-14.1) maintained in the general fund allows a district to accumulate funds for future capital projects. A capital reserve account must have been established by board resolution, a copy of which should have been filed with the county superintendent of schools. A district board of education or board of school estimate may establish a capital reserve account at any time pursuant to *N.J.S.A.* 18A:21-2 and 3, and 7G –1.

The regulations *N.J.A.C.* 6A:23A-14.1 et seq. provide procedures for capital reserve accounts (withdrawals, deposits, and transfers). The bulleted points below are highlights of that rule. Additional guidance on School Development Authority (SDA) grant accounting and use of capital reserve can be found in Section II-30.4 of this Audit Program.

<u>General Compliance:</u>

- Funds in a capital reserve account must be used to implement the capital projects in the long-range facilities plan (LRFP). Withdrawals may not be used for current expense.

- Funds in a capital reserve account in existence prior to July 18, 2000 shall be utilized for the original purpose for which the funds were deposited (*N.J.A.C.* 6A:23A-14.1(k)).

- The capital reserve account balance cannot exceed the amount needed to implement the capital projects in the LRFP not met by state support (*N.J.A.C.* 6A:23A-14.1(g)). "All excess amounts in the capital reserve account identified in the annual audit shall be reserved and designated in the subsequent year's budget." (*N.J.A.C.* 6A:23A-14.1(g)2).

Deposits:

- A district board of education or board of school estimate may increase the balance in the capital reserve by appropriating funds in the annual general fund budget certified for taxes to meet the needs of the long-range facilities plan (*N.J.A.C.* 6A:23A-14.1(c)1). Districts that applied and received approval for a Commissioner waiver in the 2009-10 budget were not permitted to deposit funds into the capital reserve account at budget time (*N.J.A.C.* 6A:23A-12.1(f)).

- A district board of education may deposit any unanticipated revenue or unexpended line-item appropriation by board resolution at year end. The board resolution for deposit at year end into a capital reserve account must be made between June 1 and June 30 of the budget year (*N.J.S.A.* 18A:7F-41, *N.J.A.C.* 6A:23A-14.3).

- A district board of education may request approval of the voters for appropriation of additional amounts into the capital reserve by a separate proposal at budget time or by a special question at one of the four special elections authorized pursuant to *N.J.S.A.* 19:60-2. A district board of education may request approval of the board of school estimate for appropriation of additional amounts into the capital reserve by a separate proposal at budget time or by special resolution. The amount expressly approved by the voters or board of school estimate for deposit into a capital reserve may be from surplus or unrestricted local miscellaneous revenue only if such source is delineated in the question and/or special resolution. (*N.J.A.C*. 6A:23A-14.1(e))

- Interest earned on capital reserve funds in the account, including that earned on current year increases, must automatically be placed in the account. Failure to budget the interest does not change the requirement to deposit the interest earned in the account.

- Deposits are not made for a specific capital project unless specific voter approval was sought and received.

Withdrawals for Local Amount of School Facilities Projects:

- Withdrawals of the local share by board resolution, after receiving voter, board of school estimate or capital project review board approval of the intended capital reserve use and specific amount in an approved referendum(s) question for the school facilities project(s). (*N.J.A.C.* 6A:26A-14.1(h)(4))

- Withdrawals for a non-referendum school facilities project may be made, by board resolution, up to 110 percent of the local share less excess costs. Withdrawals must be transferred to the capital projects fund and accounted for separately with the corresponding SCC/SDA grant. (*N.J.A.C.* 6A:26A-14.1(j)(2))

Withdrawals for Excess Costs or Other Capital Projects:

- By board resolution for the transfer of funds to the line items in the capital outlay major account/fund to fund the total costs, less any excess costs, of an "Other Capital Project" which would otherwise be eligible for State support, and has received approval from the Office of School Facilities as eligible for State support. The amount of the withdrawal should not exceed the amount necessary to complete the "Other Capital Project". Note that an approval of the "Other Capital Project" alone does not constitute eligibility for State funding. (*N.J.A.C.* 6A:23A-14.1(h)(3))

- Upon voter, board of school estimate, or capital project board approval, withdrawals may be made to fund excess costs of a school facilities project, and to fund the total costs of an "Other Capital Project" that would not otherwise be eligible for State support as determined in accordance with N.J.A.C. 6A:26. Note that a project that has not received notification of eligibility for state funding from the Office of School Facilities requires a separate Statement of Purpose in the advertised budget. (*N.J.A.C.* 6A:23A-14.1(h)(5))

- Withdrawals for additional funds to augment a previously approved referendum project may be made if voter approved through the original budget certified for taxes which must include a Statement of Purpose which includes the amount of excess costs to be withdrawn, the date of the referendum, the amount of the local share in the approved referendum, and the reason needed to exceed the original approved amount. (*N.J.A.C.* 6A:23A-14.1(h)(5))

- Withdrawals for referendum approved "Other Capital Projects" may be made if the capital reserve use and specific amount is identified in the approved question. (*N.J.A.C.* 6A:23A-14.1(h)(4))

<u>Withdrawals for Debt Service:</u>

- A district, by board resolution, may withdraw and transfer funds to the debt service fund to offset principal and interest payments for bonded projects in the LRFP.

<u>Unexpended funds remaining after completion of a project:</u>

- Capital reserve funds transferred to Capital Projects to augment a grant that are remaining after completion of a school facilities project must be returned to the capital reserve account or anticipated as part of the designated general fund balance of the subsequent school year's budget or reserved and designated in the second subsequent year budget. (*N.J.A.C.* 6A:23A-14.1(j)3)

- Any unexpended capital reserve funds transferred to capital outlay remaining after completion of the school facilities project shall be returned to the capital reserve or anticipated as part of the designated general fund balance of the subsequent school year budget or reserved and designated in the second subsequent school year budget. (*N.J.A.C.* 6A:23A-14.1(h)5)

Capital Reserve - Accounting and Reporting

The department published accounting guidance for capital reserve that was distributed to districts and copied to the public school accountants on October 19, 2001. The passage of P.L. 2004, c.73 (S1701) supersedes that guidance by eliminating the previous EFCFA authority for districts to make transfers to capital reserve at any time during the year. District staff and auditors should refer to the regulations *N.J.A.C.* 6A:23A-14.1. The following highlights from that document are still applicable.

- Activity is recorded in the budgetary and asset accounts, not fund balance accounts.

- Adjustments to fund balance are recorded as part of the year-end closing entries.

- The Capital Reserve Asset Account (10-116) is required to segregate the restricted capital reserve assets and is used during the year to record all activity.

- There is no requirement to open a separate bank account for this activity, however, it is practical to do so, given the requirements for recording interest.
- Interest earned on the money as it is spent down is an increase in the capital reserve asset account.

The Capital Reserve account is reported in the *Balance Sheet* (Exhibit B-1) of the governmental funds statements as both an asset (Capital Reserve Account) and in the "Restricted Fund Balance" category (GASBS 54) as Reserved Fund Balance - Capital Reserve Account. In the districtwide *Statement of Net Assets* (Exhibit A-1) the balance of this account is reported in the net assets section as "Restricted for Other Purposes" in the governmental activities column.

> *Auditor's Note* – The June 30, 2012 Balance Sheet should reflect the actual balance at June 30, 2012 and <u>not</u> increases/withdrawals included in the 2011-12 budget. The department recommends footnote disclosure in the Comprehensive Annual Financial Report.

Excess Surplus

<u>Overview</u>

Auditors are required to perform the calculation of excess surplus at June 30 in accordance with *N.J.S.A.* 18A:7F-7 for all regular and county vocational school districts. The audited excess surplus calculation is not applicable to Education Service Commissions (ESCs). Special services school districts are subject to an excess surplus calculation in accordance with *N.J.S.A.* 18A:46-31, as amended. This calculation will be performed by the department during the tuition rate certification process. Do not perform the excess surplus calculation or report excess surplus for a special services school district.

The excess surplus calculation is required to be documented in the Auditor's Management Report. The applicable percentage is 2 percent for regular districts and 6 percent for county vocational districts. The minimum is $250,000 for both types of districts.

> *Auditor's Note* – Districts required to use school-based budgeting should refer to the guidance on Page II-10.23 of this chapter for detailed instructions on how to complete the excess surplus calculations.

Audited excess surplus is a budget related calculation using the general fund expenditures for the fiscal year and fund balance as reported in the *Budgetary Comparison Schedule – General Fund* (Exhibit C-1) for the fiscal year. **There is only one excess surplus calculation using budgetary amounts.** The reserve for excess surplus is included in the recapitulation of fund balance presented at the end of the Exhibit C-1 schedule. These amounts are reported on the modified accrual basis with the exception of a state legally mandated revenue recognition policy that is in conflict with GASB 33. See the example on the last page of this chapter.

Amounts included in the 2012-13 certified budget (reserved fund balance – excess surplus designated for subsequent year's expenditure) and any additional amounts reserved for appropriation in the 2013-14 original annual budget (reserved fund balance - excess surplus) must be separately reported in the Audsum on the separate lines provided. See Section III-5 of this *Audit Program* for further clarification. The Audsum includes a warning edit for the calculation of excess surplus at June 30, 2012. Under *N.J.S.A.* 18A:7F-7d, the Commissioner may withhold state aid in an amount not to exceed the audited excess undesignated general fund balances for failure to comply with the required reservation and designation of the audited excess surplus.

A calculation was performed in the 2012-13 budget software in Supporting Documentation Item 9 using projected 6/30/12 surplus balances and revised 2011-12 budgeted appropriations. The software, via the edits, forced the inclusion of the greater of the audited excess surplus at 6/30/11 or the calculated projected excess surplus at 6/30/12 in the 2012-13 budget as budgeted fund balance.

The 6/30/12 audited calculation should be based upon June 30, 2012 total general fund expenditures as reported on the *Budgetary Comparison Schedule General Fund* (Exhibit C-1), including applicable transfers to other funds, and net of TPAF Pension and Social Security amounts and amounts reported as “Assets acquired under capital leases (non-budgeted).” General fund transfers to other funds not included in the general fund expenditures of the CAFR, but added to the calculation are, Transfer Capital Outlay to Capital Projects (augment SCC/SDA grant) and Transfer Capital Reserve to Capital Projects (augment SCC/SDA grant). Note that beginning with June 2012, Transfer to Food Services is no longer an adjustment to expenditures. This calculation is also adjusted for any allowable adjustments such as impact aid, sale and lease-back, extraordinary aid, and additional nonpublic transportation aid, if applicable. The adjustment for extraordinary aid and additional nonpublic transportation aid is limited to the amount of revenue recognized in the current year that was not appropriated. The impact aid adjustment only applies to districts receiving impact aid and the amount that can be deducted as an adjustment generally is the amount recognized as impact aid revenue in the current year.

The surplus used in the calculation is the total general fund surplus net of any reserve for encumbrances, capital, maintenance, emergency and tuition reserve amounts, and any other state/government imposed or department approved legal reserve that has not been appropriated in the 2012-13 budget and that are in compliance with *N.J.A.C.* 6A:23A-16.2. Adjustments for legal reserves not appropriated in 2012-13 must be supported by a board resolution establishing the legal reserve. In most cases, this adjustment will not be applicable since most legal reserves require appropriation into the next year's budget.

For any legal reserve that is for other than encumbrances or state/government imposed or other legal restriction, the school district must seek approval from the Assistant Commissioner of Finance for use as an adjustment in the excess surplus calculation. Written approval must be received by September 30 if the district is seeking approval for the current audit year.

Auditors are required to include the calculation of 6/30/12 audited excess surplus in the Auditor’s Management Report. The department requires footnote disclosure in the CAFR for those districts where excess surplus is reflected on the general fund balance sheet.

<u>2 Percent Calculation –Regular Districts</u>

Pursuant to *N.J.S.A.* 18A:7F-7, as amended, all regular districts, excluding county vocational districts, must perform the excess surplus calculation using 2 percent of general fund expenditures. The minimum balance is $250,000.

Amounts calculated in excess of 2 percent that have not been appropriated in the 2012-13 original budget certified for taxes must be reported in the “Restricted Fund Balance” category (GASBS 54) as general fund “Reserved Fund Balance - Excess Surplus” in the June 30, 2012 CAFR and appropriated in the 2013-14 budget for property tax relief. The amount which has been included in the 2012-13 budget should be reported in the “Restricted Fund Balance” category (GASBS 54) as general fund "Reserved Fund Balance - Excess Surplus, Designated for Subsequent Year's Expenditures."

Education Jobs Fund (Ed Jobs) revenues and expenditures are recorded in the general fund (fund 18) on a reimbursement basis. As such, revenue will not drop to surplus, and no portion of general fund balance at June 30, 2012 is considered to be attributable to Education Jobs Fund. Ed Jobs Fund expenditures at June 30, 2012 are included as a component of overall general fund expenditures, and also are included in total general fund expenditures for purposes of the excess surplus calculation.

The following discussion and the example on the following page illustrate the proper calculation of the 2 percent excess surplus for districts not required to use school-based budgeting (SBB). Districts required to use school-based budgeting should refer to the guidance on Page II-10.23 of this chapter:

Example: The school district had total general fund expenditures (from exhibit C-1 of CAFR) of $7,500,000. Included in the general fund expenditures were "On-Behalf State Aid Payments" (TPAF Pension & Social Security) of $405,000 and Assets Acquired Under Capital Lease of $182,000. General fund transfers to other funds not included in the general fund expenditures of the CAFR, but added to the calculation, Transfer from Capital Outlay to Capital Projects of $75,000 and Transfer from Capital Reserve to Capital Projects (augment SCC/SDA grant) of $12,000. The district received $3,000 in federal impact aid revenue during 2011-12. In the June 30, 2012 general ledger reflects that the district had the following: $4,900 of year-end "other purposes" encumbrances reported in the "Committed" fund balance category (GASBS 54); $9,000 legally restricted reported in the "Restricted" fund balance category (GASBS 54) from an unexpended 2010-11 additional spending proposal required to be designated in the 2012-13 budget for property tax relief; $55,000 reserved June 30, 2011 excess surplus required to be designated for property tax relief in the 2012-13 budget reported in the "Restricted" fund balance category (GASBS 54); $100,000 unreserved and designated in the 2012-13 budget reported in the "Assigned" fund balance category (GASBS 54); and $395,000 unreserved/undesignated reported in the "Unassigned" fund balance category (GASBS 54) prior to calculating June 30, 2012 excess surplus.

2011-12 Total General Fund Expenditures	$7,500,000 *(a)*	
Increased by Applicable Operating transfers:		
Transfer from Capital Outlay to Capital Projects	75,000 *(b)*	
Transfer from Capital Reserve to Capital Projects	12,000 *(b)*	
Decreased by:		
On-Behalf State Aid Payments	(405,000)	
Assets Acquired Under Capital Leases	(182,000)	
Adjusted General Fund Expenditures	7,000,000	
Applicable Excess Surplus Percentage	x .02	
2% of Adjusted 2011-12 General Fund Expenditures	140,000 (A)	
Greater of (A) or $250,000	250,000	
Increased by:		
Allowable Adjustment	3,000 *(c)*	
Maximum Unreserved/Undesignated Fund Balance		$ 253,000
Total General Fund fund balance (June 30, 2012)	$ 563,900	
Decreased by:		
Year-End Encumbrances	(4,900)	
Legally Restricted – Designated for Subsequent Year's Expenditures	(9,000) *(d)*	

Legally Restricted - Excess Surplus – Designated for Subsequent Year's Expenditures	(55,000) *(d)*	
Assigned fund balance - Unreserved -- Designated for Subsequent Year's Expenditures	(100,000) *(d)*	
Total Unassigned Fund Balance		395,000
Reserved – Excess Surplus (June 30, 2012)		$ 142,000*(e)*

Recapitulation of Excess Surplus as of June 30, 2012

Reserved Excess Surplus – Designated for Subsequent Year's Expenditures (Audsum line 90031)	$ 55,000 *(f)*
Reserved Excess Surplus – (Audsum line 90030)	142,000 *(g)*
Total Excess Surplus	$ 197,000

(a) Total General Fund Expenditures obtained from June 2012 CAFR Exhibit C-1 Budgetary Comparison Schedule – General Fund.
(b) Include operating transfer expenditures that relate to the general fund but were required to be maintained in another fund. Do not include general fund transfers to Capital Reserve or Debt Service Fund, or Facilities Grant transfer to Special Revenue
(c) This adjustment line is to be utilized for Impact Aid, Sale and Lease-back, Extraordinary Aid, Additional Nonpublic School Transportation Aid, if applicable.
(d) The aggregate of $164,000 represents the total amount of General Fund fund balance appropriated in the 2011-12 General Fund budget.
(e) If this amount is negative enter zero (-0-).
(f) Represents surplus generated in 6/30/11, and budgeted in 2012-13.
(g) Represents surplus generated in 6/30/12 (required to be budgeted in 2013-14).

Excess Surplus Calculation And Instructions For Districts Required To Use School-Based Budgeting

This section is included to provide detailed instructions on preparing the excess surplus calculations in districts required to use school-based budgeting. Excess surplus is a budget related calculation using the General Fund expenditures and fund balance of the budgetary comparisons statements/schedules. The amounts used in the calculation must be taken from the Budgetary Comparison Schedule – General Fund (Exhibit C-1). The calculation for SBB districts must be adjusted to reduce the total general fund budgetary expenditures by the amount allocated to restricted federal resources in fund 15. The calculation must also separate the assets acquired under capital leases with state and local funds from those acquired with the allocated federal resources.

Sample Excess Surplus Calculation for Anytown School District (a School Based Budget District)

<u>SECTION 1</u>

Calculation A: 2 Percent Excess Surplus:

All districts required to use school-based budgeting are required to complete this calculation using 2 percent on line A10.

2011-12 Total General Fund Expenditures Reported on Exhibit C-1	$_________	(A)		
Increased by Applicable Operating Transfers				
Transfer from Capital Outlay to Capital Projects	$_________	(A1a)		
Transfer from Capital Reserve to Capital Projects	$_________	(A1a)		
Less: Expenditures Allocated to Restricted Federal Resources as Reported on Exhibit D-2	$_________	(A1b)		
2011-12 Adjusted General Fund & Other State Expenditures [(A)-(A1)]			$________	(A2)
Decreased by:				
On-Behalf TPAF Pension & Social Security			$________	(A3)
Assets Acquired Under Capital Leases:				
General Fund 10 Assets Acquired Under Capital Leases reported on Exhibit C-1a	$________	(A4)		
Add: General Fund & State Resources Portion of Fund 15 Assets Acquired under Capital Leases:				
Assets Acquired Under Capital Leases in Fund 15 reported on Exhibit C-1a	$_________	(A5)		
Combined General Fund Contribution & State Resources Percent of Fund 15 Resources Reported on Exhibit D-2	_______%	(A6)		
General Fund & State Resources Portion of Fund 15 Assets Acquired Under Capital Leases [(A5)*(A6)]	$_________	(A7)		
Total Assets Acquired Under Capital Leases [(A4)+(A7)]			$_________	(A8)
2011-12 General Fund Expenditures [(A2)-(A3)-(A8)]			$_________	(A9)
2 percent of Adjusted 2011-12 General Fund Expenditures [(A9) times .02]			$_________	(A10)
Enter Greater of (A10) or $250,000			$_________	(A11)
Increased by: Allowable Adjustment *			$_________	(K)
Maximum Unassigned Fund Balance [(A11)+(K)]			$_________	(M)

Line

Instructions for Calculation

(A) The total combined general fund expenditures (Funds 11-13 plus Fund 15) reported in the actual column of the *Budgetary Comparison Schedule – General Fund* (Exhibit C-1). Note this is a balance based on budgetary amounts.

(A1a) Include selected operating transfer expenditures that relate to the general fund but were required to be maintained in another fund. Do not include general fund transfers to food services, Capital Reserve or Debt Service Fund, or Facilities Grant transfer to Special Revenue Fund.

(A1b) The total Fund 15 expenditures allocated to restricted federal resources reported on the districtwide Schedule of Expenditures Allocated by Resource Type – Actual for the Fiscal Year Ended June 30, 2012 (Exhibit D-2).

(A2) Subtract line (A1) from line (A). This results in the total amount of general fund expenditures being used to calculate the maximum "Unassigned" fund balance for district required to use school-based budgeting.

(A3) The sum of the non-budgeted TPAF pension on-behalf payment plus the non-budged TPAF social security reimbursement reported in the State Sources section of the *Budgetary Comparison Schedule – General Fund* (Exhibit C-1).

(A4) The total Fund 10 assets acquired under capital leases amount is obtained from the Actual Operating Fund column of the *Combining Budgetary Comparison Schedule – General Fund* (Exhibit C-1a).

(A5) The Fund 15 assets acquired under capital leases amount is obtained from the Actual Blended Resource Fund column of the *Combining Budgetary Comparison Schedule – General Fund* (Exhibit C-1a).

(A6) The percentage of the overall districtwide Fund 15 expenditures, which were funded with general fund contribution or state resources. This percentage is obtained from the line entitled "Combined General Fund Contribution & State Resources" on the district-wide *Blended Resource Fund 15 - Schedule of Expenditures Allocated by Resource Type – Actual* (Exhibit D-2).

(A7) The general fund and state resources portion of Fund 15 assets acquired under capital leases and is determined by multiplying the total Fund 15 assets acquired under capital leases reported on line (A5), by the combined general fund contribution and state resources percentage reported on line (A6).

(A8) The total assets acquired under capital leases with general fund contribution and state resources. Line (A8) is the sum of lines (A4) and (A7).

(A9) The total adjusted expenditures upon which the maximum unreserved/undesignated fund balance is calculated; the result of line (A2) minus line (A3) minus line (A8).

(A10) This line represents 2 percent of general fund expenditures and is calculated by multiplying line (A9) by 2 percent.

(A11) The maximum allowable amount of unreserved/undesignated fund balance, prior to allowable adjustments.

(K) This line is calculated in Section 3 of the excess surplus calculations.

(M) The total maximum allowable "Unassigned" fund balance. This amount is calculated here as line (A11) plus line (K).

SECTION 2:

Total General Fund – Fund Balances at June 30, 2012	$__________	(C)		
Decreased by:				
Year-end Encumbrances	$__________	(C1)		
Legally Restricted – Designated for Subsequent Year's Expenditures	$__________	(C2)		
Excess Surplus – Designated for Subsequent Year's Expenditures **	$__________	(C3)		
Other Restricted/Reserved Fund Balances****	$__________	(C4)		
Assigned – Designated for Subsequent Year's Expenditures	$__________	(C5)		
Total Unassigned Fund Balance [(C)-(C1)-(C2)-(C3)-(C4)-(C5)]			$________	(U)

SECTION 2 – Instructions:

Refer to Chapter II-10.28 for additional explanation of the types of reserved fund balance permitted as a decrease in this calculation.

Line

(C) The total general fund balance at June 30, 2012 (combined Fund 10 and Fund 15) per the *Budgetary Comparison Schedule* (Exhibit C-1).

(C1) The total general fund balance reserved for encumbrances at June 30, 2012 (combined Fund 10 plus Fund 15).

(C2) The amount of general fund balance (combined Fund 10 and Fund 15) legally restricted for subsequent year's expenditures. This amount is to be appropriated in the 2012-13 general fund budget.

(C3) The June 30, 2011 excess surplus amount. This amount must be included in the Audit Summary Worksheet Line 10025, and appropriated in the 2012-13 general fund budget.

(C4) Other reserved fund balances. (Such as Adult Ed. Programs, maintenance reserve, etc.) See required detailed statement below.

(C5) The Assigned fund balance designated for subsequent year's expenditures. This amount is to be appropriated in the 2012-13 general fund budget.

(U) The total Unassigned fund balance at June 30, 2012. This amount is determined by subtracting lines (C1), (C2), (C3), (C4), (C5) from line (C). This is the amount that will be compared to the maximum Unassigned fund balance reported on line (M) to determine whether an excess surplus situation exists at June 30, 2012.

SECTION 3:

Restricted Fund balance – Excess Surplus ***[(U)-(M)] IF NEGATIVE ENTER–0

	$=======	(E)
Restricted Excess Surplus – Designated for Subsequent Year's Expenditures **	$___________	(C3)
Restricted Excess Surplus ***	$___________	(E)
Total [(C3) + (E)]	$ ==========	(D)

* This adjustment line (line (K) as detailed below) is to be utilized for Impact Aid, Sale, Lease-back, Extraordinary Aid, Additional Nonpublic School Transportation Aid, if applicable. Extraordinary Aid and Additional Nonpublic School Transportation Aid for 2011-12 received after June 30 is limited to the amount of revenue recognized in the audit year that was not appropriated.

Detail of Allowable Adjustments

Impact Aid	$______________	(H)
Sale & Lease-back	$______________	(I)
Extraordinary Aid	$______________	(J1)
Additional Nonpublic School Transportation Aid	$______________	(J2)
Total Adjustments (H)+(I)+(J1)+(J2)	$ =============	(K)

** This amount represents the **June 30, 2011** Excess Surplus (C3 above) and must be included in the Audit Summary Worksheet Line **10025**.

*** Amount must agree with the **June 30, 2012** CAFR and Audit Summary Worksheet Line **10024**.

**** Amount for Other Restricted/Reserved Fund Balance must be detailed for each source and request for approval to use amounts other than state imposed legal restrictions in the excess surplus calculation must be submitted to the Assistant to the Commissioner for Finance prior to September 30.

(N-1) Capital reserve at June 30, 2012.
(N-2) Maintenance reserve minimum required under EFCFA.
(N-3) Tuition reserve at June 30, 2012.
(N-4) Emergency reserve at June 30, 2012.
(N-5) Waiver offset reserve at June 30, 2012.

Detail of Other Reserved Fund Balance

Statutory restrictions:

Approved unspent separate proposal	$________________________
Sale/lease-back reserve	$________________________
Capital reserve (N-1)	$________________________
Maintenance reserve (N-2)	$________________________
Tuition reserve (N-3)	$________________________
Emergency reserve (N-4)	$________________________
Waiver offset reserve (N-5)	$________________________
Other Restricted/Reserved Fund Balance not noted above**	**$________________________**
Total Other Restricted/Reserved Fund Balance	**$______________________ (C4)**

SECTION 3 – Instructions:

Recapitulation of Excess Surplus as of June 30, 2012

Line

(C3) Line (C3) represents excess surplus generated at June 30, 2011 and should be included on the 2011-12 Audit Summary Worksheet Line 90031. This amount was to be appropriated in the 2012-13 general fund budget.

(E) This line represents the excess surplus generated at June 30, 2012 and must agree with the June 30, 2012 CAFR and be reported in the 2011-12 Audit Summary Worksheet Line 90030.

(D) Line (D) represents the sum of the June 30, 2011 and June 30, 2012 excess surplus (lines (C3) + (E).

Detail of Allowable Adjustments

Line

(H) Line H represents the amount of Impact Aid received by the district during 2011-12. This amount is obtained from the line entitled "Federal Sources: Impact Aid" on the *Comparative Schedules of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual* (Exhibit C-1a).

(I) Line I represents the proceeds realized from the sale-lease back of textbooks and non-consumable instructional materials during the current year, and is excluded from the calculation of excess undesignated general fund balance. See the Audit Program Section II-10.13 for a more detailed discussion of this adjustment.

(J1) Line J1 represents the extraordinary aid received after June 30 for 2011-12. This amount can only be excluded from the excess surplus calculation if the district can clearly document that they did not budget this additional aid during the 2011-12 fiscal year for which they filed an application. See Section II-10.4 for a more detailed discussion of this adjustment.

(J2) This line is used for Additional Nonpublic Transportation Aid received after June 30, but recorded in 2011-12. This amount is only excluded from the excess surplus calculation if the district can document that they did not budget the additional aid during 2011-12.

(K) Line (K) is the sum of lines (H), (I), (J1), and (J2) and represents the total allowable adjustment to increase the maximum unreserved/undesignated fund balance.

6 Percent Calculation – Vocational Districts

County vocational districts must perform the 6 percent calculation.

Amounts calculated in excess of 6 percent that have not been appropriated in the 2012-13 original budget certified for taxes must be reported in the "Restricted Fund Balance" category (GASBS 54) as general fund "Reserved Fund Balance - Excess Surplus" in the June 30, 2012 CAFR and appropriated in the 2013-14 budget for property tax relief. The amount which has been included in the 2012-13 budget should be reported in the "Restricted Fund Balance" category (GASBS 54) as general fund "Reserved Fund Balance - Excess Surplus, Designated for Subsequent Year's Expenditures." Note disclosures should describe the nature of the excess surplus and the amount budgeted in the 2012-13 original budget certified for taxes and the amount reserved for the subsequent year budget.

For districts with expenditures equal to or less than $100 million, any unreserved/undesignated general fund surplus amounts in excess of the greater of 6 percent of general fund expenditures or $250,000 (after allowable adjustments) is excess surplus. For districts with expenditures greater than $100 million any unreserved/undesignated general fund surplus amounts greater than the sum of 3 percent of general fund expenditures in excess of $100 million plus $6,000,000 and allowable adjustments is excess surplus. Any excess surplus amount must be reserved for appropriation in the 2012-13 original certified budget.

Fund Balance Classifications

In February 2009, the GASB issued GASBS No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. Available for purchase from GASB at https://gasb.org/store GASB No. 54 is effective for periods beginning after June 15, 2010 and establishes accounting and financial reporting standards for governmental funds (Refer to the *Governmental Funds Balance Sheet, B-1*, from the CAFR Outline). Under GASBS 54, general fund balances are further classified into five overarching categories:

- Nonspendable (assets that are not in spendable form; e.g. inventory)
- Restricted
- Committed
- Assigned
- Unassigned

Districts will continue to maintain the existing general ledger fund balance accounts (as appropriate) such as reserve for encumbrances, capital reserve, reserve for adult education programs, maintenance reserve, legal reserve, tuition reserve, waiver offset reserve, emergency reserve, excess surplus (current year), and excess surplus – (prior year) designated for subsequent year's expenditures, etc. For purposes of presentation in the *Governmental Funds Balance Sheet, B-1,* reserve balances are further categorized into one or more of the five fund balance categories according to the degree of restriction placed upon those balances. Unreserved general fund balance is further categorized as either "assigned" or "unassigned".

For purposes of presentation in the *Governmental Funds Balance Sheet, B-1*, GASB does not consider encumbrances to be a further restriction on fund balances that are already considered restricted, committed or assigned. Accordingly, the reserve for encumbrances account is not displayed as an individual component of overall fund balance. The general ledger balance in the reserve for encumbrances account is reported within the "other purposes" or other appropriate category of committed or assigned fund balance based on the degree of restriction. Significant encumbrances at year-end should be disclosed in the notes to the financial statements, along with other significant commitments. (Par. 24).

Districts use the fund balance classifications reported at the end of the *General Fund Budgetary Comparison Schedule* (Exhibit C-1) for purposes of calculating excess surplus. Fund balance in this Schedule reflects the modified accrual basis with the exception of the last state payment. Districts must include a Recapitulation of Fund Balance at the end of this Schedule with sufficient detail for a reviewer to determine the nature of any restriction, commitment, or assignment. The department has elected to continue to require districts to separately identify the total amount of encumbrances on the fund balance recapitulation on the C-1. The "Reserve for Encumbrances" should be displayed as "Year-End Encumbrances" in the "committed" and/or "assigned" categories. "Unrestricted Fund Balance" should be displayed as "Unassigned Fund Balance". See the illustration at the end of this chapter and also the guidance in Section III-5 on Audsum.

Fund balance in the *Governmental Funds Balance Sheet* (Exhibit B-1) reflects the modified accrual basis and under GASB No. 54 should be classified into nonspendable, restricted, committed, assigned or unassigned fund balance. In the accrual basis *Statement of Net Assets* (Exhibit A-1), there are three classifications of net assets: Invested in capital assets, net of related debt, Restricted net assets (with a line item for each fund in which the net assets are restricted), and Unrestricted. Auditors and district staff should refer to GASB 34, paragraphs 30 – 37 for further clarification of these classifications.

> *Auditor's Note* – No appropriation of surplus after June 30, 2012 is to be reflected in the June 30, 2012 balance sheet as designated for subsequent year's expenditures. The department recommends footnote disclosure in the CAFR.

Under GASB No. 54, the reserved fund balance classification is further categorized as restricted, committed or assigned fund balance. Restricted fund balance will generally include amounts constrained for a specific purpose by external parties, constitutional provision, or enabling legislation, such as state or other government imposed fund balance restrictions. All other legal reserves/restrictions require departmental review and approval. The request for approval should state the amount, source, purpose and legal basis for the reserve/restriction (i.e., why the funds are not available for appropriation in the subsequent year) and the fiscal year in which it will be appropriated. School districts should submit requests to the Assistant Commissioner of Finance no later than September 30 if approval is required for the audit period under review.

Fund Balance Classifications – Reserved. Reserved fund balance is further categorized as "Restricted", "Committed", and/or "Assigned" on the *General Fund Budgetary Comparison Schedule*, C-1, and *Governmental Funds Balance Sheet* (B-1)

- The **reserve for encumbrances** is maintained in the district's general ledger and represents that amount of fund balance related to orders issued in the current year that will be honored in the subsequent year. In general, for other than construction projects, that liquidation must be made within 60 to 90 days of year-end to be a valid reserve at June 30. This should not include accounts payable, since those orders were charged as expenditures in the current year and should be included in the balance sheet as a liability. Separate lines are provided in the Audsum for the reserve for encumbrances at June 30 for the general fund and capital projects fund. The department issued a Hotline on September 16, 2003 providing additional guidance on auditor reviews of encumbrances. Districts should not be encumbering goods and services that relate to the subsequent year. The Hotline is available on the department's website at: http://www.state.nj.us/education/finance/fp/af/hotline.pdf

- The reserve for encumbrances is not separately presented on the *Governmental Funds Balance Sheet* (Exhibit B-1). GASBS 54 provides that encumbrances are not considered to be an additional restriction on the fund balance where those funds are already restricted, committed, or assigned. Amounts encumbered for a specific purpose for which amounts have not been previously restricted, committed, or assigned, should be classified as either committed or assigned. (par. 24).

- On the fund balance recapitulation presented at the end of the *General Fund Budgetary Comparison Schedule* (Exhibit C-1), the reserve for encumbrances should be displayed as "Year-end encumbrances" and further categorized as "Committed" and/or '"Assigned" fund balance depending on the nature and degree of restriction(s).

- The **capital reserve account** maintained in the general fund allows a district to accumulate funds for future capital projects. See page II-10.15 of this Audit Program for specific procedures affecting capital reserve accounting. A separate line is provided in the Audsum for this reserve account. GASBS No. 54 requires the further categorization of the capital reserve account balance on the *Governmental Funds Balance Sheet* (Exhibit B-1) as restricted, depending on the nature and degree of restriction(s). The Department recommends reporting the capital reserve under "Restricted" fund balance due to the statutory and regulatory restrictions on withdrawals from capital reserve. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1)

- The **maintenance reserve account** is maintained in the general fund. The maintenance reserve account is used to accumulate funds for the required maintenance of a facility in accordance with the EFCFA (*N.J.S.A.*18A:7G-9) as amended by P.L. 2004, c. 73 (S1701). Districts may increase the balance in the maintenance reserve account by appropriating funds in the annual general fund budget certified for taxes (*N.J.A.C.* 6A:23A-14.2) or by deposit of any unanticipated revenue or unexpended line-item appropriation by board resolution at year end. The board resolution for deposit at year end into a maintenance reserve account must be made between June 1 and June 30 of the budget year (*N.J.S.A.* 18A:7F-41, *N.J.A.C.* 6A:23A-14.3). EFCFA requires that upon district completion of a school facilities project, the district must submit a plan for the maintenance of that facility. Auditors and district staff should refer to the regulations, *N.J.A.C.*6A:26A, for further guidance. A separate line is provided in the Audsum for this reserve account. GASBS No. 54 requires the further categorization of the maintenance reserve account balance on the *Governmental Funds Balance Sheet* (Exhibit B-1) as restricted, committed, and/or assigned. The Department recommends reporting the maintenance reserve under "Restricted" fund balance due to the statutory and regulatory restrictions on withdrawals from maintenance reserve. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1)

- The **emergency reserve** is maintained in the general fund. The emergency reserve account is used to accumulate funds in accordance with *N.J.S.A.* 18A:7F-41c(1) to finance unanticipated general fund expenditures required for a thorough and efficient education. Unanticipated means reasonably unforeseeable and shall not include additional costs caused by poor planning. The maximum balance permitted at any time in this reserve is the greater of $250,000 or 1 percent of the general fund budget not to exceed $1 million. Deposits may be made to the emergency reserve account by board resolution at year end of any unanticipated revenue or unexpended line item appropriation or both. The department has defined year end for the purpose of depositing surplus into reserve accounts as an amount approved by the district board of education between June 1 and June 30. Withdrawals from the reserve require the approval of the Commissioner unless the withdrawal is necessary to meet an increase in total health care costs in excess of 4 percent. GASBS No. 54 requires the further categorization of the emergency reserve account balance on the *Governmental Funds Balance Sheet* (Exhibit B-1). The emergency reserve has significant externally imposed restrictions on its withdrawal and should be categorized as "Restricted" fund balance. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1)

- The **reserve for tuition** is maintained in the general fund. The tuition reserve represents a year end fund balance classification to reserve unrestricted fund balance for a foreseeable future tuition adjustment pursuant to *N.J.A.C.* 6A:23A-17.1(f). This reserve is only applicable for formal sending /receiving relationships between two district boards of education established under subchapter 3 of the business services code pursuant to *N.J.S.A.* 18A:38-19. It does not pertain to tuition certification or amounts owed to private schools for the handicapped. It is also not applicable to county vocational districts. The tuition reserve enables the district to reserve fund balance for an anticipated large tuition adjustment for the current contract year. The major contributing factor for tuition adjustments and use of the reserve is a significant change from estimated to the actual enrollment. The maximum amount that may be restricted at year end is 10 percent of the estimated tuition cost of the contract year. Upon certification of rates in the second year following the contract year, full appropriation of the applicable year's reserve must be liquidated and any remaining balance related to that year must be reserved and budgeted for tax relief. In the recapitulation of fund balance reported at the end of the *Budgetary Comparison Schedule* (Exhibit C-1), the reserve for each of two possible years should be reported separately. Separate lines are provided in the Audsum data collection for each applicable year's reserve, both the beginning fund balance and the ending fund balance for each of the two years reserve. See this Audit Program, Section III-5 for further clarification on the specific lines. GASBS No. 54 requires the further categorization of the tuition reserve account balance on the *Governmental*

Funds Balance Sheet (Exhibit B-1). Based upon the withdrawal requirements, the tuition reserve has significant externally imposed restrictions on its use and should be categorized as "Restricted" fund balance. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1)

- The **waiver offset reserve** is maintained in the general fund. For the 2011-12 budget year there were no Commissioner waivers available. Any remaining balance at June 30, 2011 must be budgeted for tax relief in the 2012-13 budget. GASBS No. 54 requires the further categorization of the waiver offset reserve account balance on the *Governmental Funds Balance Sheet* (Exhibit B-1). Because the waiver offset reserve must be withdrawn in accordance with *N.J.A.C.* 6A:23A-13.1, the balance should be further categorized as "Restricted" fund balance. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1)

- The **reserved fund balance-legally restricted account(s)** are maintained in the general fund. The legally restricted fund balance account(s) is used to report that portion of the general fund surplus that is legally reserved for specific purposes. In general, funds are legally restricted only when constraints placed on the use are externally imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation. This would include reserves established for register audit recoveries and restricted appropriations such as unspent funds from:

  1) Approved separate proposals as outlined in *N.J.A.C.* 6A:23A-12.13
  2) Sale/lease-back reserve *N.J.S.A.* 18A:7F-7(e)

  Legal reserves that are for anything other than state imposed or other government imposed legal restriction must be approved by the Assistant Commissioner Administration and Finance. Examples of state imposed legal restrictions include audited excess surplus, unspent separate proposals, ASSA audit recoveries, legally established capital, maintenance, and tuition reserve accounts, and a reserve established for the sale leaseback of textbooks in the year the proceeds are realized. **The request for approval should by submitted by the school district to the Assistant Commissioner Administration & Finance by <u>September 30, 2012</u> for the June 30, 2012 year.** The request should state the purpose and legal basis for the reserve (e.g., the specific "constraint imposed on the use by external parties or by laws or regulations of other governments"). Approval will only be granted for those other legal obligations that are in conformity with GAAP.

  Under GAAP, few items would constitute a legal reserve. Per GAAP, the basic concept of a legal reserve is that it is not unilaterally established by the district and it cannot be removed without the consent of those imposing the restriction or through formal due process. Districts do not have the authority to advance fund (accumulate resources) for a potential future liability by setting aside an amount as a legal reserve. Loss contingencies are not considered legal reserves but instead would be recorded as accrued liabilities if a loss is probable and reasonably estimable. For funds statements, only the amount due and payable with current resources is accrued. For the district-wide statements, the full amount is accrued. Contingent liabilities not required to be accrued should be disclosed in the notes to the financial statements. All significant facts with respect to the contingency should be disclosed. GAAP guidance is available in the GASB Codification chapter "Claims and Judgments" (C50).

- The notes to the financial statements must contain a discussion of all legally restricted balances, including the amount, source and fiscal year in which it will be appropriated. A separate line is provided in the Audsum data collection for legal reserves - general fund. These balances, if determined prior to the adoption of the budget, should have been anticipated in the 2012-13 "School District Budget Statement" and line 1660, "Amount Budgeted in FY 2012-13" in column 6, General Fund (Reserved) Legal Reserves of the Recapitulation of Balances. Amounts not anticipated in the 2012-13 budget must be shown as a legal reserve in the June 30 CAFR and appropriated in the 2012-13 budget. GASBS No. 54 requires the further categorization of the legal reserve account balance on the *Governmental Funds Balance Sheet* (Exhibit B-1). GASBS No. 54 paragraph 8 requires that amounts placed in legal reserve that are subject to:

- External constraints externally imposed by creditors, grantors, contributors, or laws or regulations of other governments; or
- Imposed by law through constitutional provisions or enabling legislation

be further categorized as "Restricted" fund balance. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1).

- The **reserved fund balance – excess surplus – designated for subsequent year's expenditures** represents the audited excess surplus from the prior year budgeted in the subsequent year. Any portion of the June 30, 2011 audited excess surplus that was appropriated in the 2012-13 original budget certified for taxes must be categorized on the *Governmental Funds Balance Sheet* (Exhibit B-1) as "Restricted" fund balance. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1). Audsum line 90031 (formerly 10025) has been provided for reserved fund balance - excess surplus – designated for subsequent year's expenditures. The following discussion and example illustrates the proper presentation of excess surplus – designated for subsequent year's expenditures.

  Example: The school district had audited excess surplus as of June 30, 2011 of $55,000 and an unexpended 2010-11 additional spending proposal of $9,000. The district appropriated $164,000 (sum of the *(a)*s) in the 2012-13 original budget (comprised of the $9,000 unexpended 2010-11 additional spending proposal, $55,000 audited excess surplus from June 30, 2011 and $100,000 of "Assigned" fund balance - designated by the BOE for subsequent year's expenditures.) As of June 30, 2012 the district had generated an additional $142,000*(b)* of excess surplus. The $142,000 (calculated in the excess surplus example) is required to be appropriated in the 2013-14 original budget and should also be reported on line 10024 of the June 30, 2012 audsum data collection.

  (See the illustration of the fund balance recapitulation section of the C-1, amended to include the classification requirements of GASBS No. 54 on page II-10.33).

	June 30, 2012	June 30, 2011
Fund Balances*:*		
Year-End Encumbrances	$ 4,900	$50,000
Legally Restricted – Unexpended Additional Spending Proposal		9,000
Legally Restricted – Designated for Subsequent Year's Expenditures	9,000 *(a)*	
Legally Restricted - Excess Surplus	142,000 *(b)*	55,000
Legally Restricted - Excess Surplus - Designated for Subsequent Year's Expenditures	55,000 *(a)*	
Assigned Fund Balance- Designated for Subsequent Year's Expenditures	100,000 *(a)*	235,000
Unassigned Fund Balance	253,000	215,000
	$ 563,900	$ 564,000

- The **reserved fund balance – excess surplus** represents audited excess surplus generated in the current audit year. Any amount calculated as excess surplus generated during the year ended June 30, 2012 that has not been appropriated in the 2012-13 original budget certified for taxes must be reported as excess surplus – current year and categorized on the *Governmental Funds Balance Sheet* (Exhibit B-1) as "Restricted" fund balance. The same categorization is applicable to the *General Fund Budgetary Comparison Schedule* (Exhibit C-1). Appropriate footnote disclosure should be made in the notes to the financial statements including the amount and an explanation that the amount represents surplus determined to be reserved and designated in the 2012-13 budget during the audited excess calculation performed at June 30 in accordance with *N.J.S.A.* 18A:7F-7. Audsum line 10024 is used to report the current year reserved fund balance - excess surplus. Please note that the Audsum includes a warning edit for the calculation of excess surplus at June 30, 2012. Auditors are required to include the calculation of excess surplus in the Auditor's Management Report.

- The **reserved fund balance – adult education programs** is a required separate restricted account. *N.J.S.A.* 18A:50-6 requires that surplus generated from the excess of receipts from donations, tuition fees, or from any source other than local taxation over the actual cost of the maintenance and operation of the district's adult education program remain in a separate account for the restricted fund balance. The account should be displayed as an asset and within the fund balance section on the *Governmental Funds Balance Sheet* (Exhibit B-1) and in the fund balance recapitulation section of the *General Fund Budgetary Comparison Schedule* (Exhibit C-1) in the "Restricted" fund balance category. In the event that the adult education program in any district is discontinued for two consecutive school years any funds remaining in the separate account shall lapse into the unreserved/unassigned general fund balance of the district. A separate line is provided in the Audsum for reserved for adult education programs - general fund.

Fund Balance – Unassigned

All other fund balance is classified as "**Unassigned" fund balance** and is considered in the excess surplus calculation. Refer to the example calculation on page II-10.19. Following are several points of clarification regarding the determination of "Unassigned" fund balance:

- In determining "unassigned" fund balance, districts may reflect management's intended use of fund balance in the subsequent year's budget certified for taxes as a separate line in the "Assigned" fund balance section of the *Governmental Funds Balance Sheet* (Exhibit B-1) and in the recapitulation of fund balance section of the *General Fund Budgetary Comparison Schedule* (Exhibit C-1). The amount of year end fund balance that has been included in the certified budget should be presented as "Designated for Subsequent Year's Expenditures" and further classified as a component of "Assigned" fund balance. Each assignation should be explained in the notes to the financial statements.

- Separate lines are provided in the Audsum data collection for Unassigned General Fund Balance (90075 replaces 10070) and Assigned General Fund Balance Designated Subsequent Year's Expenditure (90080 replaces 10075). Include in the "Assigned" fund balance section of Audsum on the designated fund balance line only those amounts which were included in the 2012-13 certified budget as budgeted fund balance on line 121 that have not already been included on another fund balance line of Audsum. Included in the "Unassigned" line are all other fund balances that have not been otherwise reported in Audsum. General Fund Unassigned Fund Balance reported in Audsum must agree with the General Fund Unassigned Fund Balance reported in the recapitulation of fund balance section of the *General Fund Budgetary Comparison Schedule* (Exhibit C-1).

For purposes of the excess surplus calculation, fund balance is the amount derived from the revenue including the last state aid payment. The following recapitulation of fund balance is to be included on the *Budgetary Comparison Schedule for the General Fund* (Exhibit C-1). Note that in the reconciliation to GAAP, the adjustment to fund balance is only to reverse the last state aid payment, not to add in the payment made for the prior year, since that payment has been included in the "budgetary" fund balance which is rolled forward on the *Budgetary Comparison Schedule.*

Recapitulation of Fund Balance:

Nonspendable Fund Balance:	
Inventory	$ xxx
Restricted Fund Balance:	
Legally Restricted – Designated for Subsequent Year's Expenditures	9,000
Reserved Excess Surplus - Designated for Subsequent Year's Expenditures	55,000
Reserve for Excess Surplus	142,000
Waiver Offset Reserve- Designated for Subsequent Year [if applicable]	xxx
Maintenance Reserve [if applicable]	xxx
Capital Reserve [if applicable]	xxx
Emergency Reserve [if applicable]	xxx
Committed Fund Balance:	
Year-end Encumbrances	4,900
Assigned Fund Balance:	
Designated for Subsequent Year's Expenditures	100,000
Unassigned Fund Balance	253,000
	563,900
Reconciliation to Governmental Funds Statements (GAAP):	
Last State Aid Payment Not Recognized on GAAP Basis	(551,385)
Fund Balance per Governmental Funds (GAAP)	$ 12,515

<u>Deficit Due to Delay of One or More June State Aid Payment(s)</u>

On the modified accrual statements, a deficit may occur in the general or special revenue fund. Pursuant to *N.J.S.A.* 18A:22-44.2 any negative unreserved, undesignated (Unassigned) fund balance that is reported as a direct result from a delay in the payment of state aid until the following fiscal year, is not considered a violation of New Jersey statute and regulation and does not require corrective action unless the deficit exceeds the last state payment(s). Refer to paragraph 19 of GASBS No. 54 for guidance regarding the reporting of a negative "Unassigned" fund balance.