1992

Audits of colleges and universities with conforming changes as of May 1, 1992; Industry audit guide; Audit and accounting guide

American Institute of Certified Public Accountants. Not-for-Profit Organizations Committee

Industry
Audit
Guide

AUDITS of COLLEGES and UNIVERSITIES

With Conforming Changes As of May 1, 1992

AICPA
American Institute of Certified Public Accountants

Industry
Audit
Guide

AUDITS of COLLEGES and UNIVERSITIES

With Conforming Changes As of May 1, 1992

This edition of the industry audit guide *Audits of Colleges and Universities* has been modified by the AICPA staff to include certain changes necessary due to the issuance of authoritative pronouncements since the guide was originally issued. The changes made are identified in a schedule in Appendix B of the guide. The changes do *not* include all those that might be considered necessary if the guide were subjected to a comprehensive review and revision.

AICPA
American Institute of Certified Public Accountants

Published for the
American Institute of
Certified Public Accountants
by
COMMERCE CLEARING HOUSE, INC.
4025 W. Peterson Ave.
Chicago, Illinois 60646

1234567890 AccS 998765432

NOTICE TO READERS

This industry audit guide presents recommendations of the AICPA Committee on College and University Accounting and Auditing on the application of generally accepted auditing standards to audits of financial statements of colleges and universities. This guide also presents the committee's recommendations on and descriptions of financial accounting and reporting principles and practices for colleges and universities. AICPA members should be prepared to justify departures from this guide.

Preface

This guide has been prepared to assist the independent auditor in auditing and reporting on financial statements of nonprofit institutions of higher education including colleges, universities, and community or junior colleges. Auditors of private or independent schools should consult the AICPA audit and accounting guide *Audits of Certain Nonprofit Organizations.* The drafting of this guide was greatly facilitated by the American Council on Education, who granted us permission to quote from and paraphrase Part 2 and the appendices of its publication.

The Committee on College and University Accounting and Auditing wishes to express its appreciation to Howard A. Withey for his fine work in preparing the initial drafts of the guide, to Joseph V. Bencivenga and Stephen J. Gallopo, former AICPA staff personnel who worked with the Committee, and to Wilbert A. Begeman, a member of the Committee during the initial period of work on the guide. Further, the Committee acknowledges the generous cooperation and assistance provided by the National Association of College and University Business Officers (NACUBO) through their assignment of Clarence Scheps and Robert B. Gilmore as consultants to this Committee. In addition, W. Harold Read, chairman of NACUBO's Accounting Principles Committee, gave generously of his time in commenting on and discussing topics dealt with in the guide.

Committee on College and University Accounting and Auditing

TABLE OF CONTENTS

Chapter 1

Introduction

1.01 Proper accounting and financial reporting have been of primary concern to college and university business officers. Literature dealing with these matters has been published since 1911. The most recent of these publications is *College and University Business Administration.* This revised edition (referred to in this guide as the Manual) combines in one volume the matters covered in previous volumes. As in earlier editions, the national committee, which prepared the text for the Manual, was comprised of individuals from the various associations of business officers, the U.S. Office of Education, the American Council on Education, the AICPA, and individuals acting as special consultants to the Committee.

1.02 Much of the material in this guide is presented as it appears in the Manual. In some instances, however, the guide recommends practices, both accounting and reporting, which differ from the Manual or which clarify or expand practices recommended by it. Also, some disclosure requirements recommended by the Accounting Principles Board, Financial Accounting Standards Board, and Governmental Accounting Standards Board are not mentioned in the Manual. Significant items added to the guide or requiring accounting or reporting practices which are different from those recommended in the Manual are listed below.

Summary of Significant Changes

1.03 *Basic Financial Statements.* Certain reporting practices differing from those included in the Manual are discussed in chapter 11 and illustrated in the financial statements in Statement of Position (SOP) 74-8, *Financial Accounting and Reporting by Colleges and Universities* [Appendix A].

1.04 *Investment Performance.* Disclosure of the total performance of the investment portfolio is discussed in Chapter 2 and illustrated in the notes to the financial statements in SOP 74-8 [Appendix A].

1.05 *Investments, Exclusive of Physical Plant.* Current market or fair value as an alternative to cost in reporting the carrying value of investments is discussed in chapter 2.

1.06 *Depreciation.* While agreeing with the premises and conclusions of the Manual with respect to depreciation accounting, the guide permits the reporting of depreciation expense in the plant fund section of the statement of changes in fund balances as stated in chapter 2. FASB Statement No. 93, *Recognition of Depreciation by Not-for-Profit Organizations,* as amended, requires not-for-profit organizations to recognize the cost of using up the future economic benefits or service potentials of their long-lived tangible assets—depreciation—and to disclose:

a. Depreciation expense for the period
b. Balances of major classes of depreciable assets, by nature or function, at the balance sheet date
c. Accumulated depreciation, either by major classes of depreciable assets or in total, at the balance sheet date
d. A general description of the method or methods used in computing depreciation for major classes of depreciable assets.

1.07 GASB Statement No. 8, *Applicability of FASB Statement No. 93, "Recognition of Depreciation by Not-for-Profit Organizations," to Certain*

State and Local Governmental Entities, provides that governmental colleges and universities should not change their accounting and reporting for depreciation of capital assets as a result of FASB Statement No. 93. Governmental colleges and universities are not precluded from depreciating their capital assets by reporting a depreciation allowance in the balance sheet and a provision for depreciation in the statement of changes in the balance of the investment-in-plant fund subsection of the plant funds group. (See paragraph 2.22).

1.08 *Funds Held in Trust by Others.* Funds held in trust by others may be included in the financial statements under the circumstances described in chapter 2.

1.09 *Institutions Operated by Religious Groups.* Chapter 2 includes guidelines for institutions operated by religious groups with respect to the accounting entity, facilities made available by religious groups, and the monetary value of contributed services.

1.10 *Endowment Income Stabilization Reserve.* Endowment income stabilization reserves are at variance with generally accepted accounting principles, and the manner in which any established reserve may be eliminated is set forth in chapter 4.

1.11 *Endowment Fund Investment Gains.* As discussed in chapter 8 and illustrated in SOP 74-8 [Appendix A], the guide clarifies and expands upon the position taken in the Manual with respect to accounting for gains and losses of investments of endowment and similar funds and discusses statement presentation when management uses the "total return" investment concept.

1.12 *Expired Term Endowments.* As stated in chapter 8 and illustrated in the financial statements in SOP 74-8 [Appendix A], upon termination, the unrestricted principal of term endowment funds should be treated as new fund additions to unrestricted current funds rather than as transfers, as recommended in the Manual.

1.13 *Debt Service on Educational Plant.* The Manual treats mandatory debt service provisions relating to educational facilities as transfers and classifies similar provisions relating to auxiliary enterprise facilities as expenditures. The guide provides for a consistent treatment in both cases as described and illustrated in SOP 74-8 [Appendix A].

1.14 *Loan Fund Matching Grant.* Mandatory transfers from current funds to loan funds to match gifts or grants are treated separately from nonmandatory transfers as described and illustrated in SOP 74-8 [Appendix A].

1.15 *Nonmandatory Transfers of Unrestricted Current Funds.* The guide in SOP 74-8 [Appendix A] distinguishes between mandatory provisions, exemplified by the two preceding items, and nonmandatory transfers, and in chapter 11 requires that any statement of current funds revenues, expenditures, and other changes include all current funds transfers.

1.16 *Provision for Encumbrances.* As stated in chapter 2, accounting for encumbrances should be in accordance with the accrual basis of accounting so that expenditures include only amounts associated with goods and services received and so that liabilities include only the unpaid amounts associated with such expenditures.

1.17 *Annuity Funds.* The actuarial method of accounting for annuity funds, providing for the determination of annuity liabilities based on a life expectancy basis, is described in chapter 10 and illustrated in SOP 74-8 [Appendix A].

1.18 *Agency Funds.* Agency funds should not be included in the statement of changes in fund balances, as set forth in chapter 10.

1.19 *Pledges, Excluding Grants.* The guide requires disclosure of pledges, as discussed in chapter 2.

1.20 *Current Funds Revenues and Expenditures.* Certain changes in categories and groupings of current funds revenues and expenditures have been made in SOP 74-8 [Appendix A].

1.21 *Accounting Changes and Disclosure Requirements Promulgated by the Body Designated by the Council of the American Institute of Certified Public Accountants.* Additional disclosure requirements occasioned by pronouncements of the Accounting Principles Board which are not mentioned in the Manual are illustrated or referred to; these requirements include reference to such matters as employee benefit plans and long-term leases. Pronouncements issued by the Financial Accounting Standards Board after this guide is issued which affect the financial statements of nongovernmental educational institutions may impose changes in accounting and further disclosure requirements which, of course, would have to be met. Pronouncements issued by the Governmental Accounting Standards Board after this guide was originally issued which affect the financial statements of governmental institutions may impose changes in accounting and further disclosure requirements which would also have to be met.

Effective Date

1.22 The guide shall be effective for all fiscal years beginning after June 30, 1973.

Chapter 2

General Accounting Principles and Audit Procedures

2.01 Service, rather than profits, is the objective of an educational institution; thus, the primary obligation of accounting and reporting is one of accounting for resources received and used rather than for the determination of net income. Frequently there is no relationship between the fees charged and the actual expenditures for program services. In addition, philanthropic sources often specify the particular program service or fund to which their contributions are to be applied. Furthermore, nonexpendable gifts must sometimes be maintained to produce income to be used for general or specific programs. Some nonexpendable resources are also restricted as to use, e.g., loans to students, faculty, or staff. In order to account properly for a diversity of resources and their use, there has developed, over a period of years, the principles and practices of "fund accounting."

General Accounting Principles

2.02 *Fund Accounting.* Fund accounting is the procedure by which resources for various purposes are classified for accounting and reporting purposes in accordance with activities or objectives as specified by donors, in accordance with regulations, restrictions, or limitations imposed by sources outside the institution, or in accordance with directions issued by the governing board.

2.03 A fund is an accounting entity with a self-balancing set of accounts for recording assets, liabilities, a fund balance, and changes in the fund balance. Separate accounts are maintained for each fund to insure observance of limitations and restrictions placed on the use of resources. For accounting and reporting purposes, however, funds of similar characteristics are combined into fund groups.

2.04 In some instances, legal provisions, regulations, and the like pertaining to certain funds may require accounting and reporting practices which may be at variance with generally accepted accounting principles. The Committee recognizes that in these instances such legal and regulatory provisions must take precedence whenever a conflict between the two exists. Such restrictions, however, do not obviate generally accepted accounting principles for the purpose of reporting financial position, changes in fund balances, and current funds revenues, expenditures, and other changes. In instances where financial statements are not presented in conformity with generally accepted accounting principles, the independent auditor would be precluded from expressing an unqualified opinion and should refer to SAS No. 58, *Reports on Audited Financial Statements,* for guidance with respect to the appropriate wording to be used in such an opinion. Paragraphs 22 through 30 of SAS No. 62, *Special Reports,* discuss reporting on special-purpose financial presentations to comply with contractual agreements or regulatory provisions that are intended solely for the use of the parties to the agreement, regulatory bodies, or other specified parties.

2.05 The fund groups usually encountered in an educational institution are as follows:

- Current funds
- Loan funds

- Endowment and similar funds
- Annuity and life income funds
- Plant funds
- Agency funds

2.06 In subsequent chapters, definitions of each of the above are followed by descriptions of the accounting principles and reporting practices unique to a particular fund group. Accounting principles and reporting practices applicable to several or all fund groups follow.

2.07 *Basic Financial Statements.* Financial reporting utilizes three basic types of statements, namely (a) balance sheet, (b) statement of changes in fund balances, and (c) statement of current funds revenues, expenditures, and other changes. See chapter 11 for further explanation and SOP 74-8 [Appendix A] for illustrations of the basic financial statements.

2.08 *Externally Restricted vs. Internally Designated Funds.* A clear distinction between the balances of funds which are externally restricted and those which are internally designated within each fund group should be maintained in the accounts and disclosed in the financial reports.

2.09 *Accrual Accounting.* The accounts should be maintained and reports prepared on the accrual basis of accounting. Revenues should be reported when earned and expenditures when materials or services are received. Expenses incurred at the balance sheet date should be accrued and expenses applicable to future periods should be deferred. However, certain deferrals and accruals, such as investment income and interest on student loans, are often omitted. Nevertheless, the only basis for their omission should be that the omission does not have a material effect on the financial statements. Revenues and expenditures of an academic term, such as a summer session, which is conducted over a fiscal year end, should be reported totally within the fiscal year in which the program is predominantly conducted.

2.10 Encumbrances representing outstanding purchase orders and other commitments for materials or services not received as of the reporting date should not be reported as expenditures nor be included in liabilities in the balance sheet. Designations or allocations of fund balances or disclosure in the notes to the financial statements should be made where such commitments are material in amount. Failure to disclose the distinction between true liabilities and encumbrances which are not true liabilities could result in the presentation of misleading information to state authorities, regulatory bodies, budget commissions, and others.

2.11 *Gifts, Bequests, and Grants.* Gifts, bequests, grants, and other receipts restricted as to use by outside grantors or agencies are recorded as additions directly in the fund group appropriate to the restricted nature of the receipt. Unrestricted gifts, bequests, and grants are recorded as unrestricted current funds revenues. (See SOP 74-8 [Appendix A].)

2.12 Pledges of gifts, including uncollected subscriptions, subscription notes, and estate notes, should be disclosed in the notes unless they are reported in the financial statements. The notes to the financial statements should disclose the gross amounts by time periods over which the pledges are to be collected and related restrictions, if any, as to use.

2.13 If the pledges are reported in the financial statements, they should be accounted for at their estimated net realizable value in the same manner as gifts received (except as to asset classification, for which pledges would be reported as a receivable), and credited to unrestricted revenues, deferred income, current restricted funds, plant funds, etc., as appropriate. The estimated net realizable value comprehends the present value of long-term pledges and reductions for any allowance for uncollectible pledges.

2.14 Grant awards not yet funded and for which the institution has not yet performed services should not be considered as assets to be accounted for in the financial statements. However, the total amount of such uncollected grant awards at the balance sheet date may be disclosed in the notes to the financial statements.

2.15 *Investments Exclusive of Physical Plant.* Investments purchased usually are reported in the financial statements at cost and investments received as gifts at the fair market or appraised value at the date of gift, unless there has been an impairment of value not considered to be temporary. Investments in wasting assets, other than institutional plant, usually are reported net of allowance for depreciation or depletion (see also paragraph 2.22, "Depreciation of Physical Plant").

2.16 As a permissible alternative, investments, exclusive of physical plant, may be reported in the financial statements at current market value or fair value, provided this basis is used for all investments of all funds. When using this alternative, unrealized gains and losses should be reported in the same manner as realized gains and losses are reported under the cost basis.

2.17 Interfund sales of investments should be recorded in the purchasing fund at fair market value. The difference between cost or carrying value and fair market value should be accounted for in the selling fund in the same manner as realized gains and losses. The financial statements or notes should set forth the total performance (i.e., yield and gains and losses) of the investment portfolio based on cost and market value.

2.18 Investments of various funds may be pooled unless prohibited by statute or by terms of the gifts. Accounting for pooled investments should provide for both the equitable distribution of income and the means of determining the equitable share of the participating funds in both realized and unrealized gains or losses on investments.

2.19 Proper determination of equities and the basis of income distribution require that pooled investment funds be administered on a basis utilizing market values on a share or unit plan. This determination is made through the use of memorandum records instead of recording each investment at market value in the accounts.

2.20 Premiums paid on interest-bearing obligations held as long-term investments should be amortized, and provision should be made for the accumulation of discounts unless inappropriate because of default or quality of the bonds.

2.21 In order to maintain the distinction between income and principal of endowment and similar funds, depreciation or depletion should be provided on wasting assets held as investments of these funds. Gains and losses on investments of all fund groups are treated as revenues or as additions to or deductions from the owning fund balance.

2.22 *Depreciation of Physical Plant.* Depreciation expense related to depreciable assets comprising the physical plant is reported neither in the statement of current funds revenues, expenditures, and other changes nor in the statement of changes in unrestricted current funds balance. The reason for this treatment is that these statements present expenditures and transfers of current funds rather than operating expenses in conformity with the reporting objectives of accounting for resources received and used rather than the determination of net income. Depreciation allowance, however, may be reported in the balance sheet and the provision for depreciation reported in the statement of changes in the balance of the investment-in-plant fund subsection of the plant funds group. FASB Statement No. 93, *Recognition of Depreciation by Not-for-Profit Organizations,* as amended, requires not-for-profit organizations to recognize the cost of using up the future economic benefits or service potentials of their long-lived tangible assets—depreciation—and to disclose:

a. Depreciation expense for the period

b. Balances of major classes of depreciable assets, by nature or function, at the balance sheet date

c. Accumulated depreciation, either by major classes of depreciable assets or in total, at the balance sheet date

d. A general description of the method or methods used in computing depreciation for major classes of depreciable assets.

2.23 GASB Statement No. 8, *Applicability of FASB Statement No. 93, "Recognition of Depreciation by Not-for-Profit Organizations," to Certain State and Local Governmental Entities,* provides that governmental colleges and universities should not change their accounting and reporting for depreciation of capital assets as a result of FASB Statement No. 93. Governmental colleges and universities are not precluded from depreciating their capital assets by reporting a depreciation allowance in the balance sheet and a provision for depreciation in the statement of changes in the balance of the investment-in-plant fund subsection of the plant funds group. (See paragraph 2.22).

2.24 *Interfund Borrowings.* Interfund borrowings of a temporary nature should be reported as assets of the fund group making the advances as well as liabilities of the fund group receiving the advances.

2.25 Advances from unrestricted current funds or quasi-endowment funds to other fund groups should be recorded as permanent transfers unless there is expectation of repayment within a reasonable period of time. Advances from donor-restricted plant funds and endowment (or term endowment) funds to other funds may be improper. Except for temporary advances, usually up to one year, the term of borrowings and repayments should be disclosed. Where one bank account is maintained for more than one fund, the cash balance may ordinarily be split among the funds in the statements. If a fund in effect has a cash overdraft in such bank account, an interfund borrowing should be shown.

2.26 *Funds Held in Trust by Others.* Funds held in trust by others are resources neither in the possession nor under the control of the institution, but held and administered by outside fiscal agents, with the institution deriving income from such funds. These funds preferably should not be included in the balance sheet with other funds administered by the institution, but should be disclosed parenthetically in the endowment and similar funds group in the balance sheet or in the notes to the financial statements. However, if the institution has legally enforceable rights or claims, including those as to income, such funds may be reported as assets, properly described, in the financial statements. The value of such funds should be supported by annual trust reports available to the institution.

2.27 If the funds were established under irrevocable trusts with no discretionary powers resting with the trustees as to distribution of income, the income should be included either as endowment income with a notation of the amount, or should be separately stated. If the funds were established under revocable trusts, or if the trustees have discretion as to the amounts to be distributed to the beneficiaries, the discretionary amounts of income are tantamount to gifts and should be so reported with disclosure of the amounts.

2.28 *Institutions Operated by Religious Groups.* Accounting records and reporting must be adequately segregated from those of the sponsoring religious group so that the educational entity is in fact accounted for as a separate entity. Facilities made available to the educational entity by the religious group should be disclosed in the financial reports together with any related indebtedness.

2.29 The monetary value of services contributed by members of the religious group should be recorded in the accounts and reported in the financial statements. The gross value of services performed (determined by reference to lay-equivalent salaries by type of personnel) should be recorded as expenditures by department or division, following the same classification as other expenditures, and a like amount should be recorded as gift revenue. The gift revenue should be reduced by the amount of maintenance, living costs, and personal expenses incurred which are related to the contributing personnel and have no counterpart in a lay employee relationship.

2.30 In some cases, checks are drawn to the religious group and charged to expenditure accounts in the same manner as other payroll checks. The religious group then makes a contribution to the institution, which is recorded as a gift. The determination of the contribution would rest with the religious group, since the latter is a separate entity.

2.31 In some cases these institutions inform the reader of the financial report as to the relative value of such contributed services by comparison with the average return on endowment fund investment. Such information should be limited to the notes to the financial statements, and the imputed capitalized value of such contributions should not be reflected in the balance sheet.

Internal Control Structure

2.32 The internal control structure of an educational institution is initiated by the charter or certificate of incorporation, bylaws, and other regulations governing the conduct of the entity. These basic controls are further delineated through organization charts, charts of accounts, accounting manuals, and other documents dealing not only with finance and accounting but with faculty and other educational procedures, research procedures, work programs, etc. Because of the unique characteristics of each educational institution, it is not possible to suggest a uniform or standard internal control structure. In the chapters which follow, internal control considerations applicable to specific areas are discussed.

General Audit Procedures

2.33 General audit procedures and inquiries appropriate to an educational institution may include the following:

1. Determination as to whether required meetings of the governing board have been held.
2. Determination as to whether resolutions of the governing board requiring action in accounting and financial matters have been acted upon, and whether financial matters requiring action of the governing board have been approved.

3. Review of federal report of tax-exempt organizations (Form 990) and federal tax-exemption letter, and notation of current compliance with conditions governing exemption.
4. Examination of support, generally pledge cards, for pledges. Other audit procedures may include investigation of credit standing of pledgors, aging of accounts, review of collections, and confirmation from pledgors.
5. Review of correspondence relating to gifts, with notation of the amount and nature of any restrictions.
6. Comparison of total gifts received in the current period with prior periods and with fund-raising estimates prepared by management. Investigation of substantial differences. Consideration of test confirmation of gifts received.
7. Determination of propriety of interfund transfers, particularly with respect to those involving restricted funds.
8. Determination of collectibility of interfund advances.

2.34 Additional audit procedures applicable to specific areas are discussed in the following chapters.

Chapter 3

Unrestricted Current Funds

3.01 The current funds group includes those economic resources of the institution which are expendable for any purpose in performing the primary objectives of the institution, i.e., instruction, research, extension, and public service, and which have not been designated by the governing board for other purposes. Resources restricted by donors or other outside agencies for specific current operating purposes are accounted for as restricted current funds (see chapter 4).

3.02 Unrestricted current funds designated by the governing board to serve as loan or quasi-endowment funds, or to be expended or appropriated for plant purposes, are included in the sections dealing with such funds. A separate fund subgroup may be established for the unrestricted current funds of auxiliary enterprises.

3.03 The balance sheet accounts of unrestricted current funds consist of the usual asset and liability accounts such as cash, short-term investments, accounts and notes receivable, inventories, prepaid expenses and deferred charges, accounts and notes payable, accrued liabilities, deposits, deferred revenues, and fund balances. Balances resulting from interfund borrowings may be either assets or liabilities.

3.04 The fund balance of unrestricted current funds represents the difference between the assets and liabilities, including deferred revenues, of unrestricted current funds. The fund balance may be subdivided to reflect portions applicable to auxiliary enterprises, gifts allocated to future periods or reserved for specific purposes, purchase orders outstanding, budget balances carried forward or other allocations of the governing board, and the unallocated balance.

3.05 Changes in the balances of unrestricted current funds include the gross amounts of all unrestricted revenues and expenditures applicable to the reporting period as determined in accordance with the accrual basis of accounting; transfers to and from other funds for the period; and transfers between unallocated and allocated subaccounts where such subaccounts are maintained.

3.06 The governing board may elect to transfer unrestricted funds to other fund groups, such as to quasi-endowment funds to serve as endowment until some other purpose is determined as more suitable; to loan funds to supplement governmental appropriations for loan funds; or to plant funds for expansion or rehabilitation or for debt retirement. Similarly, the governing board may elect to return any balances of designated funds appearing in other fund groups to unrestricted current funds.

3.07 The governing board may also elect to set aside unrestricted current funds for specific future operating purposes. Such allocations represent a subdivision of unrestricted current funds balance. Expenditures incurred for the stated purposes are charged to the expenditure accounts appearing in the statement of current funds revenues, expenditures, and other changes.

3.08 The composition of the unrestricted current funds balances (auxiliary enterprises, reserve for encumbrances, allocations, etc.) may be disclosed either in the balance sheet or in the statement of changes in fund balances.

Internal Control Structure

3.09 Internal control structure policies and procedures relevant to unrestricted current funds are similar to those applicable to commercial entities. In addition to the comments on basic internal control in chapter 2, some procedures of particular importance to educational institutions are as follows:

1. Retention of gift documents and other supporting data and recheck of gift and grant documents.
2. Approval of scholarship and other credits to students' accounts.
3. Billing procedures for student fees, auxiliary services, and rentals (including occupancy) and assignment records.
4. Control of tickets, conformity with budgets, and reasonableness of gross margins of auxiliaries.
5. Prenumbered tickets for deposits and advance payments.
6. Coordination and independence of functions of purchasing, budgeting, approvals, and payments for both materials and services.
7. Personnel appointment procedures and records for both academic and nonacademic personnel.
8. Coordination of appointment procedures with budgetary controls.

Audit Procedures

3.10 Audit tests of unrestricted current funds accounts do not vary materially from procedures in audits of commercial entities. Procedures of particular importance to educational institutions may include:

1. Summarization of cash accounts by funds and performance of the usual audit tests simultaneously. Consideration as to whether tests of cash funds, investments, notes receivable, etc. should be carried out at the same time.
2. Reconciliation and comparison of interfund accounts and determination as to whether cash offset is practicable and reasonable.
3. Review of vouchers payable and outstanding purchase orders, and institution's determination of charges to budgetary accounts as between materials and services received and those representing commitments for merchandise or services to be received.

Chapter 4

Restricted Current Funds

4.01 The restricted current funds group consists of those funds expendable for operating purposes but restricted by donors or other outside agencies as to the specific purpose for which they may be expended. Such externally imposed restrictions are to be contrasted with internally created designations imposed by the governing board on unrestricted funds. The circumstances and evidence relative to restrictions may not be clear and may require advice of legal counsel, management and independent auditor judgment, insight, and discretion. Nevertheless, the distinction between the balances of externally restricted and internally designated, but otherwise unrestricted funds, must be maintained in the accounts and disclosed in the financial reports.

4.02 The assets of restricted current funds are almost exclusively of a liquid character such as cash, investments, accounts receivable (including unbilled charges), and amounts due from other funds. The assets are sometimes combined with those of unrestricted current funds for reporting purposes. If the assets are combined, any intrafund borrowings within current funds should be disclosed. Regardless of whether or not the assets are segregated, restricted current fund balances should be disclosed separately in the financial statements and appropriately classified.

4.03 The following list illustrates major subgroupings:

1. Restricted income from endowment funds. The degree of detail required to account for the income depends upon the nature of the restrictions.
2. Gifts restricted for operating purposes, such as scholarship grants, gifts for purchase of library books, etc.
3. Grants from private or governmental sources for research, training, or other sponsored programs.
4. Appropriations from governmental sources for operational purposes where restrictions as to use have been imposed by the appropriating body.
5. Endowment income stabilization reserve. Some institutions have created such reserves by setting aside a portion of the income earned by pooled investments. In any given year, the distribution to the income accounts of participating funds from pooled earnings was made at a fixed or predetermined rate more or less than the actual earnings for the period. The difference was added to or deducted from the reserve for stabilization of income.

4.04 As compared to other accounting and reporting practices recommended elsewhere in this guide, a stabilization reserve established in the manner described above has several deficiencies:

1. The stabilization reserve can represent undistributed income which, if distributed, would be attributable to both restricted and unrestricted funds. The true nature of the reserve, therefore, cannot be accurately reported in the financial statements.
2. To the extent that the reserve includes income earned during the fiscal year attributable to unrestricted current funds but not distributed, unrestricted current funds revenues will be understated. Conversely, distributions from the reserve in excess of current period

earnings result in an overstatement of unrestricted current funds revenues.

3. Questions might arise concerning the propriety of the governing board in withholding amounts of income earned for the benefit of restricted current funds, but not distributed thereto.

4.05 If the endowment income stabilization reserve practice is followed, the independent auditor should qualify his opinion with respect to the fairness of presentation of material amounts of unrestricted funds included in the reserve, as well as to material differences between income distributed and income earned during the period.

4.06 Further additions to such an income stabilization reserve should not be made and proper disposition of the reserve balance should be effected. When the practice of using this reserve is discontinued, the existing reserve balance should be allocated back to the funds from which it was withheld. In the event precise information is not available for such reallocation, reasonable estimates should be used.

4.07 Additions to restricted current funds include (1) restricted gifts for specific operating purposes; (2) restricted endowment income earned or distributed; (3) contracts, grants, and appropriations received from private organizations or governments for research, public service, or other restricted purposes; and (4) income and gains from investments of current restricted funds. Charges to the restricted funds balances include (1) expenditures charged to the funds or amounts transferred to revenues to offset appropriate expenditures; (2) refunds to donors and grantors; (3) losses on investments of current restricted funds; and (4) transfers to unrestricted revenues representing indirect cost recoveries on sponsored programs. The changes during the reporting period are presented in the statement of changes in fund balances.

4.08 Institutions may use a columnar statement of current funds revenues, expenditures, and other changes to distinguish between unrestricted and restricted revenues and expenditures. If such a statement is presented, an amount equivalent to the expenditures is reported as restricted revenues, while the expenditures are classified by functional program similar to the classification of unrestricted expenditures. Some institutions, however, do not distinguish restricted from unrestricted sources of revenues in the statement of current funds revenues, expenditures, and other changes. In this case, the major sources of restricted revenues should be disclosed.

Internal Control Structure

4.09 Internal control structure policies and procedures relevant to the transactions in restricted current funds may include the use of the following accounting and management procedures:

1. Establishment of a separate fund subgroup for restricted current funds consisting of assets, liabilities, fund balances, and addition and deduction accounts for each fund balance.
2. Establishment of appropriate budgetary procedures for the expenditures and transfers from these funds.
3. Maintenance of adequate gift records indicating the authorized use of restricted funds to support classification in the accounts of the institution.
4. Establishment of an adequate acknowledgment procedure covering the receipt of gifts.

5. Submission of statements of financial transactions to grantors and donors.

Audit Procedures

4.10 Auditing of asset and liability accounts of restricted current funds does not present substantial differences from auditing of similar accounts in other organizations. There are, however, important additional audit tests that should be considered in the auditing of the fund balances themselves and the changes therein. These procedures include the following:

1. Examination of selected expenditure vouchers and other documentation to determine that the use of the resources is in conformity with gift and grant documents and that the proper disposition of the fund balance is made upon completion of the project or grant.
2. Review of distribution of endowment income to ascertain whether donor restrictions are being observed.
3. Tests of abstracts of gift and grant documents for conformity with original documents.
4. Review of financial data furnished to grantors and donors.
5. Substantiation of distributions from the income account of the pooled endowment fund.

Chapter 5

Current Funds Revenues

[5.01—5.20] [Superseded by SOP 74-8, *Financial Accounting and Reporting by Colleges and Universities.* See Appendix A.]

Internal Control Structure

5.21 Internal control structure policies and procedures relevant to current funds revenues are similar to many of the procedures applicable to commercial entities. Some of the procedures of particular importance to educational institutions are as follows:

1. Budgetary control over recorded revenues, including comparison with budget estimates and analysis of significant variations.
2. Control over revenues by recording on the accrual basis.
3. Independent control over issuance of credits, allowances (including scholarships), and other adjustments.
4. Procedures for receiving and acknowledging gifts and grants.

Audit Procedures

5.22 A variety of audit tests are generally applicable in reviewing revenue items. Because of the wide variations among educational institutions, it is not practicable to list all the steps used in practice. The following tests are examples of procedures to be considered:

1. Review of each major revenue account and comparison with prior period and budget estimate and determination of reasons for any significant variations.
2. Comparison of revenues with related statistical reports of enrollment, occupancy, meals served, etc., prepared by departments or individuals not related to the revenue-recording or cash-receiving functions.
3. Review and evaluation of the data underlying gifts, grants, and bequests, including gift documents, correspondence, receipt acknowledgments and notifications of the grant awards, minutes of the governing board, and comparison by type or nature with amounts for prior periods.
4. Review of the latest indirect cost computation, and review of the reports on examination of direct and indirect costs by representatives of grantors. Review of the separation of functions methods of apportionment of applicable expenses in cases where the institution is administering large grants involving research centers or similar operations.
5. Review of gross margin percentages of auxiliaries and comparison with those for prior periods and budgets.
6. Tests of records in support of revenues from sporting events including ticket sales records, ticket numbers, free tickets, tax reports, and contracts with other institutions.

Chapter 6

Current Funds Expenditures and Transfers

[6.01—6.22] [Superseded by SOP 74-8, *Financial Accounting and Reporting by Colleges and Universities.* See Appendix A.]

Internal Control Structure

6.23 Internal control structure policies and procedures relevant to expenditures of educational institutions includes many of the practices and procedures common to commercial entities. Questions of particular importance in reviewing internal control in an educational institution may include the following:

1. To what extent are budgetary procedures used to exert control over expenditures for educational as well as capital purposes?
2. Are management reports designed to conform with the concept of "responsibility reporting," that is, reporting of expenditures according to those who are accountable for their control?
3. Have the cost adjustments made by research or other grantors been reasonable considering the related cost claimed by the institution?
4. Are all expenditures recorded through liability or commitment accounts, thus affording a primary control over payments?

Audit Procedures

6.24 The audit program for expenditures of educational institutions will include the tests appropriate to many other kinds of organizations. In addition, the following procedures may be appropriate.

1. Review of procedures for evaluating and reporting contributed services.
2. Review of procedures for evaluating and reporting (for tax, insurance, and other purposes) lodging, meals, or other perquisites furnished to employees.
3. Comparison of expenses with prior year expenses and with budget authorizations, and explanation of significant variations.
4. Analysis of campaign and fund-raising costs. If costs of endowment and building campaigns have been charged against the proceeds of such campaigns, determine that such charges are proper.
5. Consideration of special audit emphasis in the payroll, purchasing, and disbursement areas in view of the following typical factors and tendencies of educational institutions:
   a. Payroll—Salaries and wages usually constitute a very significant portion of total expenditures. If controls over distribution of payroll checks are weak, surprise control of payroll distributions, review and comparison of payroll check endorsements with employee signatures in personnel records, discussions with department heads about selected employees, and review of student-faculty ratios and trends should be considered.
   b. Purchasing and disbursements—Often the procedures surrounding initiation of purchases, receipt of goods and services, and the ultimate payment of invoices are decentralized. If controls over these activities are weak, audit emphasis on approvals and support for disbursements, including visits to selected departments to examine or discuss with appropriate officials specific materials or services received, should be considered.

Chapter 7

Loan Funds

7.01 The loan funds group consists of loans to students, faculty, or staff, and of resources available for such purposes. The terms of gift agreements usually specify that the funds operate on a revolving basis, i.e., repayments of principal and interest are loaned to other individuals. Some loan funds are created on a temporary basis and require that repayments and interest be returned to the grantors. The grants may also designate that the obligation to repay all or part of the loan will be forgiven under certain circumstances. Some gift agreements may also designate the curriculum and geographical domicile of the student borrowers and the financial status of the borrowers.

7.02 The assets of loan funds may consist of cash, notes receivable for loans granted, and temporary investments of cash available for loans. See chapter 2 for a discussion of accounting for investments.

7.03 Notes receivable for loans should be carried at face value less allowance for doubtful loans. Provision for doubtful loans should be charged to the equity account of the specific loan fund. The amount of interest on loans is usually determined either by the donor or the regulations prescribed by the institution, and interest earnings usually should be credited to the specific loan fund equity account.

7.04 Liabilities which appear in the balance sheet of loan funds might consist of amounts due collection agencies for collection fees, amounts due unrestricted funds for unremitted share of administrative costs, and amounts due as refunds on refundable loan funds.

7.05 Changes in loan funds generally consist of gifts, bequests, and government advances restricted to use for loan purposes, interest on loan notes, income from endowment funds restricted to loan purposes, income and gains and losses on investments of loan funds, loans written off or deductions to provide for appropriate allowances for uncollectible loans, administrative and collection costs, transfers to and from other fund groups, and refunds to grantors. Such transactions should be reported in the statement of changes in fund balances of loan funds.

7.06 Interest on loans to students is not ordinarily recorded in the loan funds until collected. In the past, the Department of Education has not recognized loan losses or provisions for loan losses on government loans. Such omissions are rarely significant to the institution's overall financial statements. However, when the auditor reports separately upon government loan funds, he should consider the materiality of any such omissions in relation to the financial statements of government loan funds and their possible effect upon his opinion on the statements of those funds.

7.07 For appropriate disclosure, the source of the funds available for loan purposes at the balance sheet date should be separately identified in the financial statements, such as donor- and governmental restricted loan funds including funds provided by mandatory transfers required for matching purposes, unrestricted funds designated as loan funds, and funds returnable to the donor under certain conditions.

7.08 The financial statements may identify resources available for loans to students separately from those for faculty and staff and should distinguish those which may be reverted to other purposes.

Internal Control Structure

7.09 Internal control structure policies and procedures relevant to loan funds normally affect the financial assistance program, which includes scholarships, fellowships, grants-in-aid, part-time employment, and special arrangements for payment of tuition and fees, as well as the loan program. The financial assistance program is the dual responsibility of academic and financial personnel. The academic representatives develop the broad policies of the financial assistance program. The administrator of financial aid is responsible for administering the program including review of applications, evaluation of need and qualifications of applicants, and amounts and kinds of aid appropriate in the circumstances. The financial officers of the institution are responsible for the custody and disbursement of funds for financial assistance, receipt and custody of the loan notes and the accounting for, reporting, and collection of the loans. The financial officers also have the obligation to inform the student aid administrator concerning the restrictions and limitations which may exist on the use of any of the funds and to monitor their observance. The usual segregation of duties between the disbursing of funds and the recording of receivables and custody of assets are equally applicable to loan fund administration.

Audit Procedures

7.10 The audit program for auditing cash, notes receivable, and investments of educational institutions will include the tests appropriate to many other kinds of organizations. Auditing the loans may include test examination of the notes, confirmation of selected balances, review of loan and collection procedures, tests of computations of interest income, and balancing of details with control accounts. Additional procedures and tests for loan funds which may be appropriate include the following:

1. A test of compliance with special terms and conditions found in restricted loan funds, such as loans limited to students originating from particular geographical areas, loans limited to students pursuing particular courses of study, government loan funds, and so forth.
2. A test of records documenting authorization for forgiveness of repayment of all or a portion of the amount due.
3. A review of conformity with requirements covering refunds of loan funds, transfers to other funds, and interest on loans.
4. A general review of procedures for maintaining records of names, changes of address, and other data with respect to loans receivable.

7.11 The independent auditor also may wish to make inquiries concerning the following items with respect to the financial aid program in general as well as the loan program:

1. Has the student financial aid committee established appropriate policies, standards, and requirements for administering the aid program?
2. Is the financial aid program sufficiently publicized and available to prospective borrowers and other grantees of aid in terms of general rules and regulations, qualifications of applicants, type of aid and resources available, repayment terms, interest, and so forth?
3. Are loans and other aid granted in accordance with the policies, general rules, regulations, and so forth?
4. Are the financial transactions of the funds sufficiently segregated from the financial aid administration?

5. Does the usual segregation of duties in the business office provide adequate safeguards over the collection and disbursement of funds for financial aid and for loans?
6. Does the acknowledgment procedure, internal reporting program, and recording in appropriate minutes provide reasonable safeguards over the receipt of new loan funds or additions to existing funds?
7. Does the business office follow an approved collection and follow-up policy and is the control over loans previously written off adequate?

Chapter 8

Endowment and Similar Funds

8.01 The endowment and similar funds group generally includes endowment funds, term endowment funds, and quasi-endowment funds.

8.02 Endowment funds are funds with respect to which donors or other outside agencies have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity and invested for the purpose of producing present and future income which may either be expended or added to principal.

8.03 Term endowment funds are similar to endowment funds except that, upon the passage of a stated period of time or the happening of a particular event, all or a part of the principal may be expended.

8.04 Quasi-endowment funds (funds functioning as endowment) are funds which the governing board of an institution, rather than a donor or other outside agency, has determined are to be retained and invested. Since these funds are internally designated rather than externally restricted, the governing board has the right to decide at any time to expend the principal.

8.05 Quasi-endowment funds are usually set aside to fulfill the same purpose as endowment funds and, therefore, should be accounted for in the same manner as endowment and term endowment funds. The only significant difference between endowment and quasi-endowment funds is that endowment fund principal is required by the donors or other outside agencies to be retained for the production of income to help meet present and future costs whereas the principal of quasi-endowment funds is retained and invested voluntarily, for the same or similar purposes. In the case of endowment funds the need to maintain the principal or corpus intact is mandatory.

8.06 Annuity and life income funds, if insignificant in amount, may also be included in this group. If significant, these funds should be reported in a separate fund group. The caption "Endowment and Similar Funds" should be used where endowment, term endowment, quasi-endowment, annuity, and/or life income funds are combined or grouped.

8.07 Each endowment and similar fund is accounted for in a separate fund. Each fund will include its own accounts for cash and investments unless the investments are pooled with the investments of other funds. Funds must, of course, be separately invested if the gift instrument so provides. Investments must also be made in accordance with the provisions of the gift instrument if restricted, for example, to investments which are legal for trust funds. It might be permissible under some circumstances to maintain a separate pool for funds required to be invested in securities approved for investment of trust funds. Some funds own both pooled and nonpooled investments; therefore, practical as well as legal considerations determine the accounting for each fund's principal account, its investments, and its income in accordance with the particular purpose to which the income is to be devoted. As indicated in SOP 74-8 [Appendix A], income yield from investments of endowment and similar funds does not include gains and losses on investment transactions, which are considered as changes in the balances of such funds.

Total Return Concept

8.08 Traditionally, educational institutions have accounted for income yield, dividends, interest, rents, royalties, and the like, as revenues available for institutional purposes and have excluded from that category capital gains on investment transactions. Net gains and losses have either been accumulated in a pool in the endowment and similar fund group or distributed periodically to the principal of the individual funds. The majority of educational institutions still follow this practice not only with respect to true endowment funds but all endowment funds, including quasi. This practice is rooted in the traditional legal precedents that, as recipients of gifts and bequests, educational institutions have functioned as charitable trustees when gifts are accepted for administration in contrast to absolute owners of the endowment gifts. Under classical trust doctrines, gains of endowment funds can only be added to principal and not be expended. The accounting for gains as principal is sometimes referred to as the fiduciary accounting principle.

8.09 Beginning with publication in 1969 by the Ford Foundation of *The Law and the Lore of Endowment Funds,* considerable support has been generated for a sharply contrasting view that there is no authoritative support in the law that gains are akin to principal and, therefore, cannot be spent. Advocates of this legal view hold that the trust law is inapplicable to endowment funds and that the corporate law concept is more applicable where the issues involved are administrative in nature, such as endowment investment management and allocation of gains to income or principal. The corporate law concept views the institution as the absolute owner of gifts with the obligation to include gains as income. Under the corporate law concept the income beneficiary and remainderman are usually the same whereas trust law demands a fair division between the income beneficiary and the remainderman (two distinct and sometimes antagonistic interests); gains traditionally have been kept for the remainderman.

8.10 Some institutions, with the advice of their legal counsel, have adopted what is usually referred to as a "total return" approach to endowment fund investment management. This approach emphasizes total investment return—traditional yield plus or minus gains and losses. Some users of a total return approach account for the portion of gain utilized for general operating purposes as revenue instead of as a transfer. Practically all total return approaches emphasize the use of "prudence" and a "rational and systematic formula" in determining the portion of gains which may be appropriated for expenditures and call for the protection of endowment principal from the loss of purchasing power (inflation) as a primary consideration before appropriating gains. Some approaches embrace spreading (deferral and amortization) techniques to eliminate extreme short-term fluctuations in realized gains and losses which often occur as mere accidents of timing under the completed transaction method. Others would combine realized and unrealized gains in a spreading approach. Most total return approaches have been confined to appropriating only gains of quasi-endowment funds whereas some institutions have appropriated gains of virtually all such funds including true endowment. Some approaches restrict the gains available for appropriation to only realized gains whereas others have considered unrealized gains as available for appropriation also.

8.11 In 1972 the National Conference of Commissioners on Uniform State Laws drafted the Uniform Management of Institutional Funds Act as a proposed clarification of the restrictions on trustees' and managers' powers to invest for growth. Among other things, it provides for a standard of prudent use of the excess of realized *and* unrealized appreciation of invested funds over the historic dollar value of the fund. The standard encompasses price level trends and economic conditions.

8.12 Several states have enacted legislation since the late 1960s dealing with the gain utilization question. The new statutes are not consistent as to whether both realized and unrealized gains may be used, the degree to which principal should be protected, or retroactivity of application. One statute *specifies* that the historic dollar value of the fund should be adjusted from time to time to reflect the change in purchasing power of that historic dollar value before appropriating any gains. None of the statutes specifically discusses gain-spreading or related techniques. In some jurisdictions, appropriation of gains may be limited or prohibited by applicable statutory or common law.

8.13 The law and the legal profession, while by no means in accord on the subject, appear to be heading in the direction of elimination of limitations on the governing board's right to appropriate gains for expenditure. The total return concept continues, however, to cause accountants difficulty in that the concept thus far has produced few, if any, practical applications which appear to be *objectively determinable.* No clear *redefinition* of traditional income yield has evolved. The exercise of prudence is subjective and not susceptible to measurement in an accounting sense. The practical applications of the total return concept utilized to date amount substantively to the selection of a "spending rate" usually relating the rate to the market value of the portfolio. They appear in some cases to involve an intolerable element of arbitrariness. Consequently, until a general practice evolves which is *objectively determinable,* the guide would do a disservice to higher education and the accounting profession to sanction as a permissible accounting treatment the inclusion in revenue of gains utilized under a total return approach. Therefore, any portion of gains utilized should be reported in the financial statements as a transfer. To the extent such a transfer is added to current funds, it should be reported separately from traditional income yield of endowment and similar funds and should not be included in total current funds revenues. If gains utilized are treated as revenue or income, the auditor should qualify his opinion. The fact that this guide does not sanction recognition of appropriated gains as revenues should not inhibit the application of the total return policy of investment management, a policy which has economic merit.

8.14 Considerable thought has been given to a total return approach that would be *objectively determinable.* An objectively determinable method would comprehend the following:

1. Inclusion in total return of all ordinary yield and all realized and unrealized net gains, to the extent legally permitted, less
   a. Allowance for spreading of extraordinary market fluctuations over a reasonable period of time, and
   b. Allowance for adjustment of historical dollar value of fund principal for price level changes.
2. Reporting all of the remainder as additions to the funds to which the income is restricted, and if unrestricted, as revenues of unrestricted current funds.
3. Application of this method to all endowment and similar funds, whether or not investments are pooled.
4. Utilization of generally accepted objectively determinable measures for
   a. Market or fair value of investments,
   b. Time period for spreading extraordinary market fluctuations, and
   c. Index for price level changes.

5. Utilization of this method by all institutions adopting the total return concept.
6. Application of this method on a consistent basis.

8.15 Transfers of investments between funds require that consideration be given to the market or appraised value of the securities because any change in value up to the date of the transfer should accrue or be charged to the owning fund for the holding period. As noted above, some transfers may involve legal considerations which require legal advice or court approval before consummation, depending on the terms of the gift instruments giving rise to the endowment.

8.16 Assets of endowment and similar funds usually consist of cash and investments but may also include accounts receivable, prepaid items, and the like. Investments may consist of marketable securities, nonmarketable securities, real estate, patents, copyrights, royalties, participations, etc., or evidences of indebtedness with respect to institutional plant. Investments are accounted for in accordance with the procedures explained in chapter 2.

8.17 Liabilities of endowment and similar funds consist of any form of indebtedness against assets representing investments of endowment real estate, balances due on purchases of investments, and interfund indebtedness arising from interfund transactions.

8.18 Income from endowment and similar funds should be reported in conformance with any limitations on the use of such income. Income from investments should be reported as either for

1. Restricted purposes, credited to the respective unexpended endowment income accounts in current restricted funds, or to fund balances such as endowment, plant, or loan, as specified by the terms of the endowment gift, or
2. Unrestricted purposes, credited to unrestricted current funds revenues.

8.19 Changes in principal of endowment and similar funds are comprised of additional gifts and bequests restricted to endowment, income added to principal as provided in the gift instrument, net gains or losses on investment transactions, transfers to quasi-endowment from other funds, and withdrawals or transfers to other funds. Fund-raising expenses should not be charged to the principal of endowment and similar funds unless they directly relate to the proceeds of a campaign for this purpose.

8.20 Upon termination, the unrestricted principal of term endowment funds should be added to unrestricted current funds revenues and clearly identified or disclosed so that no inference is made that a *new* gift has been received. Such addition should be directly to a group other than unrestricted current funds if the gift instrument specifies such other disposition of the fund.

Internal Control Structure

8.21 Internal control structure policies and procedures relevant to endowment and similar funds include those generally applicable to investments of commercial entities. In addition, internal control structure policies and procedures peculiar to endowment and similar funds may include the following:

1. Segregation of similar funds in fund groups and maintenance of asset accounts for each fund or merged assets for groups of funds.
2. Maintenance of adequate information for each individual fund indicating nature of principal, restrictions on investment of principal or use of income, termination, etc. This usually involves the mainte-

nance by the institution of an up-to-date register of each endowment fund containing summary information about the donor, time and amount of gift, type of fund, any external or internal restrictions, and reference to formal acceptance by the institution, as well as individual files of correspondence with donors and their representatives and copies of all bequests and other documents pertinent to the administration of a gift.

3. Adequate internal reporting of new gifts and the status and changes in principal of all individual or merged funds.
4. Maintenance and periodic review of a record of contingent bequests.
5. Periodic review of basis of distribution of gains and losses to individual funds.

Audit Procedures

8.22 Audit inquiries and tests of assets and fund balances of endowment and similar funds which may be applicable include the following:

1. Review of summary of investments of all funds and performance of the usual audit tests of all investment, principal, and income and gain accounts simultaneously.
2. Review of basis of valuation, amortization of premiums and accumulation of discount policies, and changes in participation in pooled investments. Tests of additions to and deductions from the pool or pools. Tests of computations where unit or share method of accounting for pooled investments is utilized.
3. Consideration of necessity for a valuation allowance if quoted market values of investments are substantially less than cost and there appears to be a permanent impairment in value.
4. Determination that the titles of the fund groups adequately describe the nature of the accounts included therein and that all of the individual funds of a particular group have the same general characteristics.
5. Determination that disclosure is made in the classification of donor-restricted funds as contrasted with unrestricted funds designated by the governing board to serve as quasi-endowment funds.
6. Review of gift acknowledgment procedures and determination that restrictive covenants are being followed.
7. Review of distribution of investment income and tests of accuracy of credits to restricted funds.
8. Review of distribution to individual funds of gains and losses on disposal of investments.
9. Consideration of obtaining confirmation from legal counsel of the propriety of any disposition of realized or unrealized gains.

Chapter 9

Plant Funds

9.01 The plant funds group consists of (1) funds to be used for the acquisition of physical properties for institutional purposes but unexpended at the date of reporting; (2) funds set aside for the renewal and replacement of institutional properties; (3) funds set aside for debt service charges and for the retirement of indebtedness on institutional properties; and (4) funds expended for and thus invested in institutional properties.

9.02 Some institutions combine the assets and liabilities of the four subfund groups for reporting purposes; however, separate fund balances should be maintained. Resources restricted by donors or outside agencies for additions to plant should be recorded directly in the particular fund subgroup, generally unexpended plant funds.

9.03 When physical plant assets are sold or otherwise disposed of, the carrying value should be removed from the asset accounts and net investment in plant should be reduced accordingly. The proceeds may be used to liquidate liabilities, if any, against the property and the remainder added to unexpended plant funds. Such amounts added to unexpended plant funds may be restricted, depending on the source of the funds of the property disposed of, and the educational institution should consider obtaining a legal opinion in that regard. If the proceeds are unrestricted and will not be reinvested in plant, they may be transferred to unrestricted current funds. If unrestricted proceeds are kept in unexpended plant funds, they should be properly disclosed in the financial statements as being unrestricted.

9.04 Student fees specifically assessed for debt service or plant expansion in such a manner as to create an obligation equivalent to an externally imposed restriction should be reported as additions to the appropriate plant fund subgroup. Such a restriction could be created, for example, when an institution publicly represents that it will use certain fees only for the retirement of certain debt or for the construction of a particular building. If, on the other hand, the governing board retains the right at its discretion to use such fees for other purposes, such fees are not restricted and accordingly should be reported as unrestricted current funds revenue.

9.05 Indebtedness incurred to finance plant acquisition, construction, and the like, should be included as a liability of the unexpended plant funds subgroup until the proceeds of the indebtedness are expended, at which time the expended amount and the related liability should be transferred to the investment-in-plant subgroup.

9.06 Board-designated balances in each of the fund subgroups—except for investment in plant—as opposed to funds restricted by donors for plant fund purposes, should be disclosed. Income and gains, net of losses, on investments of both board-designated and donor-restricted plant funds should be added to the fund balance of the related subgroup.

9.07 Transfers from other fund groups to plant funds for the acquisition of physical properties, renewals and replacements, and debt service should be represented by the appropriate transfer of cash or other liquid assets. Temporary advances from other fund groups to plant funds should be made only upon authorization or approval of the governing board stipulating the terms of repayment. If it is determined that such advances cannot or will not be repaid by plant funds, the governing board should authorize the permanent transfer of the funds.

Unexpended Plant Funds

9.08 Assets of unexpended plant funds consist of cash, investments, accounts receivable, and amounts due from other funds.

9.09 Liabilities of unexpended plant funds may consist of accounts payable, bonds, notes, and mortgages payable, to the extent the proceeds are unexpended at the reporting date, and amounts due to other funds.

9.10 Fund balances of unexpended plant funds represent amounts remaining unexpended at the reporting date. Additions to unexpended plant fund balances include donations from private sources restricted to plant purposes; restricted appropriations of governmental agencies; income and gains from the investment of unexpended plant funds; and transfers from other fund groups including those from current funds. Deductions include disbursements for plant purposes; losses on investments of unexpended plant funds; return of unrestricted balances to unrestricted current funds; and other appropriate charges such as fund-raising expenses related to a building fund campaign.

9.11 Asset accounts and corresponding accountability may also be maintained in this subgroup for construction in progress during the period of construction, if not included in the investment-in-plant subgroup.

Funds for Renewals and Replacements

9.12 Assets of funds for renewals and replacements consist of cash, investments, funds on deposit with others, accounts receivable, and amounts due from other fund groups. Liabilities of these funds consist of accounts payable and amounts due to other fund groups for temporary advances.

9.13 Fund balances represent unexpended resources held for renewal and replacement of physical plant and should be subdivided between unrestricted resources designated by the governing board for these purposes and restricted resources including balances arising from agreements with outside agencies such as trustees under bond indentures, as well as restricted gifts, grants, governmental appropriations, and the like. An account or accounts are usually maintained for each specific project or indenture.

9.14 Additions to funds for renewals and replacements arise from mandatory and voluntary transfers from current funds and income and gains on investments of these funds. In some cases governmental appropriations and other gifts and grants are made specifically for these purposes and recorded as direct additions to the restricted portion of the fund balance. Deductions from the fund balance consist primarily of expenditures for renewals and replacements of plant, some of which may be considered as additions to plant assets in the investment-in-plant subgroup, and some may be renewals and replacements of a type not ordinarily capitalized. Other deductions might include losses on investments of these funds and transfers of funds back to unrestricted current funds.

Funds for Retirement of Indebtedness

9.15 Assets of funds for retirement of indebtedness consist of cash, investments, funds on deposit with others, accounts and notes receivable, and amounts due from other fund groups. Liabilities consist of sundry accounts payable for such items as trustees' fees.

9.16 Fund balances represent resources held for the retirement of and interest on debt and include sinking funds established under bond indentures, mortgage amortization payments accumulated but not yet due, and other resources accumulated for interest and debt retirement. Fund balances should be subdivided between unrestricted resources designated by the governing board for these purposes and restricted resources including balances arising from agreements with outside agencies such as trustees under bond indentures, as well as restricted gifts, grants, governmental appropriations, and the like which are recorded or direct additions to the restricted portion of the fund balance. Separate accounts are ordinarily maintained for each debt.

9.17 Additions to fund balances of funds for retirement of indebtedness include mandatory and voluntary transfers from current funds for interest and principal payments; income and gains on investments of these funds; gifts, grants, and governmental appropriations restricted to debt retirement; and transfers from other fund groups as directed by donors, such as expired term endowment, annuity, or life income funds. Deductions from fund balances include payments on principal of debt and interest thereon, trustees' fees and expenses, and any losses on investments of these funds.

Investment in Plant

9.18 Assets of the investment-in-plant subgroup consist of land, buildings, improvements other than buildings, and equipment (including library books). Construction in progress may be included in this subgroup if it is not included in unexpended plant funds.

9.19 The basis of valuation for assets purchased or constructed is cost; for assets acquired by gift, it is fair market value at the date of gift. In the absence of historical cost records, the assets may be stated at historically based appraised values with subsequent additions at cost. The basis of valuation should be adequately disclosed in the financial statements, by footnote or other means. Library books should be valued at cost or some other reasonable basis. For discussion of depreciation see chapter 2.

9.20 Liabilities consist of accounts payable and evidences of indebtedness such as bonds, notes, and mortgages payable for funds borrowed and expended for acquisition or construction of plant assets included in this fund subgroup.

9.21 The net investment in plant is the fund balance account representing the excess of investment-in-plant assets over liabilities. Additions to this fund balance account arise from capital expenditures of unexpended plant funds and funds for renewals and replacements; from reduction of indebtedness made by funds for retirement of indebtedness; from expenditures from current funds for replacement of equipment; and from gifts of plant assets, including equipment, art and other collections, and books. Reductions in the fund balance account result from the recording of disposal, abandonment, or sale of plant assets.

Internal Control Structure

9.22 Internal control structure policies and procedures relevant to transactions in plant funds will be aided by the maintenance of the four subgroups mentioned in this chapter. Features of an internal control structure relevant to plant funds may include the following:

1. Control by the governing board over capital budgets and changes therein.
2. Recording of commitments and appropriations as well as expenditures in control or project accounts as part of the regular system of accounting.
3. Maintenance of plant ledgers.
4. Periodic internal physical inventory of moveable equipment.

5. Custodial control of both fixed and moveable equipment and control of interdepartmental movements.
6. Procedures for control over disposals and salvage.
7. Maintenance of records of property in the custody of, but not owned by, the institution.
8. Authorization and documentation procedures for creation of long-term debt, including records of assets or revenue pledged, sinking funds, or installment payments required.
9. Records documenting building fund campaigns including records of restricted or special gifts.
10. Receiving and acknowledgment procedures for gifts of fixed assets.
11. Procedures for provisions and transfers from unrestricted current funds based on requirements for renewals, replacements, and retirement of indebtedness.

Audit Procedures

9.23 Audit tests of plant funds generally should include the procedures appropriate for commercial entities. Audit procedures peculiar to educational institutions may include the following:

1. Examination of provisions of gifts and bequests for plant purposes.
2. The review and testing, by reference to appropriate documents, of the validity of capitalizing expenditures of current funds representing equipment purchased by such funds. Determination that title to the equipment so acquired is vested in the institution.
3. The review and testing of transactions of building fund-raising campaigns.
4. Review of procedures relating to the receipt of gifts in kind, including methods used in valuing such gifts.
5. Review of provisions of long-term debt agreements and observation that requirements have been met, including the nature and extent of pledging of assets and revenues and approval by governing board.
6. Examination on a test basis of documents supporting other changes in fund balances.

Chapter 10

Other Fund Groups

ANNUITY FUNDS

10.01 The annuity funds group consists of funds acquired by an institution subject to agreements whereby assets are made available to the institution on the condition that the institution bind itself to pay stipulated amounts periodically to designated individuals. Payments of such amounts terminate at a time specified in the agreements.

10.02 In many jurisdictions the "selling" or acceptance of annuities by a nonprofit organization is subject to the regulations of the appropriate governmental department or agency. Annuities can be issued only under regulations promulgated by the agency and, in some instances, investments of the annuity funds must be deposited or a security deposit made with the governmental jurisdiction. The supervising agency may also designate the types of investments which may be made from these funds.

10.03 Upon termination, the principal of annuity funds is transferred to the fund group designated by the grantor or, in the absence of such a designation, to unrestricted current funds revenue and accorded the same treatment as unrestricted expired term endowments.

10.04 There are two methods of recording and reporting annuity funds, only one of which is included in the Manual. The actuarial method requires the recording of the assets at cost or at fair market value at date of receipt. The liability side includes an account for the present value of the aggregate liability for annuities payable, based upon acceptable life expectancy tables, and an account for the fund balance or deficit. When a gift is received, the present value of the annuities payable is credited to the liability account and the remainder to the fund balance. Investment income and gains are credited, and annuity payments and investment losses are charged, to the liability account. Periodically, an adjustment is made between the liability and the fund balance to record the actuarial gain or loss due to recomputation of the liability based upon the revised life expectancy. By recognizing the present value of the annuities as a liability, the actuarial method meets the requirements of generally accepted accounting principles and therefore should be used.

10.05 The method explained in the Manual provides for the recording of the assets at cost or at fair market value at date of receipt with the resulting credit to the annuity fund balance. Income and gains are credited, and losses charged, to the fund balance. Annuity payments are charged to the fund balance.

10.06 Because the method explained in the Manual does not recognize as a liability the present value of the annuities, it is in conflict with generally accepted accounting principles, and therefore should not be used.

10.07 The assets of annuity funds include cash, securities, and other types of investments, the valuation of which is determined and reported in a manner comparable to that for investments of endowment and similar funds. Assets are sometimes merged for investment purposes depending upon the frequency of adjustments of shares owned by individual funds, the actual number of funds, and the regulations of supervisory authorities.

10.08 The liabilities of annuity funds include indebtedness against any of the assets of the funds, annuity payments currently due, amounts due to other funds for advances made on annuity payments, and the actuarial amount of annuities payable.

10.09 Increases in annuity fund balances consist of additions of new gifts in excess of actuarial liability for annuities payable. Decreases include transfers to other funds upon termination of annuity funds. Additional changes in the fund balances occur when an adjustment is made between the liability and the fund balance, representing changes due to revised life expectancy.

10.10 The basic statement of changes in annuity fund balances is usually combined with the changes in life income funds.

Internal Control Structure and Audit Procedures

10.11 Internal control structure policies and procedures and audit procedures that may be applicable to annuity funds do not differ materially from those applicable to endowment funds described in chapter 8. The annuity liability and fund balance amounts should be tested by reference to life expectancy and interest tables.

LIFE INCOME FUNDS

10.12 The life income funds group consists of funds contributed to an institution subject to the requirement that the institution periodically pay the income earned on the assets to designated beneficiaries. Such payments terminate at a time specified in the agreements, usually upon death of a designated individual. In order to qualify for and maintain a tax-exempt status for pooled life income funds, it is extremely important that the institution acting as trustee be thoroughly conversant with the tax laws governing the formation and operation of life income funds.

10.13 Life income funds are usually accounted for as a separate fund group but are combined for reporting purposes with annuity funds. When amounts are not material, both of these fund groups may be reported as a subclassification of endowment and similar funds. The transactions of life income funds should be reported separately and not as current funds revenues or expenditures. A separate set of accounts must be maintained for each life income fund. Upon termination, the balance of the fund is transferred to the fund group designated by the grantor or, in the absence of a designation, to unrestricted current funds and accorded the same treatment as unrestricted expired term endowments.

10.14 The assets of life income funds include cash, securities, and other types of investments, the valuation of which is determined and reported in a manner comparable to that for investments of endowment and similar funds. Assets of life income funds may be separately invested, pooled with other life income fund assets, or pooled with assets of annuity funds and/or endowment and similar funds.

10.15 The liabilities of life income funds include indebtedness against the assets, life income payments currently due, and amounts due other funds for advances made to income beneficiaries.

10.16 Changes in life income fund balances consist of additions of new gifts, gains and losses on investments, and transfers to other funds upon termination of the agreements.

10.17 The financial statement presentation of life income funds is similar to the presentation of, and sometimes combined with, annuity funds.

Internal Control Structure and Audit Procedures

10.18 Internal control structure policies and procedures and audit procedures that may be applicable to life income funds conform generally to those appropriate for endowment funds discussed in Chapter 8.

AGENCY FUNDS

10.19 The agency funds group consists of funds held by an institution as custodian or fiscal agent for others such as student organizations, individual students, or faculty members. Agency funds should be accounted for as a separate fund group although, if immaterial in amount, they may be reported as assets and liabilities of current funds. Transactions of agency funds represent charges or credits to the individual asset and liability accounts and are not transactions of unrestricted or restricted current funds.

10.20 Assets of agency funds include cash, investments, and sometimes accounts receivable or interfund receivables. Liabilities of agency funds include accounts payable to third parties, interfund payables, and balances representing the net assets owing to the individual or organization for which the institution is acting as custodian.

10.21 Accountability for agency funds usually requires the submission of periodic reports of transactions and balances to the individual or organization that owns the net assets. It is adequate to report in the basic financial statements only the assets and liabilities by major type and the net assets held as deposits in custody for others.

10.22 The Manual suggests that a statement of changes in fund balances be submitted showing total balances at the beginning, total additions, total deductions, and total balances at the end of the reporting period. While this statement would give some indication of the magnitude of the transactions, the balances are liabilities and, therefore, this statement should not be considered a basic financial statement. In most cases its presentation is questionable and therefore it should be omitted.

Internal Control Structure

10.23 Internal control structure policies and procedures relevant to agency funds are similar to those over cash, investments, and other assets of the institution. Control is improved by the segregation of such funds in a separate fund group for accounting and reporting purposes. Internal control is exercised by requiring the approval of transactions by the owning individual or organization. In the case of student organizations, additional review may be exercised by a faculty advisor or administrator.

Audit Procedures

10.24 Audit procedures applicable to agency fund assets are comparable to procedures performed with respect to similar assets of other fund groups. Audit procedures applicable to liabilities consist primarily of a test of the transactions, including a review of documentation and confirmation on a test basis with the owning individuals or organizations.

OTHER FUNDS

10.25 The accounting, reporting, and auditing of other fund groups administered by the institution—such as pension funds—are comparable with the procedures for endowment and/or agency funds, and in some instances are comparable with those of commercial pension funds. A review of internal control must be performed in order to tailor the audit procedures to the needs of the particular engagement with respect to these special funds.

Chapter 11

Financial Reports

11.01 Financial reporting for educational institutions should generally include three basic types of financial statements, namely (a) balance sheet, (b) statement of changes in fund balances, and (c) statement of current funds revenues, expenditures, and other changes.

11.02 Accounting Principles Board (APB) Opinion No. 19* refers to the use by all profit-oriented entities of a statement of changes in financial position as a basic financial statement. The statement of changes in fund balances sets forth essentially the same information included in a statement of changes in financial position. Where significant resources or expenditures such as financing activities and investments in plant are not included in the statement of changes in fund balances, such activities may be separately disclosed in a note or elsewhere in the financial statements.

11.03 The statement of current funds revenues, expenditures, and other changes is a statement unique to educational and similar institutions. It is a statement of financial activities of current funds related to the current reporting period showing the details of current funds revenues by source, current funds expenditures by function, and all other changes in current funds. See SOP 74-8 [Appendix A] for definitions and descriptions of revenue sources and expenditure functions, respectively. It does not purport to present the results of operations or the net income or loss for the period as would a statement of income or a statement of revenues and expenses. The net increases or decreases reported on this statement should be the same as the amounts reported as net changes in unrestricted and restricted current funds in the statement of changes in fund balances.

11.04 The statement of current funds revenues, expenditures, and other changes is intended to achieve certain reporting objectives, namely the following:

1. To provide the reader with adequate information concerning the details of the sources and uses of current funds,
2. To enable the institution to report the total of unrestricted and restricted current funds expended for each of the functional categories so that the total level of financial activity for each such function is disclosed, and
3. To facilitate the presentation of a comparison with prior years if desired.

11.05 These objectives may be achieved in other ways. For example, the statement of changes in fund balances may be expanded to show the unrestricted revenues by source, rather than in summary totals only, and a third statement may be used to report the details of expenditures by function. In so doing, however, it should be remembered that revenues arising from the use of restricted funds are not normally the equivalent of restricted current fund additions. Therefore, the amounts earned through the use or expenditure

---

* [Note—APB Opinion No. 19 has been superseded by FASB Statement No. 95, *Statement of Cash Flows.* Not-for-profit entities are excluded from the scope of FASB Statement No. 95. GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Funds and Governmental Entities That Use Proprietary Fund Accounting,* superseded APB Opinion No. 19 for state and local governmental units. Governmental colleges and universities that adopt the AICPA College Guide Model are exempt from the requirement to present a statement of cash flows.]

of such funds should also be disclosed in these basic statements or in the notes thereto.

11.06 Variations in format and presentation also may be desirable in instances where institutional management requirements or practices would be more readily communicated to the reader through such reporting devices. For example, institutions which manage unrestricted gifts as separate resources may prefer to add additional columns in the statement of changes in fund balances and the statement of current funds revenues, expenditures, and other changes in which such gifts received or transferred, and balances at the beginning and end of the reporting period, could be separately disclosed. Similarly, the revenues, expenditures, transfers, assets, liabilities, and fund balances of current funds allocated to auxiliary enterprises, hospitals, or other special activities may be set forth in separate columns as fund subgroups. In all such cases, however, the statements should clearly indicate the unrestricted nature of such funds and related changes for the period. In addition, a total column for all unrestricted current funds revenues, expenditures, and other changes for the period should be included in the appropriate statements.

11.07 The financial statements in SOP 74-8 [Appendix A], thus, are guidelines illustrating the accounting principles and reporting practices embodied throughout this guide. They are not intended to represent the only forms since the requirements of fairness and objectivity are always paramount for both the institution and the independent auditor.

11.08 The balance sheet may be presented with funds arranged sequentially in vertical order as illustrated, or it may be presented in columnar form with a column for each major fund group. Changes in fund balances may be presented in columnar fashion in a single statement as illustrated or in separate statements for each major fund group. Special considerations relating to the use of a columnar statement are the following:

1. In the balance sheet, columnar fund group figures should not be cross-footed in a total column, to reflect an overall financial picture of the institution, unless all necessary disclosures are made, including interfund borrowings.
2. In the statement of changes in fund balances, columns should not be cross-footed unless care is taken to avoid the mislabeling of cross-footed totals and duplication of gross changes.
3. Balances of any fund subgroups necessary for fair presentation, particularly those subgroups segregating donor-restricted from board-designated resources, must be disclosed either in the balance sheet or in the statement of changes in fund balances.

11.09 For adequate disclosure, all separately incorporated but related units for which the reporting institution is fiscally responsible, such as university presses, intercollegiate athletics, and research foundations, should be (1) included in the financial statements, (2) adequately disclosed by notes, or (3) presented in separate financial statements accompanied by and cross-referenced in the basic financial statements of the institution.

11.10 The basic financial statements may be accompanied by supplemental schedules setting forth in greater detail the data included in the basic statements. One such schedule which may be particularly useful to institutions employing the total return concept and/or managing unrestricted gifts as separate resources would be a schedule of current funds expenditures and resources utilized. Such a schedule could relate the total of current funds expenditures and mandatory provisions to the current funds resources which were utilized in meeting these needs. The totals of both sections of the schedule—expenditures plus mandatory provisions and resources utilized—would be equal. Other schedules which might prove to be useful and informative may be the following:

- Summary of gifts received by source and purpose
- Schedule of current funds revenues
- Schedule of current funds expenditures
- Schedules of auxiliary enterprise operations
- Summary of investments
- Summary of property, plant, and equipment
- Schedule of long-term debt
- Details of fund balances and changes therein during the period in each fund within each fund subgroup

Reporting Accounting Changes

11.11 Adjustments resulting from a change in accounting method to comply with recommendations in this audit guide should be treated as adjustments of prior periods, and financial statements presented for the periods affected should be restated appropriately. For guidelines in reporting upon the financial statements that have been restated, the independent auditor should refer to Statement on Auditing Standards (SAS) No. 58, *Reports on Audited Financial Statements,* paragraph 36. For any accounting changes subsequent to those required for conforming with this audit guide, the Committee reaffirms the applicability of APB Opinion No. 20, which defines various types of accounting changes and establishes guides for determining the manner of reporting each type.

11.12 APB Opinion No. 20 deals with the reporting of changes in accounting principles and estimates, changes in the reporting entity, and the correction of an error in previously issued financial statements. However, if an industry audit guide prepared by a committee of the American Institute of Certified Public Accountants prescribes the manner of reporting such changes, the provisions of the Opinion do not apply. This audit guide prescribes that the provisions of APB Opinion No. 20 apply to the statements of colleges and universities except for those provisions which relate to the presentation of results of operations for business organizations (and, therefore, have no counterpart in statements of colleges and universities) such as:

1. Inclusion, in the net income of the period of change, of the prior year cumulative effect on retained earnings of changing to a new accounting principle.
2. Disclosure of pro forma net income and per share data on the face of the income statement.

11.13 In most cases, as applied to educational institutions, the reporting of a change in accounting principles would be as follows:

1. The financial statements for prior periods would be presented as previously reported,
2. The effect of the change on the current and prior periods shown would be disclosed in the financial statements or in the notes to the statements, and
3. The cumulative effect of the change would be shown in the statement of changes in fund balances.

Illustrative Financial Statements

[11.14—11.19] [Superseded by SOP 74-8, *Financial Accounting and Reporting by Colleges and Universities.* See Appendix A.]

Chapter 12

Reports of Independent Auditors

12.01 The opinions of independent auditors are expressed on the basic financial statements of the institution as a whole. In addition, opinions of independent auditors may be required with respect to special financial reports covering individual funds or activities. The independent auditor should refer to SAS No. 62, *Special Reports,* for a discussion of the general requirements respecting special reports.

Form of Reports

12.02 The standard report format has heretofore been used frequently by independent auditors in reporting on the basic financial statements of educational institutions. This report refers to "results of operations" commonly deemed to embody changes in net worth as well as in revenues, expenses, and net income for the period.

12.03 As described in chapter 11, the statement of current funds revenues, expenditures, and other changes does not purport to present the results of operations or the net income for the period of the institution as a whole, as would an income statement or a statement of revenues and expenses. For example, the statement of current funds revenues, expenditures, and other changes does not include a provision for depreciation. On the other hand, it does include charges for capital outlay, such as mandatory provisions for payment of principal of indebtedness, mandatory provisions for renewals and replacements of equipment, and expenditures from current funds for renewals and replacements of equipment.

12.04 As a result of the nature of the statements described above, the independent auditor's opinion should use wording more descriptive of the information in the statements rather than "results of operations." An example of such wording is "changes in fund balances and current funds revenues, expenditures, and other changes."

12.05 An example of the independent auditor's report follows.

<u>Independent Auditor's Report</u>

The Board of Trustees
Sample Educational Institution:

We have audited the accompanying balance sheet of Sample Educational Institution as of June 30, 19__ and the related statements of changes in fund balances and current funds revenues, expenditures, and other changes for the year then ended. These financial statements are the responsibility of the Institution's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Sample Educational Institution as of June 30, 19__, and the changes in fund balances and the current funds revenues, expenditures, and other changes for the year then ended in conformity with generally accepted accounting principles.

[Signature]

[Date]

12.06 Where the basic financial statements are accompanied by supplemental schedules, the extent of the independent auditor's responsibility should be indicated.

12.07 For information on auditing federally funded student financial assistance programs, refer to the U.S. Department of Education Audit Guide, *Audits of Student Financial Assistance Programs.* Copies of the Guide can be obtained from:

U.S. Department of Education
Office of Inspector General
330 C Street SW
Washington, DC 20202

Appendix A

Statement of Position 74-8

FINANCIAL ACCOUNTING AND REPORTING BY COLLEGES AND UNIVERSITIES

August 31, 1974

Issued by Accounting Standards Division
American Institute of Certified Public Accountants

NOTICE TO READERS

Statements of Position of the Accounting Standards Division present the conclusions of at least a majority of the Accounting Standards Executive Committee, which is the senior technical body of the AICPA authorized to speak for the Institute in the areas of financial accounting and reporting. Statement on Auditing Standards No. 69, *The Meaning of* Present Fairly in Conformity With Generally Accepted Accounting Principles *in the Independent Auditor's Report,* identifies AICPA Statements of Position as sources of established accounting principles that an AICPA member should consider if the accounting treatment of a transaction or event is not specified by a pronouncement covered by Rule 203 of the AICPA Code of Professional Conduct. In such circumstances, the accounting treatment specified by this Statement of Position should be used or the member should be prepared to justify a conclusion that another treatment better presents the substance of the transaction in the circumstances. However, an entity need not change an accounting treatment followed as of March 15, 1992 to the accounting treatment specified in this Statement of Position.

AICPA

American Institute of Certified Public Accountants
1211 Avenue of the Americas, New York, New York
10036 (212) 575-6200

August 31, 1974

Marshall S. Armstrong, CPA
Chairman
Financial Accounting Standards Board
High Ridge Park
Stamford, Connecticut 06905

Dear Mr. Armstrong:

Proposal to Amend the
AICPA Industry Audit Guide
on Audits of Colleges and
Universities

Two recent publications on college and university financial accounting and reporting have endorsed expansion, clarification, and revision of the AICPA Industry Audit Guide on *Audits of Colleges and Universities* (Audit Guide) in certain respects. The new publications are *College and University Business Administration—Administrative Service*, published in May 1974 by the National Association of College and University Business Officers, and *Report of the Joint Accounting Group*, published in March 1974 by the Western Interstate Commission for Higher Education.

Members of the AICPA Accounting Standards Task Force on Colleges and Universities participated in a consultative capacity in the development of both publications and the Task Force has prepared the accompanying Statement of Position. Its purpose is to bring to your attention amendments to the Audit Guide recommended by the Task Force to conform the guide to the new publications and to request that the profession be advised, by whatever means seem appropriate, whether FASB concurs with the proposed amendments.

The amendments would give effect to the revenue, expenditure, and transfer descriptions and classifications set forth in Part 5 of the Administrative Service. They would be consistent with recommendations in those respects in the *Report of the Joint Accounting Group.*

Issuance of this Statement of Position will help to apprise independent auditors and others who are interested in college and university accounting and financial reporting matters of the existence of the two new publications and of the recommendation of the Task Force as to the appropriate corresponding amendment of the Audit Guide. We urge, however, as a further and more conclusive step that FASB advise the accounting profession at an early date as to whether it believes the proposed amendments are appropriate and should be regarded as having the same authoritative support as if they had been included in the Audit Guide initially. A prompt indication to the profession is especially desirable in view of the extensive recent distribution of the two aforementioned publications and in anticipation that some institutions may want to adopt the revised classifications in their fiscal 1974 financial statements.

Members of the Task Force will be glad to meet with you or your representatives to discuss these proposals. It would appreciate being advised as to the Board's proposed action on its recommendations.

Sincerely yours,

ACCOUNTING STANDARDS TASK FORCE
ON COLLEGES AND UNIVERSITIES

Jay H. Anderson, Chairman
Delford W. Edens
Daniel D. Robinson
Russel F. Viehweg

Audits of Colleges and Universities

Background Information

At the time of final editing of the Industry Audit Guide on *Audits of Colleges and Universities* (Audit Guide) in June 1973, the Committee of AICPA members which prepared the Audit Guide was aware of discussions then in progress among members of the Accounting Principles Committee of the National Association of College and University Business Officers (NACUBO) and the National Center for Higher Education Management Systems (NCHEMS) concerning the classification of revenues and expenditures in higher education financial accounting and reporting. The Preface of the Audit Guide mentions that the guide was developed with the coordination and cooperation of representatives of NACUBO.

The fundamental accounting principle relating to presentation of revenues and expenditures which was adopted by the Audit Guide Committee was that *revenues should be classified by source and expenditures by function.* The Committee felt that, as long as this basic classification philosophy was adhered to, any reasonable amount of detail of revenues, expenditures, and transfers desired by the industry would be agreeable to the accounting profession. The detailed categories of revenues, expenditures, and transfers shown in the Audit Guide reflected the most recent recommendations of NACUBO at that time and deviated somewhat from those displayed in the 1968 revised edition of *College and University Business Administration*, or *CUBA* (1968). CUBA (1968) was published by the American Council on Education and, until publication of the Audit Guide by the AICPA in August 1973 and Part 5 of *College and University Administration—Administrative Service* (Administrative Service) by NACUBO in May 1974, was regarded as the major authoritative pronouncement on college and university accounting and financial reporting.

Efforts were launched in the summer of 1969 by NACUBO to revise *CUBA* (1968). Efforts were under way at NCHEMS to prepare a Higher Education Finance Manual (HEFM), a project sponsored by the U.S. Office of Education to provide, among other things, procedures and formats for reporting financial data needed for planning and management at the institutional as well as state and federal government levels. A meeting of representatives of each of three interested groups (NACUBO, NCHEMS, and AICPA) resulted in the concept of a joint effort to identify and clarify areas of difference and explore mutually satisfactory ways of developing more uniformity. The Chairman of the AICPA Committee which had developed the Audit Guide and two other members of that Committee, which officially dissolved in October 1973, were invited to become members, along with NACUBO and NCHEMS representatives, of a new Joint Accounting Group (JAG) to carry out these objectives.

JAG's work was completed with the publication by the Western Interstate Commission for Higher Education, Boulder, Colorado, in March 1974 of the *Report of the Joint Accounting Group.* The primary recommendation of that report was that, with the exception of current funds revenues, expenditures and transfers, higher education institutions should utilize the accounting definitions and practices outlined in the Audit Guide. The JAG report in Appendixes I and II set forth recommended revenue, expenditure, and transfer category descriptions which represented a revision of those presented in the Audit Guide. The JAG also recommended that its revised revenue, expenditure, and transfer categories be incorporated into the Audit Guide and the new Administrative Service. The categories recommended by the JAG were later used by NACUBO in its preparation of Part 5 of the new Administrative Service. Thus, the report of the JAG was an initial step toward the inclusion of the revised revenue, expenditure, and transfer categories in the new Administrative Service which the Task Force now considers more current than those included in the Audit Guide.

The JAG was formed in the summer of 1973 and at the same time, at the request of officials of NACUBO, the Accounting Standards Division of the AICPA organized a Task Force, consisting of four of the members of the former Audit Guide Committee (including the three individuals participating with the JAG), to consult with NACUBO's Accounting Principles Committee regarding the revision of *CUBA* (1968). This revision was published as a section (Part 5) of the new looseleaf Administrative Service. It can be obtained by subscription from NACUBO, Suite 510, One Dupont Circle, Washington, D.C. 20036. The new Administrative Service replaces *CUBA* (1968) as the major authoritative pronouncement on college and university accounting and financial reporting published by the industry.

Both the NACUBO and JAG efforts were conducted in close coordination with each other and involved overlap of representatives of AICPA, NACUBO, and NCHEMS. Both of these projects involved a certain amount of refinement of revenue, expenditure, and transfer definitions and classifications. However, no deviations from the fundamental accounting principles, auditing procedures or standards of financial statement presentation from those set forth in the Audit Guide were advocated in the two publications. Neither of the publications deals at all with auditing standards. The participation of AICPA Committee and Task Force members in these two publication efforts was geared to provide the two primary constituencies (NACUBO and NCHEMS) with background information and explanations about the content of the Audit Guide and to assist them in making sure that their publications did not deviate from the basic accounting principles and standards of financial reporting contained in the Audit Guide. Even though the JAG report and the new Administrative Service reflect different literary styles, the Task Force members who were involved in the consulting projects believe that those publications do not contain any significant deviations from the accounting principles and reporting standards reflected in the Audit Guide. The Audit Guide concept of revenues by source and expenditures by function has been followed.

Recommendation

The Task Force believes that the descriptions and classifications of revenues, expenditures, and transfers, as they pertain to current funds, set forth in Chapters 5:2 (Current Funds), 5:6 (Chart of Accounts), and 5:7 (Illustrative Exhibits) of the new Administrative Service should be recognized by practitioners as representing more current descriptions and classifications than those presented in the Audit Guide and that, until such time as the Audit Guide is revised, independent auditors should refer to those parts of NACUBO's new Administrative Service, which are appended to this Statement of Position, in connection with current funds revenue, expenditure, and transfer account descriptions and classifications.

Specifically, the Task Force believes the Audit Guide should be considered as being superseded by the Administrative Service as follows:

a. Chapter 5.01-5.20, Current Funds Revenues, of the Audit Guide, through the section on Expired Term Endowments, should be superseded by the section Current Funds Revenues beginning on Page 2 of Chapter 5:2, Current Funds, of the Administrative Service.

b. Chapter 6.01-6.22, Current Funds Expenditures and Transfers, of the Audit Guide, through the section on Other Transfers — Unrestricted Current Funds, should be superseded by the section on Current Funds Expenditures and Transfers, beginning on Page 6 of Chapter 5:2, Current Funds, of the Administrative Service.

c. The Illustrative Financial Statements in Exhibits 11.14-11.16 of the Audit Guide should be superseded by Chapter 5:7, Illustrative Exhibits, of the Administrative Service.

d. The section of Chapter 5:6, Chart of Accounts, of the Administrative Service, beginning with Current Funds Revenues Accounts through the end of Page 10, should be added to the Audit Guide as Appendix A.

The Task Force further believes that adoption of the expanded descriptions and classifications should be effective for all fiscal years beginning after June 30, 1974.

Current Funds

The current funds group includes those economic resources of a college or university which are expendable for the purpose of performing the primary missions of the institution—instruction, research, and public service—and which are not restricted by external sources or designated by the governing board for other than operating purposes. The term "current" means that the resources will be expended in the near term and that they will be used for operating purposes.*

The Current Funds group has two basic subgroups—unrestricted and restricted. Unrestricted current funds include all funds received for which no stipulation was made by the donor or other external agency as to the purposes for which they should be expended. Restricted current funds are those available for financing operations but which are limited by donors and other external agencies to specific purposes, programs, departments, or schools. Externally imposed restrictions are to be contrasted with internal designations imposed by the governing board on unrestricted funds. Internal designations do not create restricted funds, inasmuch as the removal of the designation remains at the discretion of the governing board.

The distinction between unrestricted and restricted funds is maintained through the use of separately balanced groups of accounts in order to provide acceptable reporting of stewardship to donors and other external agencies. This distinction also emphasizes to governing boards and other sources of financial support the various kinds of resources of the Current Funds group that are available to meet the institution's objectives.

Separate accounting entities may be provided for auxiliary enterprises, hospitals, and independent operations in either the Unrestricted Current Funds or Restricted Current Funds subgroup or both, as appropriate.

Assets, Liabilities, and Fund Balances of Current Funds

Assets usually consist of cash, accounts receivable, including unbilled charges, notes receivable, undrawn appropriations, investments, amounts due from other fund groups, inventories, prepaid expenses, and deferred charges. "Unbilled charges" are those which have been earned but which, because of

*Reprinted from *College and University Business Administration*, second revised edition (1974), by permission of the National Association of College and University Business Officers.

inadequate information, incomplete projects or programs, or the timing of the billing cycle, have not been formally billed at the balance sheet date. "Undrawn appropriations" are those to which the institution is entitled, but which have not been remitted or made available to the institution by the appropriating federal, state, or local agency. "Deferred charges" are expenditures that are related to projects, programs, activities, or revenues of future fiscal periods.

Liabilities usually consist of accounts and notes payable, accrued liabilities, deposits, amounts due to other fund groups, and deferred credits. Accrued liabilities include such items as interest, wages, salaries, and taxes. Deferred credits are those revenues of unrestricted current funds that are applicable to a future period, when they become earned.

The individual assets and liabilities, but not the fund balances, of unrestricted and restricted current funds are sometimes combined for reporting purposes, but, if they are combined, the borrowings between unrestricted and restricted funds should be disclosed by footnote or other appropriate means.

The fund balances may be subdivided to show allocations applicable to auxiliary enterprises, hospitals, independent operations, outstanding encumbrances, other allocations by operating management or by the governing board, budget balances brought forward from prior fiscal periods, and the unallocated balance.

Changes in the balances of unrestricted current funds include the gross amount of all unrestricted revenues and expenditures applicable to the reporting period, as determined in accordance with the accrual basis of accounting, and transfers to and from other fund groups for the period. Significant allocations of unrestricted current fund balances should be disclosed.

The fund balances of restricted current funds should be classified in the accounting system to show the various classes and sources of funds and purposes of restriction. Such restrictions often relate to the use of endowment fund income; gifts, grants, and contracts from private and governmental sources; and legislative appropriations. Further breakdowns may be provided to show amounts restricted to auxiliary enterprises, hospitals, and independent operations, if such activities are the beneficiaries of restricted current funds.

Additions to fund balances of restricted current funds arise from the sources indicated in the preceding paragraph. Deductions from restricted fund balances result from:

1. Direct expenditures and mandatory transfers.
2. Refunds to donors and other external agencies.
3. Amounts transferred to unrestricted revenues representing indirect cost recoveries on appropriate programs.
4. Nonmandatory transfers.

Current Funds Revenues

Current funds revenues include (1) all unrestricted gifts, grants, and other resources earned during the reporting period and (2) restricted resources to the extent that such funds were expended. Current funds revenues do not include restricted current funds received but not expended or resources that are restricted by external persons or agencies to other than current funds.

Interdepartmental transactions between service departments and storerooms and other institutional departments or offices should not be reported as revenues of the service departments but rather as reductions of expenditures of such departments, since these transactions are essentially interdepartmental transfers of costs. The billed price of services and materials obtained from service departments and central stores by offices and departments of the institution should be accounted for as expenditures of those offices and departments, just as if they had been obtained from sources outside the institution. Any difference between costs and billed prices as recorded in the service department account, whether credit or debit, should be reported under the Institutional Support expenditures classification.

Certain intrainstitutional transactions, however, should be reflected in the operating statements of the institution as revenues and expenditures. Materials or services produced by an instructional department by a by-product of the instructional program and sold to other departments or to auxiliary enterprises or hospitals—for example, milk sold by the dairy department to the dining halls—should be treated as sales and services revenues of the selling department and as expenditures of the receiving department. Sales and services of auxiliary enterprises to other departments—for example, catering by the food services department in the entertainment of institutional guests and sales by the college store to instructional departments—should be treated as sales and services revenues of the respective auxiliary enterprises and as expenditures of the unit receiving the services or materials.

Unrestricted and restricted current funds revenues should be grouped into the following major classifications by source of funds:

Tuition and Fees

Federal Appropriations

State Appropriations

Local Appropriations

Federal Grants and Contracts

State Grants and Contracts

Local Grants and Contracts

Private Gifts, Grants, and Contracts

Endowment Income

Sales and Services of Educational Activities

Sales and Services of Auxiliary Enterprises

Sales and Services of Hospitals

Other Sources, *including expired term endowments and expired life income agreements, if not material; otherwise, separate category*

Independent Operations

Tuition and Fees

This category should include all tuition and fees assessed against students (net of refunds) for educational purposes. Tuition and fees should be recorded as revenue even though there is no intention of collection from the student. The amounts of such remissions or waivers should be recorded as expenditures and classified as Scholarships and Fellowships or as staff benefits associated with the appropriate expenditure category to which the personnel relate.

When specific fees are assessed under binding external restrictions for other than current operating purposes—for example, debt service on educational plant or on renewals, replacements, or additions to plant—they should be reported as additions to the appropriate fund group (in the above example, plant funds), since they are not legally available for current operating purposes. Fees normally are not considered as assessed under binding external restrictions unless there is an explicit representation to the individuals remitting the fees that the fee or a specific portion thereof can be used only for the specific nonoperating purpose.

If some portion of total tuition or fee receipts is pledged under bond indenture agreements, the total receipts should be reported as unrestricted current funds revenues and the pledged amount treated as a mandatory transfer to plant funds.

If some portion of tuition or fees is allocated by action of the governing board, or subject to change by the governing board alone, for other than operating purposes, such as financing construction, the whole of the tuition charges or fees should be recorded as unrestricted current funds revenues and the portion allocated should be treated as a nonmandatory transfer to the appropriate fund group (in the above example, plant funds).

Revenues pledged under bond indenture agreements should not be reported as additions to plant funds, but should be reported as unrestricted current funds revenues, and funding of debt service requirements treated as mandatory transfers.

If an all-inclusive charge is made for tuition, board, room, and other services, a reasonable distribution should be made between revenues for tuition and revenues for sales and services of auxiliary enterprises.

Revenues from tuition and student fees of an academic term that encompasses two fiscal years—for example, a summer session—should be reported totally within the fiscal year in which the program is predominantly conducted.

If tuition or fees are remitted to the state as an offset to the state appropriation, the total of such tuition or fees should be deducted from the total for state appropriations and added to the total for tuition and fees.

Governmental Appropriations

This category includes (1) all unrestricted amounts received for current operations from, or made available to an institution by, legislative acts or local taxing authority and (2) restricted amounts from those same sources to the extent expended for current operations. This category does not include governmental grants and contracts. Amounts paid directly into a state or local retirement system by the appropriating government on behalf of the college or university should be recorded as revenue of the institution. This category does not include institutional fees and other income reappropriated by the legislature to the institution.

The determination of whether a particular government appropriation should be classified as restricted or unrestricted funds is based on the ability of the governing board of the institution to effect a change in the intended use of the funds. If a change in a particular restriction can be made without having to go through the legislative process, the funds should be considered unrestricted. Funds are unrestricted even if they are distributed to the institution for purposes specified by an intermediate group, such as the governing board. In this case, if a change in the use of funds needs to be made, it can be made by the intermediate body without going through the legislative process; the funds therefore would be unrestricted. Such appropriations should be considered unrestricted funds unless the restrictions are so specific that they substantially reduce the institution's flexibility in financial operations. Appropriations in terms of major object classes or to colleges and branch institutions should be classified as unrestricted current funds.

Governmental appropriations should be classified to identify the governmental level—federal, state, or local—of the legislative body making the appropriation to the institution. The fundor level is the level of the agent that makes the decision that the moneys will be appropriated to the particular purpose for which they ultimately are expended. For example, if the federal government stipulates a specific use for some funds that merely flow through the state to the institution, the funds should be classified as federal funds. However, if the federal government distributes funds to the state for unspecified general purposes—for example, general revenue sharing—and the state then appropriates all or a portion of those funds, the funds received by the institution should be classified as state rather than federal funds.

Governmental Grants and Contracts

This category includes (1) all unrestricted amounts received or made available by grants and contracts from governmental agencies for current operations and (2) all amounts received or made available through restricted grants and contracts to the extent expended for current operations.

Amounts equal to direct costs incurred by restricted current funds should be recorded as revenues of those funds, while amounts equal to associated indirect cost recoveries should be reported as unrestricted current funds revenues.

The government fundor level should be disclosed using the same criterion described for governmental appropriations.

Private Gifts, Grants, and Contracts

This category includes amounts from nongovernmental organizations and individuals, including funds resulting from contracting or the furnishing of goods and services of an instructional, research, or public service nature. It includes all unrestricted gifts, grants, and bequests as well as all restricted gifts, grants, and contracts from nongovernmental sources to the extent expended in the current fiscal year for current operations. Gifts, grants, and contracts from foreign governments should be treated as private gifts, grants, and contracts. Income from funds held in revocable trusts or distributable at the direction of the trustees of the trusts should be reported as a separate revenue source under this classification. This category excludes revenues derived from contracts and other activities, such as utility services, that are not related directly to instruction, research, or public service.

Amounts equal to the direct costs incurred by restricted current funds should be reported as revenues of those funds, while amounts equal to the associated indirect cost recoveries should be recorded as unrestricted current funds revenues.

Endowment Income

This category includes:

1. Unrestricted income from endowment and similar funds.
2. Restricted income from endowment and similar funds to the extent expended for current operations.
3. Income from funds held by others under irrevocable trusts, which should be identified separately under this revenue heading.

The unrestricted income from investments of endowment and similar funds credited to unrestricted current funds revenues should be the total ordinary income earned (or yield), except for income that must be added back to the principal in accordance with the terms of the agreement of donation. If endowment fund investments include real estate, the income should be reported on a net basis after allowing for all costs of operating and managing the properties.

Income from investments of endowment and similar funds does not include capital gains and losses, since such gains and losses are accounted for in the Endowment and Similar Funds group as additions to and deductions from fund balances. If any portion of the gains of endowment or quasi-endowment funds is utilized for current operating purposes, the portion so utilized should be reported as a transfer rather than as revenue (see Chapter 5:3).

When investments of endowment and similar funds are pooled, the amounts reported as revenues of unrestricted current funds and as additions to restricted current funds should be substantially equal to the amounts earned during the fiscal period and attributable to the various funds.

Many institutions have established endowment income stabilization reserves to spread or allocate current investment income. Two methods have been followed in establishing such reserves.

Under one method, a portion of the total revenue from the investment pool is not allocated to the participating funds, but is set aside in a stabilization reserve; the balance of the investment pool revenue is distributed to the participating funds. This method is not in accordance with generally accepted accounting principles for the following reasons:

1. The balance in the stabilization reserve may represent undistributed income attributable to both restricted and unrestricted current funds. Thus, the balance in the reserve cannot be reported accurately in the financial statements.
2. To the extent any of the undistributed income earned during the fiscal year is attributable to unrestricted current funds, an understatement of revenues of unrestricted current funds will occur.
3. Questions might arise as to the authority of the governing board to withhold amounts of income attributable to, but not distributed to, restricted current funds.

Institutions carrying balances in endowment income stabilization reserves created under this method should dispose of them as appropriate.

The second method, which conforms to generally accepted accounting principles, would distribute *all* income from the pools to the participating funds. The amount applicable to unrestricted current funds would be reported as endowment income. Any amounts set aside for a stabilization reserve should be shown as an allocation of the unrestricted current funds balance and appropriately reflected in the balance sheet as a subdivision of that balance. Amounts applicable to restricted current funds should be reported as an addition to those fund balances. The amounts expended from such balances should be shown as revenues of endowment income in the restricted current funds. Amounts unexpended would remain as balances to be carried forward to the next period.

Sales and Services of Educational Activities

This category includes (1) revenues that are related incidentally to the conduct of instruction, research, and public service and (2) revenues of activities that exist to provide an instructional and laboratory experience for students and that incidentally create goods and services that may be sold to students, faculty, staff, and the general public. The type of service rendered takes precedence over the form of agreement by which these services are rendered. Examples of revenues of educational activities are film rentals, sales of scientific and literary publications, testing services, and sales of products and services of dairy creameries, food technology divisions, poultry farms, and health clinics (apart from student health services) that are not part of a hospital. Revenues generated by hospitals (including health clinics that are a part thereof) should be classified as sales and services of hospitals.

If sales and services to students, faculty, or staff, rather than training or instruction, is the purpose of an activity, the revenue should be classified as sales and services of auxiliary enterprises or hospitals.

Sales and Services of Auxiliary Enterprises

This category includes all revenues generated through operations by auxiliary enterprises. An auxiliary enterprise is an entity that exists to furnish goods or services to students, faculty, or staff, and that charges a fee directly related to, although not necessarily equal to, the cost of the goods or services. The general public incidentally may be served by some auxiliary enterprises.

Auxiliary enterprises usually include residence halls, food services, intercollegiate athletics (if essentially self-supporting), college unions, college stores, and such services as barber shops, beauty parlors, and movie theaters. Even though they may serve students and faculty, hospitals are classified separately because of their size and relative financial importance.

This category is limited to revenues derived directly from the operation of the auxiliary enterprises themselves. Revenues from gifts, grants, or endowment income restricted for auxiliary enterprises should be reported under their respective source categories.

Sales and Services of Hospitals

This category includes revenues (net of discounts, allowances, and provision for doubtful accounts) generated by hospitals from daily patient, special, and other services. Revenues of health clinics that are part of a hospital should be included in this category. Not included are revenues for research and other specific-purpose gifts, grants, or endowment income restricted to the hospital. Such funds should be included in the appropriate revenue sources described above.

Other Sources

This category should include all sources of current funds revenue not included in other classifications. Examples are interest income and gains and losses on investments in current funds, miscellaneous rentals and sales, expired term endowments, and terminated annuity or life income agreements, if not material.

Note: It is appropriate to subtotal all revenues described; the subtotal excludes revenues of independent operations.

Transfers From Other Funds

Unrestricted amounts transferred from other fund groups back to the Current Funds group are not revenues of the current funds. An example is the return of quasi-endowment funds from the endowment and similar funds to unrestricted current funds. Such amounts should be identified separately and included in Nonmandatory Transfers (see expenditure categories).

Independent Operations

This category includes all revenues of those operations which are independent of, or unrelated to, but which may enhance the primary missions of the institution—instruction, research, and public service. Included are revenues associated with major federally funded research laboratories and other operations not considered an integral part of the institution's educational, auxiliary enterprise, or hospital activities. This category does not include the net profit (or loss) from operations owned and managed as investments of the institution's endowment funds.

Additions to Fund Balances

The term "additions" is in contrast to revenues and transfers. Additions are amounts received or made available to the restricted current funds during the reporting period as distinguished from the amounts of restricted funds expended during the fiscal period, which are reported as restricted fund revenues.

Current Funds Expenditures and Transfers

Current funds expenditures represent the costs incurred for goods and services used in the conduct of the institution's operations. They include the acquisition cost of capital assets, such as equipment and library books, to the extent current funds are budgeted for and used by operating departments for such purposes. If the amount of ending inventories or the cost of services benefiting subsequent fiscal periods is material (in terms of effect on financial statements), both inventories and deferred charges should be recorded as assets and previously recorded expenditures appropriately decreased. In a subsequent fiscal period these inventories and deferred charges as consumed should be included as expenditures of that period. Significant inventories of materials are usually present in central stores.

A capital asset is defined as any physical resource that benefits a program for more than one year. Capital expenditures therefore include funds expended for land, improvements to land, buildings, improvements and additions to buildings, equipment, and library books. Most institutional accounting systems provide for recording at least a portion of capital expenditures in the current fund expenditures accounts of the various operating units. Whether an expenditure is to be considered a capital expenditure is generally a matter for institutional determination, or in the case of some public institutions, it is prescribed by state regulation.

The general criteria for defining a capital asset are the relative significance of the amount expended and the useful life of the asset acquired, or in the case of repairs and alterations, the extent to which the useful life is extended. For expenditure reporting purposes, any item costing more than a specified amount, as determined by the institution or appropriate governmental unit, and having an expected useful life of more than one year generally should be classified as a capital expenditure.[1]

Interdepartmental transactions ordinarily should be accounted for as an increase in current fund expenditures of the department receiving the materials, services, or capital assets and as a decrease in current fund expenditures of the transferring department. Thus, total institutional expenditures are not inflated by the transactions. Examples are sales and services of service departments and central stores and transfers of material and equipment from one department to another. Any differences between the revenue from sales and services and the operating costs of service departments or central stores, whether debit or credit, are treated as Institutional Support expenditures. On the other hand, sales and services of an auxiliary enterprise to another department or auxiliary enterprise, or sales of materials produced by an instructional department to another department or auxiliary enterprise, would be reported as an expenditure of the department or auxiliary enterprise receiving the materials or services and as revenue of the department or auxiliary enterprise selling the materials or services.

Expenditures differ from transfers. Expenditures are the recognition of the expending of resources of the Current Funds group toward the objectives of each of the respective funds of that group. Transfers are amounts moved between fund groups to be used for the objectives of the recipient fund group. There are two types of transfers, mandatory and nonmandatory, which are fully described later in this chapter.

Expenditures and transfers may be classified in a variety of ways to serve a variety of purposes. Some of the factors bearing on the desired classification are:

1. The context in which appropriations, gifts, grants, and other sources of revenue are made to the institution.
2. The mode best suited for preparing and executing the budget.
3. The form that best serves the needs for financial reporting.
4. The presentation that will improve the quality of comparative studies among institutions.

Thus, expenditures and transfers may be classified in terms of programs, functions, organizational units, projects, and object classes.

Classifications by *program* often cut across organizational, functional, and even fund group lines and are useful in the planning processes. The *functional* classification pattern—educational and general, auxiliary enterprises, hospitals, independent operations, and their subcategories—provides the greatest comparability of data among institutions. The classification by *organizational units* provides data corresponding to channels of intra-institutional administrative responsibilities. Classification by *projects* serves to provide data corresponding to the pattern in which gifts, grants, and contracts are utilized by the institution. Classification by *object class*—that is, according to materials or capital assets purchased or services received, such as personal services, staff benefits, printing and stationery, travel, communica-

[1] The Cost Accounting Standards Board (CASB) has stipulated $500 and a useful life of more than two years as the threshold at which items must be considered capital assets, and OMB Circular A-21 (formerly FMC Circular 73-8) defines equipment as items having an acquisition cost of $500 or more and an expected service life of two years or more. Different limits which are reasonable and consistently applied are acceptable.

tions, food, fuel, utilities, repairs, equipment, and library books—serves internal management needs.

Published financial reports usually classify expenditures and transfers in terms of function, organizational unit, and object, in that order.

It is suggested that the following functional classification be followed:

- Educational and General
  - Expenditures
    - Instruction
    - Research
    - Public Service
    - Academic Support
    - Student Services
    - Institutional Support
    - Operation and Maintenance of Plant
    - Scholarships and Fellowships
  - Mandatory Transfers
  - Nonmandatory Transfers
- Auxiliary Enterprises
  - Expenditures
  - Mandatory Transfers
  - Nonmandatory Transfers
- Hospitals
  - Expenditures
  - Mandatory Transfers
  - Nonmandatory Transfers
- Independent Operations
  - Expenditures
  - Mandatory Transfers
  - Nonmandatory Transfers

Educational and General

Instruction. This category should include expenditures for all activities that are part of an institution's instruction program, with the exception of expenditures for remedial and tutorial instruction, which should be categorized as Student Services. Expenditures for credit and noncredit courses, for academic, occupational, and vocational instruction, and for regular, special, and extension sessions should be included.

Expenditures for departmental research and public service that are not separately budgeted should be included in this classification. This category excludes expenditures for academic administration when the primary assignment is administration—for example, academic deans. However, expenditures for department chairmen, in which instruction is still an important role of the administrator, are included in this category.

Research. This category should include all expenditures for activities specifically organized to produce research outcomes, whether commissioned by an agency external to the institution or separately budgeted by an organizational unit within the institution. Subject to these conditions, it includes expenditures for individual and/or project research as well as those of institutes and research centers. This category does not include all sponsored programs (training grants are an example) nor is it necessarily limited to sponsored research, since internally supported research programs, if separately budgeted, might be included in this category under the circumstances described above. Expenditures for departmental research that are separately budgeted specifically for research are included in this category.

Public Service. This category should include funds expended for activities that are established primarily to provide noninstructional services beneficial to individuals and groups external to the institution. These activities include community service programs (excluding instructional activities) and cooperative extension services. Included in this category are conferences, institutes, general advisory services, reference bureaus, radio and television, consulting, and similar noninstructional services to particular sectors of the community.

Academic Support. This category should include funds expended primarily to provide support services for the institution's primary missions—instruction, research, and public service. It includes (1) the retention, preservation, and display of educational materials—for example, libraries, museums, and galleries; (2) the provision of services that directly assist the academic functions of the institution, such as demonstration schools associated with a department, school, or college of education; (3) media, such as audiovisual services and technology such as computing support; (4) academic administration (including academic deans but not department chairmen) and personnel development providing administrative support and management direction to the three primary missions; and (5) separately budgeted support for course and curriculum development. For institutions that currently charge certain of the expenditures—for example, computing support—directly to the various operating units of the institution, such expenditures are not reflected in this category.

Student Services. This category should include funds expended for offices of admissions and registrar and those activities whose primary purpose is to contribute to the student's emotional and physical well-being and to his intellectual, cultural, and social development outside the context of the formal instruction program. It includes expenditures for student activities, cultural events, student newspapers, intramural athletics, student organizations, intercollegiate athletics (if the program is operated as an integral part of the department of physical education and not as an essentially self-supporting activity), supplemental educational services to provide matriculated students with supplemental instruction outside of the normal academic program (remedial instruction is an example), counseling and career guidance (excluding informal academic counseling by the faculty), student aid administration, and student health service (if not operated as an essentially self-supporting activity).

Institutional Support. This category should include expenditures for: (1) central executive-level activities concerned with management and long-range planning of the entire institution, such as the governing board, planning and programming, and legal services; (2) fiscal operations, including the investment office; (3) administrative data processing; (4) space management; (5) employee personnel and records; (6) logistical activities that provide procurement, storerooms, safety, security, printing, and transportation services to the institution; (7) support services to faculty and staff that are not operated as auxiliary enterprises; and (8) activities concerned with community and alumni relations, including development and fund raising.

Appropriate allocations of institutional support should be made to auxiliary enterprises, hospitals, and any other activities not reported under the Educational and General heading of expenditures.

Operation and Maintenance of Plant. This category should include all expenditures of current operating funds for the operation and maintenance of physical plant, in all cases net of amounts charged to auxiliary enterprises, hospitals, and independent operations. It does not include expenditures made from the institutional plant fund accounts. It includes all expenditures for operations established to provide services and maintenance related to grounds and facilities. Also included are utilities, fire protection, property insurance, and similar items.

Scholarships and Fellowships. This category should include expenditures for scholarships and fellowships in the form of outright grants to students selected by the institution and financed from current funds, restricted or unrestricted. It also should include trainee stipends, prizes, and awards, except trainee stipends awarded to individuals who are not enrolled in formal course work, which should be charged to instruction, research, or public service as appropriate. If the institution is given custody of the funds, but is not allowed to select the recipient of the grant—for example, the federal Basic Educational Opportunity Grants program or ROTC scholarships—the funds should be reported in the Agency Funds group rather than in the Current Funds group. The recipient of an outright grant is not required to perform service to the institution as consideration for the grant, nor is he expected to repay the amount of the grant to the funding source. When services are required in exchange for financial assistance, as in the federal College Work-Study Program, the charges should be classified as expenditures of the department or organizational unit to which the service is rendered. Aid to students in the form of tuition or fee remissions also should be included in this category. However, remissions of tuition or fees granted because of faculty or staff status, or family relationship of students to faculty or staff, should be recorded as staff benefit expenditures in the appropriate functional expenditure category.

Mandatory Transfers. This category should include transfers from the Current Funds group to other fund groups arising out of (1) binding legal agreements related to the financing of educational plant, such as amounts for debt retirement, interest, and required provisions for renewals and replacements of plant not financed from other sources and (2) grant agreements with agencies of the federal government, donors, and other organizations to match gifts and grants to loan and other funds. Mandatory transfers may be required to be made from either unrestricted or restricted current funds.

Nonmandatory Transfers. This category should include those transfers from the Current Funds group to other fund groups made at the discretion of the governing board to serve a variety of objectives, such as additions to loan funds, additions to quasi-endowment funds, general or specific plant additions, voluntary renewals and replacements of plant, and prepayments on debt principal. It also may include the retransfer of resources back to current funds.

Auxiliary Enterprises

An auxiliary enterprise is an entity that exists to furnish goods or services to students, faculty, or staff, and that charges a fee directly related to, although not necessarily equal to, the cost of the goods or services. The distinguishing characteristic of auxiliary enterprises is that they are managed as essentially self-supporting activities. Examples are residence halls, food services, intercollegiate athletics, (only if essentially self-supporting), college stores, faculty clubs, faculty and staff parking, and faculty housing. Student health services, when operated as an auxiliary enterprise, also should be included. The general public may be served incidentally by auxiliary enterprises. Hospitals, although they may serve students, faculty, or staff, are separately classified because of their relative financial significance.

This category includes all expenditures and transfers relating to the operation of auxiliary enterprises, including expenditures for operation and maintenance of plant and for institutional support; also included are other direct and indirect costs, whether charged directly as expenditures or allocated as a proportionate share of costs of other departments or units.

Expenditures. Expenditures of auxiliary enterprises are identified by using the same general criteria as for educational and general expenditures to distinguish them from transfers.

Mandatory Transfers. This type of transfer follows the same criteria of identification as for educational and general mandatory transfers to distinguish them from expenditures and nonmandatory transfers.

Nonmandatory Transfers. This type of transfer follows the same criteria of identification as for educational and general nonmandatory transfers in order to distinguish them from expenditures and mandatory transfers.

Hospitals

This category includes all expenditures and transfers associated with the patient care operations of the hospital, including nursing and other professional services, general services, administrative services, fiscal services, and charges for physical plant operations and institutional support. Also included are other direct and indirect costs, whether charged directly as expenditures or allocated as a proportionate share of costs of other departments or units. Expenditures for those activities which take place within the hospital, but which are categorized more appropriately as instruction or research, should be excluded from this category and accounted for in the appropriate categories.

Expenditures. The same criteria for identifying expenditures are used as in the case of educational and general expenditures to distinguish them from transfers.

Mandatory Transfers. The same criteria for identifying mandatory transfers are used as in the case of educational and general mandatory transfers to distinguish them from expenditures and nonmandatory transfers.

Nonmandatory Transfers. The same criteria for identifying nonmandatory transfers are used as in the case of educational and general nonmandatory transfers to distinguish them from expenditures and mandatory transfers.

Independent Operations

This category includes expenditures and transfers of those operations which are independent of, or unrelated to, but which may enhance the primary missions of the institution. This category generally is limited to expenditures associated with major federally funded research laboratories. This category excludes expenditures associated with property owned and managed as investments of the institution's endowment funds.

Expenditures. The same criteria for identifying expenditures are used as in the case of educational and general expenditures to distinguish them from transfers.

Mandatory Transfers. The same criteria for identifying mandatory transfers are used as in the case of educational and general mandatory transfers to distinguish them from expenditures and nonmandatory transfers.

Nonmandatory Transfers. The same criteria for identifying nonmandatory transfers are used as in the case of educational and general nonmandatory transfers to distinguish them from expenditures and mandatory transfers.

Deductions from Fund Balances

The term "deductions" is in contrast to expenditures and transfers. Deductions represent decreases in current fund balances, such as refunds to donors and grantors, and unencumbered or unexpended funds returned or returnable to the state treasury at fiscal year-end, depending on provisions of state statutes or appropriation acts.

Illustrative Exhibits

The figures used in the accompanying exhibits are illustrative only and are not intended to indicate any relationship among accounts. The summary of significant accounting policies and notes to financial statements relate to the illustrative statements. Modifications should be made thereto as appropriate to actual circumstances.

Exhibit 1

SAMPLE EDUCATIONAL INSTITUTION
Balance Sheet
June 30, 19__
with comparative figures at June 30, 19__

Assets	Current year	Prior year	Liabilities and Fund Balances	Current year	Prior year
Current funds:			Current funds:		
Unrestricted:			Unrestricted:		
Cash	$ 210,000	110,000	Accounts payable	$ 125,000	100,000
Investments	450,000	360,000	Accrued liabilities	20,000	15,000
Accounts receivable, less allowance of $18,000 both years	228,000	175,000	Students' deposits	30,000	35,000
Inventories, at lower of cost (first-in, first-out basis) or market	90,000	80,000	Due to other funds	158,000	120,000
Prepaid expenses and deferred charges	28,000	20,000	Deferred credits	30,000	20,000
			Fund balance	643,000	455,000
Total unrestricted	1,006,000	745,000	Total unrestricted	1,006,000	745,000
Restricted:			Restricted:		
Cash	145,000	101,000	Accounts payable	14,000	5,000
Investments	175,000	165,000	Fund balances	446,000	421,000
Accounts receivable, less allowance of $8,000 both years	68,000	160,000			
Unbilled charges	72,000	—			
Total restricted	460,000	426,000	Total restricted	460,000	426,000
Total current funds	1,466,000	1,171,000	Total current funds	1,466,000	1,171,000

Continued

SAMPLE EDUCATIONAL INSTITUTION
Balance Sheet, Continued

Assets, Continued	Current year	Prior year
Loan funds:		
Cash	$ 30,000	20,000
Investments	100,000	100,000
Loans to students, faculty, and staff, less allowance of $10,000 current year and $9,000 prior year	550,000	382,000
Due from unrestricted funds	3,000	—
Total loan funds	683,000	502,000
Endowment and similar funds:		
Cash	100,000	101,000
Investments	13,900,000	11,800,000
Total endowment and similar funds	14,000,000	11,901,000
Annuity and life income funds:		
Annuity funds:		
Cash	55,000	45,000
Investments	3,260,000	3,010,000
Total annuity funds	3,315,000	3,055,000
Life income funds:		
Cash	15,000	15,000
Investments	2,045,000	1,740,000
Total life income funds	2,060,000	1,755,000
Total annuity and life income funds	5,375,000	4,810,000

Liabilities and Fund Balances, Continued	Current year	Prior year
Loan funds:		
Fund balances:		
U.S. government grants refundable	$ 50,000	33,000
University funds:		
Restricted	483,000	369,000
Unrestricted	150,000	100,000
Total loan funds	683,000	502,000
Endowment and similar funds:		
Fund balances:		
Endowment	7,800,000	6,740,000
Term endowment	3,840,000	3,420,000
Quasi-endowment — unrestricted	1,000,000	800,000
Quasi-endowment — restricted	1,360,000	941,000
Total endowment and similar funds	14,000,000	11,901,000
Annuity and life income funds:		
Annuity funds:		
Annuities payable	2,150,000	2,300,000
Fund balances	1,165,000	755,000
Total annuity funds	3,315,000	3,055,000
Life income funds:		
Income payable	5,000	5,000
Fund balances	2,055,000	1,750,000
Total life income funds	2,060,000	1,755,000
Total annuity and life income funds	5,375,000	4,810,000

SAMPLE EDUCATIONAL INSTITUTION
Balance Sheet, continued

Plant funds:		
Unexpended:		
Cash	$ 275,000	410,000
Investments	1,285,000	1,590,000
Due from unrestricted current funds	150,000	120,000
Total unexpended	1,710,000	2,120,000
Renewals and replacements:		
Cash	5,000	4,000
Investments	150,000	286,000
Deposits with trustees	100,000	90,000
Due from unrestricted current funds	5,000	—
Total renewals and replacements	260,000	380,000
Retirement of indebtedness:		
Cash	50,000	40,000
Deposits with trustees	250,000	253,000
Total retirement of indebtedness	300,000	293,000

Plant funds:		
Unexpended:		
Accounts payable	10,000	—
Notes payable	100,000	—
Bonds payable	400,000	—
Fund balances:		
Restricted	1,000,000	1,860,000
Unrestricted	200,000	260,000
Total unexpended	1,710,000	2,120,000
Renewals and replacements:		
Fund balances:		
Restricted	25,000	180,000
Unrestricted	235,000	200,000
Total renewals and replacements	260,000	380,000
Retirement of indebtedness:		
Fund balances:		
Restricted	185,000	125,000
Unrestricted	115,000	168,000
Total retirement of indebtedness	300,000	293,000

Continued

SAMPLE EDUCATIONAL INSTITUTION

Balance Sheet, Continued

Assets, Continued	Current year	Prior year	Liabilities and Fund Balances, Continued	Current year	Prior year
Investment in plant:			Investment in plant:		
Land	500,000	500,000	Notes payable	790,000	810,000
Land improvements	1,000,000	1,110,000	Bonds payable	2,200,000	2,400,000
Buildings	25,000,000	24,060,000	Mortgages payable	400,000	200,000
Equipment	15,000,000	14,200,000	Net investment in plant	38,210,000	36,540,000
Library books	100,000	80,000			
Total investment in plant	41,600,000	39,950,000	Total investment in plant	41,600,000	39,950,000
Total plant funds	43,870,000	42,743,000	Total plant funds	43,870,000	42,743,000
Agency funds:			Agency funds:		
Cash	50,000	70,000	Deposits held in custody for others	110,000	90,000
Investments	60,000	20,000			
Total agency funds	110,000	90,000	Total agency funds	110,000	90,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements

Exhibit 2

SAMPLE EDUCATIONAL INSTITUTION

Statement of Changes in Fund Balances
Year Ended June 30, 19__

	Current Funds		Loan Funds	Endowment and Similar Funds	Annuity and Life Income Funds	Plant Funds			
	Unrestricted	Restricted				Unexpended	Renewal and Replacements	Retirement of Indebtedness	Investment in Plant
Revenues and other additions:									
Unrestricted current fund revenues	$7,540,000								
Expired term endowment—restricted						$50,000			
State appropriations—restricted						50,000			
Federal grants and contracts—restricted		$500,000							
Private gifts, grants, and contracts—restricted		370,000	$100,000	$1,500,000	$800,000	115,000		$65,000	$15,000
Investment income—restricted		224,000	12,000	10,000		$5,000	5,000	5,000	
Realized gains on investments—unrestricted				109,000					
Realized gains on investments—restricted			4,000	50,000		10,000	5,000	5,000	
Interest on loans receivable			7,000						
U.S. government advances			18,000						
Expended for plant facilities (including $100,000 charged to current funds expenditures)									1,550,000
Retirement of indebtedness									220,000
Accrued interest on sale of bonds								3,000	
Matured annuity and life income restricted to endowment				10,000					
Total revenues and other additions	7,540,000	1,094,000	141,000	1,679,000	800,000	230,000	10,000	78,000	1,785,000

Continued

SAMPLE EDUCATIONAL INSTITUTION

Statement of Changes in Fund Balances—continued

	Current Funds					Plant Funds			
	Unrestricted	Restricted	Loan Funds	Endowment and Similar Funds	Annuity and Life Income Funds	Unexpended	Renewal and Replacements	Retirement of Indebtedness	Investment in Plant
Expenditures and other deductions:									
Educational and general expenditures	4,400,000	1,014,000							
Auxiliary enterprises expenditures	1,830,000								
Indirect costs recovered		35,000							
Refunded to grantors		20,000	10,000						
Loan cancellations and write-offs			1,000						
Administrative and collection costs			1,000					1,000	
Adjustment of actuarial liability for annuities payable					75,000				
Expended for plant facilities (including noncapitalized expenditures of $50,000)						1,200,000	300,000		
Retirement of indebtedness								220,000	
Interest on indebtedness								190,000	
Disposal of plant facilities									115,000
Expired term endowments ($40,000 unrestricted, $50,000 restricted to plant)				90,000					
Matured annuity and life income funds restricted to endowment					10,000				
Total expenditures and other deductions	6,230,000	1,069,000	12,000	90,000	85,000	1,200,000	300,000	411,000	115,000
Transfers among funds—additions/(deductions):									
Mandatory:									

SAMPLE EDUCATIONAL INSTITUTION

Statement of Changes In Fund Balances—continued
Year Ended June 30, 19__

Principal and interest	(340,000)							340,000	
Renewals and replacements	(170,000)						170,000		
Loan fund matching grant	(2,000)		2,000						
Unrestricted gifts allocated	(650,000)		50,000	550,000		50,000			
Portion of unrestricted quasi-endowment funds investment gains appropriated	40,000			(40,000)					
Total transfers	(1,122,000)		52,000	510,000		50,000	170,000	340,000	
Net increase/(decrease) for the year	188,000	25,000	181,000	2,099,000	715,000	(920,000)	(120,000)	7,000	1,670,000
Fund balance at beginning of year	455,000	421,000	502,000	11,901,000	2,505,000	2,120,000	380,000	293,000	36,540,000
Fund balance at end of year	$643,000	$446,000	$683,000	$14,000,000	$3,220,000	$1,200,000	$260,000	$300,000	$38,210,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements

Continued

Exhibit 3

SAMPLE EDUCATIONAL INSTITUTION

Statement of Current Funds Revenues, Expenditures, and Other Changes
Year Ended June 30, 19__

	Current Year			Prior
	Unrestricted	Restricted	Total	Year Total
Revenues:				
Tuition and fees	$2,600,000		2,600,000	2,300,000
Federal appropriations	500,000		500,000	500,000
State appropriations	700,000		700,000	700,000
Local appropriations	100,000		100,000	100,000
Federal grants and contracts	20,000	375,000	395,000	350,000
State grants and contracts	10,000	25,000	35,000	200,000
Local grants and contracts	5,000	25,000	30,000	45,000
Private gifts, grants, and contracts	850,000	380,000	1,230,000	1,190,000
Endowment income	325,000	209,000	534,000	500,000
Sales and services of educational departments	190,000		190,000	195,000
Sales and services of auxiliary enterprises	2,200,000		2,200,000	2,100,000
Expired term endowment	40,000		40,000	
Other sources (if any)				
Total current revenues	7,540,000	1,014,000	8,554,000	8,180,000
Expenditures and mandatory transfers:				
Educational and general:				
Instruction	2,960,000	489,000	3,449,000	3,300,000
Research	100,000	400,000	500,000	650,000
Public service	130,000	25,000	155,000	175,000
Academic support	250,000		250,000	225,000
Student services	200,000		200,000	195,000
Institutional support	450,000		450,000	445,000

SAMPLE EDUCATIONAL INSTITUTION

Statement of Current Funds Revenues, Expenditures, and Other Changes—Continued

	Current Year			Prior
	Unrestricted	Restricted	Total	Year Total
Operation and maintenance of plant	220,000		220,000	200,000
Scholarships and fellowships	90,000	100,000	190,000	180,000
Educational and general expenditures	4,400,000	1,014,000	5,414,000	5,370,000
Mandatory transfers for:				
Principal and interest	90,000		90,000	50,000
Renewals and replacements	100,000		100,000	80,000
Loan fund matching grant	2,000		2,000	
Total educational and general	4,592,000	1,014,000	5,606,000	5,500,000
Auxiliary enterprises:				
Expenditures	1,830,000		1,830,000	1,730,000
Mandatory transfers for:				
Principal and interest	250,000		250,000	250,000
Renewals and replacements	70,000		70,000	70,000
Total auxiliary enterprises	2,150,000		2,150,000	2,050,000
Total expenditures and mandatory transfers	6,742,000	1,014,000	7,756,000	7,550,000
Other transfers and additions/(deductions):				
Excess of restricted receipts over transfers to revenues		45,000	45,000	40,000
Refunded to grantors		(20,000)	(20,000)	
Unrestricted gifts allocated to other funds	(650,000)		(650,000)	(510,000)
Portion of quasi-endowment gains appropriated	40,000		40,000	
Net increase in fund balances	188,000	25,000	213,000	160,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements

Continued

Sample Educational Institution

Summary of Significant Accounting Policies

June 30, 19__

The significant accounting policies followed by Sample Educational Institution are described below to enhance the usefulness of the financial statements to the reader.

Accrual Basis

The financial statements of Sample Educational Institution have been prepared on the accrual basis except for depreciation accounting as explained in notes 1 and 2 to the financial statements. The statement of current funds revenues, expenditures, and other changes is a statement of financial activities of current funds related to the current reporting period. It does not purport to present the results of operations or the net income or loss for the period as would a statement of income or a statement of revenues and expenses.

To the extent that current funds are used to finance plant assets, the amounts so provided are accounted for as (1) expenditures, in the case of normal replacement of movable equipment and library books; (2) mandatory transfers, in the case of required provisions for debt amortization and interest and equipment renewal and replacement; and (3) transfers of a nonmandatory nature for all other cases.

Fund Accounting

In order to ensure observance of limitations and restrictions placed on the use of the resources available to the Institution, the accounts of the Institution are maintained in accordance with the principles of "fund accounting." This is the procedure by which resources for various purposes are classified for accounting and reporting purposes into funds that are in accordance with activities or objectives specified. Separate accounts are maintained for each fund; however, in the accompanying financial statements, funds that have similar characteristics have been combined into fund groups. Accordingly, all financial transactions have been recorded and reported by fund group.

Within each fund group, fund balances restricted by outside sources are so indicated and are distinguished from unrestricted funds allocated to specific purposes by action of the governing board. Externally restricted funds may only be utilized in accordance with the purposes established by the source of such funds and are in contrast with unrestricted funds over which the governing board retains full control to use in achieving any of its institutional purposes.

Endowment funds are subject to the restrictions of gift instruments requiring in perpetuity that the principal be invested and the income only be utilized. Term endowment funds are similar to endowment funds except that upon the passage of a stated period of time or the occurrence of a particular event, all or part of the principal may be expended. While quasi-endowment funds have been established by the governing board for the same purposes as endowment funds, any portion of quasi-endowment funds may be expended.

All gains and losses arising from the sale, collection, or other disposition of investments and other noncash assets are accounted for in the fund which owned such assets. Ordinary income derived from investments, receivables, and the like is accounted for in the fund owning such assets, except for income derived from investments of endowment and similar funds, which income is accounted for in the fund to which it is restricted or, if unrestricted, as revenues in unrestricted current funds.

All other unrestricted revenue is accounted for in the unrestricted current fund. Restricted gifts, grants, appropriations, endowment income, and other restricted resources are accounted for in the appropriate restricted funds. Restricted current funds are reported as revenues and expenditures when expended for current operating purposes.

Other Significant Accounting Policies

Other significant accounting policies are set forth in the financial statements and the notes thereto.

Sample Educational Institution

Notes to Financial Statements

June 30, 19__

1. Investments exclusive of physical plant are recorded at cost; investments received by gift are carried at market value at the date of acquisition. Quoted market values of investments (all marketable securities) of the funds indicated were as follows:

	Current year	*Prior year*
Unrestricted current funds	$ 510,000	$ 390,000
Restricted current funds	180,000	165,000
Loan funds	105,000	105,000
Unexpended plant funds	1,287,000	1,600,000
Renewal and replacement funds	145,000	285,000
Agency funds	60,000	20,000

Investments of endowment and similar funds and annuity and life income funds are composed of the following:

	Carrying value	
	Current year	*Prior year*
Endowment and similar funds:		
Corporate stocks and bonds (approximate market, current year $15,000,000, prior year $10,900,000)	$13,000,000	$10,901,000
Rental properties—less accumulated depreciation, current year $500,000, prior year $400,000	900,000	899,000
	13,900,000	11,800,000
Annuity funds:		
U.S. bonds (approximate market, current year $200,000, prior year $100,000)	$ 200,000	$ 110,000
Corporate stocks and bonds (approximate market, current year $3,070,000, prior year $2,905,000)	3,060,000	2,900,000
	3,260,000	3,010,000
Life income funds:		
Municipal bonds (approximate market, current year $1,400,000, prior year $1,340,000)	$ 1,500,000	$ 1,300,000

Corporate stocks and bonds (approximate market, current year $650,000, prior year $400,000)	545,000	440,000
	2,045,000	1,740,000

Assets of endowment funds, except nonmarketable investments of term endowment having a book value of $200,000 and quasi-endowment having a book value of $800,000, are pooled on a market value basis, with each individual fund subscribing to or disposing of units on the basis of the value per unit at market value at the beginning of the calendar quarter within which the transaction takes place. Of the total units, each having a market value of $15.00, 600,000 units were owned by endowment, 280,000 units by term endowment, and 120,000 units by quasi-endowment at June 30, 19__.

The following tabulation summarizes changes in relationships between cost and market values of the pooled assets:

	Pooled Assets			
	Market	*Cost*	*Net Gains (Losses)*	*Market Value per Unit*
End of year	$15,000,000	$13,000,000	$2,000,000	$15.00
Beginning of year	10,900,000	10,901,000	(1,000)	12.70
Unrealized net gains for year			2,001,000	
Realized net gains for year			159,000	
Total net gains for year			2,160,000	2.30

The average annual earnings per unit, exclusive of net gains, were $.56 for the year.

2. Physical plant and equipment are stated at cost at date of acquisition or fair value at date of donation in the case of gifts, except land acquired prior to 1940, which is valued at appraisal value in 1940 at $300,000. Depreciation on physical plant and equipment is not recorded.

3. Long-term debt includes: bonds payable due in annual installments varying from $45,000 to $55,000 with interest at 5 7/8%, the final installment being due in 19__, collateralized by trust indenture covering land, buildings, and equipment known as Smith dormitory carried in the accounts at $2,500,000, and pledged net revenue from the operations of said dormitory; and mortgages payable due in varying amounts to 19__ with interest at 6%, collateralized by property carried in the accounts at $800,000 and pledged revenue of the Student Union amounting to approximately $65,000 per year.*

4. [Pension note deleted—See FASB Statement No. 87, *Employers' Accounting for Pensions* or GASB Statement No. 5, *Disclosure of Pension Infor-*

* FASB Statement No. 47, *Disclosure of Long-Term Obligations,* also requires disclosure of maturities of long-term obligations for each of the five years following the balance sheet date.

mation by Public Employee Retirement Systems and State and Local Governmental Employers, for current disclosure requirements.]

5. Contracts have been let for the construction of additional classroom buildings in the amount of $3,000,000. Construction and equipment are estimated to aggregate $5,000,000, which will be financed by available resources and an issue of bonds payable over a period of 40 years amounting to $4,000,000.

6. All interfund borrowings have been made from unrestricted funds. The amounts due to plant funds from current unrestricted funds are payable within one year without interest. The amount due to loan funds from current unrestricted funds is payable currently.

7. Pledges totaling $260,000, restricted to plant fund uses, are due to be collected over the next three fiscal years in the amounts of $120,000, $80,000, and $60,000, respectively. It is not practicable to estimate the net realizable value of such pledges.

Chart of Accounts

A systematic classification of accounts is an essential part of an accounting system. The accounts should be developed to be compatible with the organizational structure of the institution, and their form and content should be arranged in agreement with the financial reports to be presented.

The arrangement should be formalized in a chart of accounts, and, for ease of identification and reference, each account should be assigned an appropriate code number or symbol. Classification should be according to the funds and fund groups of the institution, as described in the preceding chapters of Part 5. Within each fund group, the accounts should be listed according to assets, liabilities, and fund balance accounts.

The illustrative chart of accounts for a college or university presented below shows those accounts usually found in the general ledger or carried in subsidiary ledgers with appropriate control accounts in the general ledger. This chart is presented as a guide for institutions in developing their own detailed charts of accounts and to help them set up their accounts in conformity with the principles of accounting and reporting presented in the preceding chapters of Part 5. The system of accounts may be expanded, contracted, or modified to meet the needs of the individual institution and to conform to its organizational structure, but in any case it should incorporate the basic elements common to all educational institutions.

In designing or revising a chart of accounts, the code numbers or symbols assigned to the accounts should progress in a logical order. Because each fund and fund group is carried in the accounting records as a separately balanced group, the accounts in any given group should be assigned a code number that, perhaps by a prefix, identifies that fund group—for example, all accounts related to current funds should be identifiable as such; all accounts for plant funds should be identifiable as such. Similarly, within the fund groups, consistent code numbers should identify subgroups, assets, liabilities, and fund balances. For revenue accounts, code numbers or symbols can be used to identify sources. For expenditure accounts, code numbers or symbols can be used to identify functions, organizational units, projects, programs, and objects of expenditures. The individual fund identity should be an integral part of the fund balance, revenue, and expenditure account codes.

In developing a chart of accounts, it is important to exercise economy in the use of digits and characters for code numbers, to plan a logical arrangement for the chart, and to make ample provision for future expansion of account numbers.

Reprinted from *College and University Business Administration*, second revised edition (1974), by permission of the National Association of College and University Business Officers.

General Ledger Accounts

Current Funds—Unrestricted

Asset Accounts

Cash

Petty Cash

Investments

Accounts Receivable—*detailed as needed, for example:*

Students

Hospital Patients

Governmental

Unbilled Charges

Notes Receivable—*detailed as needed*

Allowance for Doubtful Accounts and Notes—*credit balance account associated with each type of receivable*

Inventories—*detailed as needed, for example:*

College Store

Dining Halls

Central Stores

Plant Operation and Maintenance Supply Store

Prepaid Items and Deferred Charges—*detailed as needed*

Due from Other Fund Groups

Liability and Fund Balance Accounts

Notes Payable

Accounts Payable and Accrued Expenses—*detailed as needed*

Deferred Credits

Deposits

Due to Other Fund Groups

Fund Balances—Allocated—*detailed as needed, for example:*

Auxiliary Enterprises

Reserve for Encumbrances

Reserve for Computer Use Survey

Reserve for Faculty Self-Improvement Program

Fund Balance—Unallocated

Operating Accounts. The following control accounts in the general ledger for actual revenues, expenditures, and other changes are supported in detail by Current Funds Revenues and Current Funds Expenditures and Other Changes accounts in subsidiary ledgers. If desired, several control accounts may be provided in lieu of single control accounts:

Revenues Control—*credit account*

Expenditures and Other Changes Control—*debit account*

When budgetary accounts are carried in the general ledger, the following control accounts would appear in the chart of accounts. They are supported in detail by Current Funds Revenues and Current Funds Expenditures and Other Changes accounts in subsidiary ledgers:

Estimated Revenues *or* Unrealized Revenues

Expenditures and Other Changes Allocations or Budget Allocations for Expenditures and Other Changes

Unallocated Budget Balance or Unassigned Budget Balance

Current Funds—Restricted

These accounts are to be used if the assets and liabilities of such funds are separated from those of Unrestricted Current Funds.

Asset Accounts

Cash

Investments

Accounts Receivable—*detailed as needed, for example:*

Governmental

Other

Unbilled Charges

Allowance for Doubtful Accounts—*credit balance account*

Due from Other Fund Groups

Liability and Fund Balance Accounts

Accounts Payable

Due to Other Fund Groups

Fund Balances—Allocated—*detailed as needed, for example:*

Reserve for Encumbrances

Auxiliary Enterprises

Fund Balances—Unallocated

Both of the fund balance accounts may be control accounts supported by separate subsidiary ledger accounts for each restricted current fund and for each type of fund balance. Additional control accounts may be provided as required or desired.

Operating Accounts. Expenditures of restricted current funds may be recorded in the operating accounts of unrestricted current funds, in which case transfers of restricted current funds to current funds revenues accounts would be made to finance such expenditures. When this is not done, operating accounts for each current restricted fund must provide for proper classification of expenditures by object, as well as providing for appropriate categorization of sources of additions, deductions other than expenditures, and transfers to and from other funds.

Loan Funds

Asset Accounts

Cash

Investments

Notes Receivable from Students, Faculty, and Staff

Allowance for Doubtful Loans—*credit balance account*

Liability and Fund Balance Accounts

Accounts Payable to Collection Agencies

Due to Other Fund Groups

Refunds Payable on Refundable Government Grants

Fund Balances—This may be a control account supported by separate subsidiary ledger accounts for each fund. Separate accounts should be carried to identify the sources of funds available for loans, such as donor- and government-restricted loan funds, including funds provided by mandatory transfers required for matching purposes, unrestricted funds designated as loan funds, and funds returnable to the donor under certain conditions. Accounts to identify allocations of fund balances should be provided. Accounts may be maintained to identify resources available for loans to students separately from those for faculty and staff.

Endowment and Similar Funds

Asset Accounts

Cash

Accounts Receivable

Notes Receivable

Allowance for Doubtful Accounts and Notes—*credit balance account*

Prepaid Items

Investments—*detailed as needed, for example*:

Bonds

Allowance for Unamortized Bond Premiums

Allowance for Unamortized Bond Discounts

Preferred Stocks

Common Stocks

Mortgage Notes

Real Estate

Allowance for Depreciation—*credit balance account*

Due from Other Fund Groups

Liability and Fund Balance Accounts

The fund balance accounts should be classified as to Endowment, Term Endowment, and Quasi-Endowment Funds, even though the investments of the funds may be merged in one or more investment pools.

Payables—*detailed as needed, for example*:

Mortgages Payable

Notes Payable

Accounts Payable

Collateral Due on Securities Loaned

Due to Other Fund Groups

Balances of Endowment Funds

Balances of Term Endowment Funds

Balances of Quasi-Endowment Funds—Unrestricted

Balances of Quasi-Endowment Funds—Restricted

In order to differentiate between the balances of funds for which the income is unrestricted and those for which the income is restricted, the following accounts may be employed:

Balances of Endowment Funds—Unrestricted

Balances of Endowment Funds—Restricted—*detailed as needed, for example:*

Professorships

Instructional Departments

Scholarships

Library

Loan Funds

Note. The balances of term endowment funds also may be identified in this manner.

Undistributed Gains and Losses on Investment Transactions—*Separate accounts should be established for each investment pool.*

Undistributed Share Adjustments—*Separate accounts should be established for each investment pool.*

Annuity and Life Income Funds

If the funds in this section are pooled for investment purposes, accounts for the assets may be classified as shown below for each investment pool. If any funds are separately invested, accounts should be set up for the investment of such funds.

Asset Accounts

Cash

Accounts Receivable

Notes Receivable

Allowance for Doubtful Accounts and Notes—*credit balance account*

Investments—*detailed as needed, for example:*

Bonds

Allowance for Unamortized Bond Premiums

Allowance for Unamortized Bond Discounts

Preferred Stocks

Common Stocks

Mortgage Notes

Real Estate

Allowance for Depreciation—*credit balance account*

Due from Other Fund Groups

Liability and Fund Balance Accounts

Accounts Payable

Annuity Payments Currently Due

Annuities Payable

Life Income Payments Currently Due

Due to Other Funds for Advances on Annuity Payments

Due to Other Funds for Advances to Income Beneficiaries

Undistributed Income—Annuity Funds

Undistributed Income—Life Income Funds

Balances of Annuity Funds

Balances of Life Income Funds

These may be control accounts supported by subsidiary ledger accounts for each fund. Within the two categories the accounts may be listed alphabetically by name, or they may be classified in any other manner at the discretion of the institution.

Undistributed Gains and Losses on Investment Transactions—*Separate accounts should be established for each investment pool.*

Undistributed Share Adjustments—*Separate accounts should be established for each investment pool.*

Income, Expenditure, and Transfer Accounts

Income from Investments—*credit account, detailed by each agreement*

Expenditures and Transfers—*debit account, detailed by each agreement*

Plant Funds—Unexpended

Asset Accounts

Cash

Investments

Receivables—*detailed as needed*

Allowance for Doubtful Accounts—*credit balance account*

Due from Other Fund Groups

Construction in Progress—*alternatively can be shown in Investment in Plant subgroup of Plant Funds*

Liability and Fund Balance Accounts

Accounts Payable

Notes Payable

Bonds Payable

Mortgages Payable

Due to Other Fund Groups

Fund Balances—*This may be a control account supported by subsidiary ledger accounts which should differentiate between unrestricted and restricted funds.*

Plant Funds—Funds for Renewals and Replacements

These accounts should be used if the assets of such funds are separated from the assets of other subgroups of Plant Funds.

Asset Accounts

Cash

Accounts Receivable

Allowance for Doubtful Accounts—*credit balance account*

Investments

Deposits with Trustees

Due from Other Fund Groups

Liability and Fund Balance Accounts

Accounts Payable

Due to Other Fund Groups

Fund Balances—*This may be a control account supported by subsidiary ledger accounts which should differentiate between unrestricted and restricted funds.*

Plant Funds—Funds for Retirement of Indebtedness

These accounts should be used if the assets of such funds are separated from the assets of other subgroups of Plant Funds.

Asset Accounts

Cash

Accounts and Notes Receivable

Allowance for Doubtful Accounts—*credit balance account*

Investments

Deposits with Trustees

Due from Other Fund Groups

Liability and Fund Balance Accounts

Accounts Payable

Due to Other Fund Groups

Fund Balances—*This may be a control account supported by subsidiary ledger accounts which should differentiate between unrestricted and restricted funds.*

Plant Funds—Investment in Plant

Asset Accounts

Land

Buildings

Allowance for Depreciation—*credit balance account*

Improvements Other than Buildings

Allowance for Depreciation—*credit balance account*

Equipment

Allowance for Depreciation—*credit balance account*

Library Books

Art Museums and Collections

Construction in Progress—*alternatively can be shown in the Unexpended Plant Funds subgroup of Plant Funds*

Liability and Fund Balance Accounts

Accounts Payable

Notes Payable

Bonds Payable

Mortgages Payable

Leaseholds Payable

Due to Other Fund Groups

Net Investment in Plant—*detailed as needed*

Agency Funds

Asset Accounts

Cash

Accounts Receivable

Notes Receivable

Allowance for Doubtful Accounts and Notes—*credit balance account*

Investments

Due from Other Fund Groups

Liability Accounts

Accounts Payable

Due to Other Fund Groups

Deposit Liabilities—*Accounts for each agency fund should be carried either in the general ledger or in subsidiary ledgers.*

Current Funds Revenues Accounts

(Separate Restricted and Unrestricted Accounts)

Tuition and Fees—*detailed as needed*

Federal Appropriations

State Appropriations

Local Appropriations

Federal Grants and Contracts

State Grants and Contracts

Local Grants and Contracts

Private Gifts, Grants, and Contracts—*detailed as needed*

Endowment Income—*detailed as needed, for example:*

Income from Funds Held by Others Under Irrevocable Trusts

Sales and Services of Educational Activities—*detailed as needed, for example:*

Film Rentals

Testing Services

Home Economics Cafeteria

Demonstration Schools

Dairy Creameries

Food Technology Divisions

Sales and Services of Auxiliary Enterprises—*detailed as needed, for example:*

Residence Halls

Faculty Housing

Food Services

College Union

Additional revenue accounts may be established for sources of sales, types of products and services, and cash and interdepartmental sales.

Sales and Services of Hospitals—*detailed as needed, for example:*

Daily Patient Services

Nursing Services

Other Professional Services

Health Clinics *if an integral part of the hospital*

Other Sources—*detailed as needed*

Independent Operations—*detailed as needed by organization units*

Current Funds Expenditures and Transfers Accounts

Current funds expenditures accounts should bear identifying codes and symbols that will identify functions, such as Instruction, Institutional Support, and Scholarships and Fellowships; identify organizational units, such as Department of Physics, Controller's Office, and Registrar's Office; and identify the object of expenditures, such as Personnel Compensation, Supplies and Expenses, and Capital Expenditures. If desired, interdepartmental purchases, as contrasted with purchases from external sources, also may be identified by code or symbol. The object coding and symbols should be designed to provide for common usage of the objects throughout the entire chart of accounts, although, of course, there will be individual object codings that will be used only for particular functional categories.

Educational and General

Instruction

Accounts by divisions, schools, colleges, and departments of instruction following the administrative organization of the institution. The four functional subcategories are:

General academic instruction

Occupational and vocational instruction

Special session instruction

Community education

Research

Accounts by individual projects, classified by organizational units. The two functional subcategories are:

Institutes and research centers

Individual or project research

Public Service

Accounts by activities, classified by type of activity, such as:

Community Service

Conferences and Institutes

Cooperative Extension Service

Public Lectures

Radio

Television

Academic Support

Accounts by activities, classified by type of activity, such as:

Academic Administration and Personnel Development

Audiovisual Services

Computing Support *(excluding administrative data processing), unless distributed to using activities*

Course and Curriculum Development

Demonstration Schools

Libraries

Museums and Galleries

Student Services

Accounts by activities, classified by type of activity, such as:

Admissions Office

Counseling and Career Guidance

Cultural Events

Dean of Students

Financial Aid Administration

Health and Infirmary Services *if not an integral part of a hospital nor operated as an essentially self-supporting operation*

Intramural Athletics

Intercollegiate Athletics *if operated as an integral part of department of physical education and not essentially self-supporting*

Registrar

Student Organizations

Remedial Instruction

Institutional Support—*detailed as needed, for example:*

Governing Board

Chief Executive Office

Chief Academic Office

Chief Business Office

Investment Office

Legal Counsel

Administrative Data Processing

Alumni Office

Auditing, internal and external

Safety

Security

Catalogues and Bulletins

Commencements

Convocations

Development Office

Employee Personnel and Records

Fund Raising

General Insurance *other than Property Insurance*

Interest on Current Funds Loans

Legal Fees

Memberships

Printing

Provision for Doubtful Accounts and Notes

Publications

Public Relations

Purchasing

Service Departments

There should be interim accounts for all organizational units classified in this category; these accounts should be closed out at the end of each fiscal year.

Space Management

Telephone and Telegraph, *unless charged to departmental budgets*

Transportation *including motor pool, unless operated as a service department*

Operation and Maintenance of Plant

Accounts for all organizational units and functions, such as:

Administration

Custodial Services

Maintenance of Buildings

Maintenance of Grounds

Utilities

Trucking Services

Fire Protection

Property Insurance

Scholarships and Fellowships

Accounts as needed and desired for scholarships, fellowships, grants-in-aid, trainee stipends, prizes, and awards.

Tuition and Fee Remissions, *unless properly classified as staff benefit expenditures*

Accounts may be set up for instructional divisions and departments, such as:

School of Medicine

Department of Physics

Mandatory Transfers, Educational and General—*detailed to show subcategories, such as:*

Provision for Debt Service on Educational Plant

Loan Fund Matching Grants

Nonmandatory Transfers, Educational and General *(to and from)—detailed to show significant subcategories, such as:*

Loan Funds

Quasi-Endowment Funds

Appreciation on Securities of Endowment and Similar Funds

Plant Funds

Renewals and Replacements of Plant Assets

Additions to Plant Assets

Voluntary Payments on Debt Principal

Auxiliary Enterprises, Hospitals, and Independent Operations

Auxiliary Enterprises

Accounts as needed and desired for such enterprises as included in the Current Funds Revenues accounts.

Provision should be made for identification of mandatory and nonmandatory transfers—to and from—by significant subcategories.

Hospitals

Accounts as needed and desired. Provision should be made for identification of mandatory and nonmandatory transfers—to and from—by significant subcategories.

Independent Operations

Accounts as needed and desired for organizational units.

Provision should be made for identification of mandatory and nonmandatory transfers—to and from—by significant subcategories.

Classification of Expenditures by Object

The object classification of expenditures identifies that which is received in return for the expenditures. Object classification has importance as a tool for internal management, but should be considered complementary to the classification of expenditures by function and organizational unit and should not replace these classifications in the various schedules of current funds expenditures. The value of object classification will depend on the usefulness of the information it provides to management. The classifications may be omitted from published financial reports or they may be used to any degree considered desirable by the institution. The use of object classifications and the related identifying codes and symbols should not be carried to an extreme; the number of categories should be limited to those that will be of significant value to management.

Three major object classifications are found in most colleges and universities: Personnel Compensation, Supplies and Expenses, and Capital Expenditures. Breakdowns of objects within these major categories may be necessary or desirable in some situations.

Personnel Compensation

This classification includes salaries, wages, and staff benefits. In the various salary and wage expense accounts, it may be desirable to distinguish between groups of faculty and other staff members, such as full-time and part-time personnel; student and nonstudent workers; and professional, secretarial, clerical, skilled, and nonskilled employees. Appropriate code numbers and symbols within this category will aid in identifying, collecting, and summarizing information.

Supplies and Expenses

Because of their general significance to nearly all organizational units within an institution, it may be beneficial to identify significant categories of these expenditures, such as supplies, telephone, travel, and contractual services.

Capital Expenditures

The following object categories within this classification (which includes both additions to and renewals and replacements of capital assets) may prove helpful in the accounting and reporting systems of educational institutions: scientific equipment, laboratory apparatus, office machines and equipment, library books, furniture and furnishings, motor vehicles, machinery and tools, building remodeling, minor construction, and livestock.

Appendix B

Schedule of Changes Made to Audits of Colleges and Universities

Reference	Change	Date
General	The term "examination" has been changed to "audit" to conform to the terminology used in SAS No. 58.	October, 1990
General	The terminology used to refer to "internal controls" has been changed to "internal control structure" to conform to SAS No. 55.	October, 1990
Paragraph 1.02	References to the Financial Accounting Standards Board and Governmental Accounting Standards Board added.	October, 1990
Paragraph 1.06	Reference to FASB Statement No. 93 added.	October, 1990
Paragraph 1.07	Paragraph added to make reference to GASB Statement No. 8.	December, 1991
Paragraph 1.21	Reference to Governmental Accounting Standards Board added.	December, 1991
Paragraph 2.04	Reference to reporting guidance based on SAS No. 1 replaced with references to SAS Nos. 58 and 62.	October, 1990
Paragraph 2.22	Reference to FASB Statement No. 93 added.	October, 1990
Paragraph 2.23	Paragraph added to make reference to GASB Statement No. 8.	December, 1991
Paragraphs 5.01—5.20	Paragraphs deleted.	April, 1992
Paragraphs 6.01—6.22	Paragraphs deleted.	April, 1992
Paragraph 7.06	Reference to the Department of Health, Education and Welfare changed to the Department of Education.	April, 1992
Paragraph 8.14	Reference to FASB study of total return concept as part of project on accounting for marketable securities deleted.	October, 1990
Paragraph 11.02	Footnote reference to FASB Statement No. 95 added.	October, 1990
Paragraph 11.02 (Footnote *)	Footnote reference updated.	December, 1991
Paragraph 11.11	Reference to SAS No. 1, section 546 changed to SAS No. 58.	October, 1990
Paragraphs 11.14—11.19	Illustrative financial statements deleted.	April, 1992

Reference	Change	Date
Chapter 12	References and illustrative reports conformed to SAS Nos. 58 and 62; Opinions and Compliance Reporting on Material Defense Student Loan Funds and College Work—Study Programs replaced with reference to U.S. Department of Education Student Financial Assistance Programs Audit Guide.	October, 1990
Appendix A	Footnote updated.	October, 1990
Appendix A	Notice to Readers revised to reflect SAS No. 69.	April, 1992
Appendix A	Notes to financial statements updated to: add footnote reference to FASB Statement No. 47 to note 3 (long-term debt); delete note 4 (pension plans) and add references to FASB Statement No. 87 and GASB Statement No. 5.	May, 1992

In addition to the above, notes have been added to highlight areas that will be updated in future editions. Those areas include:

Chapter 12, *Reports of Independent Auditors,* outdated material on auditing federally funded student financial assistance programs deleted from this edition of the guide, will be replaced by materials that conform to current pronouncements and regulations.

013321