

DEBT PARTICULARS

LEASES:

Lease-purchase agreements may be in the form of capital or operating leases. A capital lease is, for the most part, viewed as an installment purchase of property rather than the rental of property. An operating lease does not involve the purchase of property and payments represent the rental expenditures. Capital leases exist if ANY of the following conditions are met.

- (a) The lease transfers ownership of the property to the lessee by the end of the lease term.
- (b) The lease contains a bargain purchase option.
- (c) The lease term is equal to 75% or more of the estimated economic life of the leased property.
- (d) The sum of the principal lease payments equal 90% of the fair value of the asset.

Once it has been determined that a capital lease exists, then the following entries would be required for those capital leases that exceed the capitalization policy:

- | | | | |
|----|-----------------------------------------|----|----|
| 1. | Equipment (Account No. 90 204) | xx | |
| | Net Assets Invested in Capital (90 706) | | xx |

To capitalize the present value of the minimum lease payments in the General Capital Asset Accounts.

- | | | | |
|----|---------------------------------------|----|----|
| 2. | Expenditure- (Applicable Department) | xx | |
| | Other Financing Source (Account 5124) | | xx |
| | Cash - Down payment if applicable | | xx |

At the start of the lease, the present value of the minimum lease payments must be recognized as an expenditure against the budget and as an other financing source. The expenditure category used should relate to the type of asset acquired. (typically recorded in the CO Fund)

- | | | | |
|----|-------------------------------------------|----|----|
| 3. | Net Assets Invested in Capital (00 706) | xx | |
| | Other Long-Term Debt (Account No. 00 509) | | xx |

This entry is necessary to recognize the liability in the General Long-Term Liability Accounts. The amount capitalized should be the present value of the minimum lease payments.

4.	Expenditure	xx
	Cash	xx

To record the periodic payments in future periods. The expenditure account to recognize these payments to service the debt should be account "5000 Debt Services", more than likely from the CO Fund.

If the lease is an operating lease, the lease would be recorded as follows:

Expenditures - Rent	xx
Cash (Vouchers Payable)	xx

To record the operating lease at the inception of the lease. This would be coded to the respective function that correlates to the type of item purchased.

The preceding reflects the standard approach in accounting for leases. There are many different types of leases out there, so consideration should be given for unique applications that may apply. GASB 62 , para 213

GENERAL LONG-TERM LIABILITIES

Fund 00 serves the purpose of keeping track of how much each district owes. It is only used to keep track of governmental debt.....which is almost the only type of debt a school district has. Districts should periodically update Fund 00 so that it will have the proper balances at yearend.

I would like to see districts phase out of using the offset accounts.....Amount to be Provided (302) and Amount Available(303). Instead, I believe districts would be better served by using the accounts from the statement of net assets such as Net Assets Invested in Capital (706) and Net Assets Unrestricted (708). To identify with the proper offset account, each liability should be assessed as to whether it is "capital" related or not. A sample trial balance of fund 00 is as follows:

706 Net Assets Invested in Capital	2,330,000
708 Net Assets Unrestricted	130,000
501 Bonds Payable	1,000,000
50201 CO Certificate Payable – H.S.	500,000
50202 CO Certificate Payable – Elementary	800,000
504 Compensated Absences	50,000
505 Early Retirement Benefits Payable	60,000
506 Net OPEB Obligation	20,000
509 Other Long-term Debt Payable (capital leases)	30,000

STATEMENT OF NET ASSETS – LONG TERM DEBT

Long-term debt on the statement of net assets is aggregated into the following two lines:

- A. Due Within One Year
- B. Due in More than One Year

Bond issues, capital outlay certificates and copy machine installment payments are fairly easy to report on the preceding two accounts. Just take the payments that will be made in the subsequent year and report on the Due within One Year line.....and all subsequent payments will be lumped on the Due in More than One Year line. The interest portion of payments is not recorded as a liability.

Since OPEB liabilities relate primarily to healthcare payments of active employees in their retirement years, the entire amount of the OPEB liability may be recorded on the Due in More than One Year line.

The recording of early retirement liabilities will depend on the district's policy. Some are single pay in the next school year (Due Within One Year), while others pay in installments over a number of years.....(reported on both the One Year and More than One Year lines). A spreadsheet that plots the payments will be beneficial in many cases.

Since each entity adopts their own policies for compensated absences, a.k.a. accrued leave, a.k.a. vacation and sick leave, the reporting of these balances will vary depending on the details of a given entity's policies.

VACATION LEAVE – is accrued at the end of the year if:

- balance is attributable to services already rendered
- employer will compensate employee with paid time off or cash upon termination

The amount of vacation leave to be reported as Due Within One Year will depend on if the entity has a “use it or lose it” policy or a rolling balance that goes from year to year. Sometimes the leave used in the current year may be used as an estimate for the leave used in the ensuing year.

SICK LEAVE – a liability should be accrued using one of the following termination approaches:

- A. A liability should be accrued as the benefits are earned by the employees if it is probable that the employer will compensate the employees for the benefits through cash payments conditioned on the employees' termination or retirement. Therefore, an accrual for earned sick leave should be made only to the extent it is probable that the

benefits will result in termination payments, rather than be taken as absences due to illness. The sick leave liability generally would be an estimate based on a governmental entity's past experience of making termination payments for sick leave, adjusted for the effect of changes in its termination payment policy and other current factors.
(termination payment method)

B. Alternatively, a governmental entity should estimate its accrued sick leave liability based on the sick leave accumulated at the balance sheet date by those employees who currently are eligible to receive termination payments as well as other employees who are expected to become eligible in the future to receive such payments. To calculate the liability, these accumulations should be reduced to the maximum amount allowed as a termination payment. Accruals for those employees who are expected to become eligible in the future should be based on assumptions concerning the probability that individual employees will become eligible to receive termination payments. (vesting method)

All leave liability balances should be increased for the employer's share of social security. A factor to reduce this amount may need to be devised for those entities that have signed up for the special pay plan.

Pursuant to SDCL 3-12-47 (20) (b), lump sum payments for sick leave and annual leave are exempt from having SDRS withheld.

Compensated absences liability should be calculated based on the pay or salary rates in effect at the balance sheet date.

The bulk of the compensated absence liability is reported on the Statement of Net Assets. However, a small amount, as applicable may also need to be reported on the Food Service Fund balance sheet.

Governmental fund financial statements, which are on the modified accrual basis of accounting, would only report compensated absences that would be liquidated with expendable available financial resources. This may entail staff that have recently signed termination/retirement papers and will be currently receiving a payment from available resources.

SICK LEAVE EXAMPLES

Calculations of Sick Leave Liabilities - C60.902

. Benefit provisions:

- All employees receive one day of sick leave a month. Sick leave is posted to leave records as it is earned—one day a month.
- Sick leave can only be used for paid time off for the illness of the employee or a dependent. Sick leave taken in time off is paid at the employee's normal pay rate.

- There is no limit on the accumulation of sick leave balances.
- If an employee terminates with at least ten years of service, he or she will be paid in cash for sick leave balances up to thirty days, at one-half his or her final pay rate.

Example 4: **Termination Payment Method**

One possible approach to calculating the termination payment method liability would include the following steps. (Governmental entities may develop other appropriate approaches for calculating termination payment liabilities, for example, by developing a ratio based on historical data of sick leave paid at termination compared with sick leave accumulated and by applying that ratio to the sick leave accumulated by the current employee population as of the balance sheet date.)

1. Obtain the following information for all employees (or a representative sample) who have separated from service with the governmental entity over a reasonable period of time, for example, three to five years:
 - a. Total number of sick leave days paid to those employees OR total dollar amount of sick leave termination payments made to those employees.
 - b. Total number of years those employees worked.
2. Determine the sick leave termination cost for each year worked. This can be done by dividing a by b.
 - If the total number of sick days paid is used for the numerator, convert that number to the sick leave termination cost by multiplying it by a factor that considers both the current average daily pay rate for all employees on the payroll and the sick leave termination payment arrangements.
 - If the total dollar amount of sick leave termination payments is used for the numerator, increase the amount of each termination payment included by the average increase in pay from the year of payment to the current year. After this calculation, adjust the result by a factor that converts the retiree pay rate to the average active employee pay rate.
3. Determine the year-end sick leave liability by multiplying the result in step 2 by the number of years all active employees have worked. The number of years all active employees have worked can be determined by means of statistical sampling. Also, increase the liability for salary-related payments.

Liability calculation:

1. Obtain information about termination payments and length of service for employees who have terminated service during the past five years.

<u>Employee</u>	<u>Year Terminated</u>	(a)		<u>Sick Leave Termination Payment</u>	(b) <u>Number of Years Worked</u>
		<u>Sick Days Paid</u>	<u>or</u>		
1	19X2	10		\$ 400	25
2	19X3	0		0	5
3	19X4	30		1,350	30
4	19X5	5		250	25
5	19X6	<u>5</u>		250	<u>15</u>
		50			100

2. Determine the sick leave termination cost for each year worked.
- If the total number of sick days paid is used, convert to termination payment per year worked.

Sick days paid (50)
 × Current average daily pay rate for active employees (\$72)
 × Sick leave termination payment rate (50%)
 = \$1,800

Adjusted sick leave payments = $\frac{\$1,800}{100}$ = \$18 per year worked
 Years worked

3. Calculate the year-end liability: There are ten employees on the payroll, five of whom have been employed for ten years and five of whom have been employed for six years. This means that active employees have eighty person-years of service [(5 x 10) + (5 x 6)]. The liability calculated below includes the employer's share of social security and medicare taxes.

	Total person-years worked by active employees	80
x	Sick leave termination payment per year worked	\$ 18
=	Sick leave termination payment liability	1,440
+	Additional salary-related payments (7.65 percent)	<u>110</u>
=	Total liability	\$1,550

Example 5: Vesting Method

Leave records:

The following are leave records for the three employees as of year-end:

<u>Employee</u>	<u>Length of Service</u>	<u>Sick Leave Balance (in days)</u>	<u>Daily Pay</u>
1	4 years, 11 months	42	\$ 70
2	7 years, 2 months	53	60
3	0 years, 2 months	2	50

Liability calculation:

To calculate the vesting method liability, the preparer should determine whether it is probable that employees with less than ten years of service will in the future meet that condition to receive a cash payment at termination for their sick leave balances. Often, group averages or patterns of attaining the condition would be the basis for making the determination.

In this example, it is the preparer's judgment that, based on past employee behavior, it is probable that (a) all administrative employees who attain seven years of service also eventually attain ten years of service and (b) all police officers attain ten years of service. Employees 2 and 3 are administrative employees. Only employee 2 has attained seven years of service; therefore, employee 3's balances are not included in the calculation. Employee 1 is a police officer and, thus, his sick leave balance is included in the liability calculation.

The preparer also should apply any benefit maximums (for example, the thirty-day maximum) and reduced payment rates (for example, one-half final pay rate) to leave balances to calculate the liability.

The liability calculated below includes the employer's share of social security and medicare taxes.

<u>Employee</u>	<u>Sick Leave Days</u>		<u>Pay Rate</u>	<u>Pay Rate Reduction</u>	<u>Sick Leave Liability</u>
	<u>Accumulated</u>	<u>Accrued</u>			
1	42	30	\$70/day	50 percent	\$1,050
2	53	30	60/day	50 percent	<u>900</u>
Sick leave vesting liability					1,950
Additional salary-related payments (7.65 percent)					<u>149</u>
Total liability					\$ 2,099