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Presented by:
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MSBO Course 170b Accounting and Audit Update - 2022



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Agenda

- GASB 87 – Leases - Year of adoption
- Other Accounting and Auditing Matters
 - GASB 96 – Subscription Based IT Arrangements
 - GASB 98 – Statement name change
 - SAS 136 – New audit standard
 - Audit considerations and planning
 - Beyond the numbers – what else to consider



GASB 87 - Leases



GASB 87 – It's Finally Here?!

- YES!
- Effective for year ends June 30, 2022
- Remind me what GASB 87 means....
- What do I need to do?
- What will the impact be
- Where can I get help?



Step 1 – Identification of a lease



Definition of a Lease

“A contract that conveys control of the right to use another entity’s nonfinancial asset (underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction.”

- Control is defined as right to the following as specified in the contract (must meet both):
 - a. Right to obtain present service capacity from use of the underlying asset AND
 - b. Right to determine the nature and manner of use of the underlying asset
- Period of time or lease term to be defined...
- Exchange or exchange-like transaction means each party is essentially giving up and receiving something in equal value.



Identifying population to be analyzed

- Not all contracts/agreements that will fall under the scope of GASB 87 will be called a “lease”
- Consider the following:
 - Review current lease disclosures and lease agreements
 - Review recurring payments to or from vendors or third parties (other than direct customers, constituents, etc.)
 - Review fixed asset lapse schedules
 - Review of governing body minutes/agendas

This step is perhaps one of the more critical steps in the process. If you fail to identify and analyze all potential leases, it is possible you will miss significant contracts that fall under this standard.



Identifying the lease population

Common leases for School Districts.....

- Computers
- Student I pads
- Smartboards
- Copiers
- Buildings
- Office space
- Buses
- Leased cars
- Equipment
- Land





Step 2 – Determine lease term



Lease Term

Period during which a lessee has a noncancelable right to use an underlying asset *plus* the following periods (as applicable):

- a) *Lessee's* option to extend the lease if reasonably certain that *Lessee* will exercise option
- b) *Lessee's* option to terminate the lease if reasonably certain that *Lessee* will NOT exercise option
- c) *Lessor's* option to extend the lease if reasonably certain that *Lessor* will exercise option
- d) *Lessor's* option to terminate the lease if reasonably certain that *Lessor* will NOT exercise option

If both lessee and lessor have option to terminate lease without permission from other party, it is not considered part of lease term.

There is a lot of judgement involved here – what is reasonably certain?



Short term lease exception

Lease that at commencement, has a maximum possible term under the lease contract of 12 months (or less) after consideration of lease options to extend.

- Options to extend must be considered regardless of probability of being exercised
- Reasonably certain does not apply here

Accounting treatment for short term leases:

- No balance sheet or full accrual impact
- Statement of revenue & expenses is based on payment provisions in contract



Step 3 – Determine initial amounts



Accounting – Lessee – Adoption at 7/1/21

At July 1, 2021, *if not a short term lease or contract with ownership transfer*, lessee recognizes the following:

Full accrual:

| | | |
|-----|---------------------------|--|
| Dr. | Right to use leased asset | Amortized over the shorter of lease term or useful life of asset |
| Cr. | Lease liability | Present value of future lease payments during lease term that will be reduced as lease payments are made |

Modified accrual (Funds): No Entries



Accounting – Lessee (after initial adoption)

At lease commencement, *if not a short term lease or contract with ownership transfer*, lessee recognizes the following:

Full accrual:

| | | |
|-----|---------------------------|--|
| Dr. | Right to use leased asset | Amortized over the shorter of lease term or useful life of asset |
| Cr. | Lease liability | Present value of future lease payments during lease term that will be reduced as lease payments are made |

Modified accrual (Funds):

| | |
|-----|-------------------------|
| Dr. | Capital Outlay |
| Cr. | Other financing sources |



Lessee Initial Measurement– Lease Liability

Present value of payments expected to be made over lease terms should include the following (as applicable):

- Fixed payments
- Variable payments dependent on an index or rate
 - Measured using rate or index in effect at lease commencement
- Variable payments fixed in substance
 - Should NOT include payments based on future performance of the lessee or usage of the underlying asset (outflows of resources as they occur)
- Exercise price of purchase option if reasonably certain to be exercised by lessee
- Penalties for terminating lease if lease term reflects the lessee exercising option to (a) terminate lease or (b) cancellation clause
- Lease incentives receivable from lessor



Lessee Initial Measurement– Discount Rate

To calculate the present value of expected lease payments, must utilize a discount rate.

- Implicit rate in the lease contract
- Incremental borrowing rate
 - Estimated interest rate that would be charged to borrow funds to make lease payments
 - Does the District have a line of credit?
 - Does the District have borrowings from the State?



Lessee Initial Measurement – Lease Asset

Right to use asset is recorded as the sum of the following:

- Initial measurement of lease liability
 - + Lease payments made to lessor at or before the commencement of lease term (less lease incentives)
 - + Initial direct ancillary charges necessary to place lease asset in service



Step 4 – Determine the subsequent accounting (Lessee)



Subsequent Reporting –Lease Liability

On a full accrual level...

| | | |
|-----|------------------|--|
| Dr. | Lease liability | Lease liability decreases as lease payments are made Lease payments should be allocated to accrued implied interest first |
| Dr. | Interest expense | Amortization of the discount on the lease liability which is reported as outflow of resources (interest expense) |
| Cr. | Cash | |

- Modified accrual would be expenditure for lease payment when due (record as DEBT SERVICE expenditure)



Subsequent Reporting –Lease Asset

On a full accrual level...

| | | |
|-----|--------------------------|---|
| Dr. | Amortization expense | <ul style="list-style-type: none">• Asset is amortized over the shorter of the lease term or useful life of underlying asset• May be combined with depreciation expense for financial reporting purposes• If lease contains a purchase option that is reasonably certain to be exercised, the lease asset should be amortized over the life of the asset. |
| Cr. | Accumulated amortization | |



Subsequent Lease Modifications

Changes to the lease terms after initial execution of agreement

- May – be treated as a lease modification (remeasurement)
- May – be treated as a separate lease as opposed to a modification
- May – be treated as a lease termination



Step 5 - Disclosure Requirements



Disclosures– Lessee

Lessee should disclose the following in regard to leases (can be grouped together):

- General description of lease contracts including terms & conditions
- Total amount of lease assets and accumulated amortization (separate from capital assets)
- Total amount of lease assets by major classes of underlying assets (separate from capital assets)
- Amount of outflows of resources recognized in the current period not previously included in lease liability
 - Variable payments
 - Residual value guarantees
 - Termination penalties



Disclosures– Lessee (Cont.)

Lessee should disclose the following in regards to leases (can be grouped together):

- Principal and interest requirements to maturity (disclosed separately)
- Any impairment loss on lease assets and change in lease liability as a result

Include the lease liability in your long-term obligation table in your long-term deb disclosure too.

Adoption of new accounting standard footnote – to be included for 2022.



GASB 87- Final Takeaways



GASB 87 – Lessor Accounting

- GASB 87 applies to Lessors as well
- At lease inception, lease receivable is equal to net present value of payments expected to be received.
- No difference between full accrual/modified accrual accounting.

| Journal Entry at Lease Inception – Same for Modified and Full Accrual | |
|---|-----|
| DR. Lease Receivable | \$X |
| CR. Deferred Inflow | \$X |

| Journal Entries at Subsequent Month – Same for Modified and Full Accrual | |
|--|-----|
| DR. Cash | \$X |
| CR. Lease Receivable | \$X |
| CR. Interest Revenue | \$X |
| DR. Deferred Inflow | \$X |
| CR. Lease Revenue | \$X |



1022 Manual – Account Code Changes

- Change notice coming soon to the 1022 manual related to:
 - Background on GASB 87
 - Example journal entries that we just covered
 - NEW account codes to use in both the funds and full accrual reporting. Most the entries we covered will get NEW codes, some are old codes but, renamed.
 - Maintenance of effort/equity issues



GASB 87 – Where can I get some help?

- Plante Moran Webinars – Available to the public
 - “What you need to know for successful implementation”
 - <https://www.plantemoran.com/explore-our-thinking/events/2019/06/gasb-87-leases-what-you-need-to-know-for-successful-implementation>
 - “A Closer Look”
 - <https://www.plantemoran.com/explore-our-thinking/events/2020/11/gasb-87-leases-a-closer-look>
 - “Advanced implementation questions answered”
 - <https://www.plantemoran.com/explore-our-thinking/events/2021/08/gasb-87-implementation-questions-answered>



GASB 87 – Where can I get some help?

- GASB 87 Q&A on implementation –
 - <https://www.plantemoran.com/explore-our-thinking/insight/2021/03/gasb-87-leases-your-implementation-questions-answered>
- Your Auditor
 - Now is the time to get in contact with your auditor to start discussing
 - Your auditor may also have tools/templates to help you implement
 - Consider materiality



GASB 87 – Summarized Action Items

1. Figure out which leases were in place as of 7/1/21
2. Work with your auditor to determine (1) if material and (2) which tool you will use to use to calculate the impact as of adoption date
3. Determine which lease agreements were entered into after 7/1/21. Add those to your GASB 87 calculator
4. Record the journal entries (full accrual and modified accrual)
 - Impact at 7/1/21 – Adoption
 - Activity during 2022 (consider capital outlay/other financing sources impact for new leases in 2022, in budget amendments)
5. Disclosures – work with auditor to make sure you have all that you need for your capital lease financial statement disclosure.



Other Accounting and Auditing Matters and Other Items to Consider



GASB 96 – Subscription Based IT Arrangements

- Referred to as “SBITAs”
- GASB 87 equivalent, but for software. Software is scoped out of GASB 87.
 - BUT if the arrangement includes hardware in the agreement, GASB 96 will apply to the hardware going forward, not GASB 87
- **Effective Date:** Required adoption for June 30, 2023, early adoption permitted.



GASB 96 – Subscription Based IT Arrangements

What is a SBITA?

- Contract that conveys control of the right to use another party's IT software alone or in combination with tangible assets (IT hardware)
- Term = period in which the entity has the noncancellable right to use the software
 - Generally same definition as GASB 87 – consider extensions etc.
 - Same 12-month short term definition applies to GASB 96
 - “month to month” agreements are scoped out
- Example = Cloud based accounting system subscription



GASB 98 - Annual Comprehensive Financial Report

- Impact:
 - Replaces the term “comprehensive annual financial report” with “annual comprehensive financial report”. Associated acronym is “ACFR”.
 - Adoption required for June 30, 2022 year ends



New Audit Standard – SAS #134

New Auditor Reporting Standard

- First major change to auditor opinion letters in years - form and content changes
- Objective of new standard = Enhance relevance and usefulness of the auditor's report
 - Revised “ordering” for elements in the opinion letter. The opinion is now at the beginning vs. end.
 - New section on auditor independence
 - Expansion on explanation for basis of auditor's opinion
 - Explanation of how misstatements are determined to be material
 - Defines “reasonable assurance” and alerts reader of inherent fraud risks
 - Enhanced wording regarding auditor's responsibilities including around professional judgement, internal controls, and communicating to those charged with governance
- Similar changes to the report letters for your Single Audit too!



2022 – Budgeting Considerations

Heading into Budget Season.....

- Revenue Recognition – All Grants - GAN Dates
- State budget - timing???
- New leases in 2022? Don't forget to budget and account for the capital outlay expenditure and Other Financing Sources



2022 – Grant Considerations

11t – ESSER III Equalization

- Application opened 3/18/22
- Have 90 days to submit application
- MDE committed to getting GANs approved by June 30.....BUT.....
 - MUST have FULLY approved GAN by June 30 to recognize revenue in 2022
 - FULLY approved means having an award date in the GAN
 - Recall last year, some districts were caught off guard with the timing of ESSER 2 (part 1) awards!
- USDE – Will be scrutinizing MDE's spending plan, therefore expect potential higher scrutiny on your spending plan



2022 – Grant Considerations

Terminology Change

- CFDA number is now called the ALN (Assistance Listing Number)
- No changes to actual codes, still five digits

Emergency Connectivity Fund

- Subject to Single Audit - Don't forget to code as federal and include on SEFA!
- ALN #32.009
- If a new Type A for your District, your auditor will be testing

FEMA Grants

- Seeing more districts get awards
- Reminder – Revenue recognition occurs when the project worksheets are in the “obligated” status

School Safety Funding

- \$150M to be allocated likely based on some form of pupil count
- For vaccination/testing support



2022 – Grant Considerations

Childcare Grants

- Districts saw significant dollars in FY 2022. Absent any new or additional information made available these should continue to be EXCLUDED from SEFA as conclusion is that the district is a beneficiary NOT sub-recipient.

“MDE Financial Accounting Guidance During the COVID-19 Pandemic”

- Live document updated by MDE – don’t just download once, check for updates
- Very important to follow the guidance here re: grant codes to use for all the unique grants. Saw many districts last year using wrong grant codes.

Michigan Catastrophic Claims Association Refunds (\$400 per vehicle)

- Should not be material, but recording to revenue class code 199 was the 1022 referent group consensus.



Other Considerations

Data Security

- Education is a top target for ransomware attacks
- Global risk in cyberattacks

Systems

- Are you using the right ERP system?
- Hosted solution vs. district data centers

Fraud

- Review the 3 key components: incentive, opportunity, and rationalization



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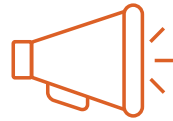


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Thank you!