July
2013

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Accounting Newsletter for Arizona School Districts

Are You Disposing of Surplus Property Correctly?

by Marvin M. Mendieta, CPA, Audit Manager

Managing District property is a major responsibility, and properly disposing of surplus property is an essential part of that responsibility. One of the questions in the USFR Compliance Questionnaire that addresses this area is, "Did the District follow R7-2-1131(C) when disposing of stewardship and capital asset items?" To ensure your district's compliance, it is important to review and understand the rules and regulations that districts must follow for disposing of surplus property.

According to R7-2-1131(C) of the Arizona Administrative Code, the District can use several methods to dispose of property. Some more common available methods that can be advantageous to districts include:

- Competitive sealed bids
- Public auctions
- Trade-ins
- Posted prices
- State surplus property

(Continued on P.3)

Update to Employer Shared Responsibility Provisions of the Affordable Care Plan

On July 2, 2013, the U.S. Department of the Treasury announced that the delayed implementation of certain provisions of the Afffordable Care Plan, in particular those impacting the shared responsibility penalty for employers and the employer and plan reporting requirement. These will both be delayed for one year (until 2015). You can read the Treasury's announcement online here. The IRS has also removed their Q&A and they are expected to provided updated information soon. ■

Delayed Payroll System Requirements for Arizona School Districts

by Karin M. Smith, MBA, SFO, Consulting Manager

Arizona school districts are required to implement a delayed payroll system. Under a delayed payroll system, payments are made after the end of a pay period based on actual time worked during that pay period. This type of system allows time for payroll adjustments to be made before payment to help ensure that employees receive only the compensation they have earned. The USFR indicates that districts should determine how long to delay payment to allow adequate time for adjustments; however, districts may not delay payments more than their normal 2-week payroll processing cycle.

In accordance with A.R.S. §23-351(C)(2) and Attorney General Opinion I04-007, employees may elect to have their compensation paid over the actual months worked or prorated in any number of payments. However, this proration option does not exempt districts from implementing a delayed payroll system.

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Also in This Issue

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Delayed Payroll Systems

(cont'd from P.1)

In the recently revised USFR compliance questionnaire dated 3/2013, the compliance questions were updated to include the following:

- Did the District establish a delayed payroll system so that employees were paid only the compensation they have earned? (Payroll, Q3)
- If the District provided prorated compensation payments to employees:

  - Were elections for prorated compensation made before any work was performed and not changed after work began?
  - Did the District have adequate controls in place, in addition to a delayed payroll system, to ensure that the annual compensation of employees receiving prorated wage payments (for both continuing employees and employees who terminated employment during the year) was equal to the amount actually earned?
  - Were adjustments to the annual compensation of hourly employees who were receiving prorated wage payments based on the employee's official hourly rate of pay that was used to calculate the original annual compensation amount?
  - Did the District ensure that at no point during the year was an employee paid for more than actual hours worked to date? (Payroll, Q4 a-d)

The intent of the requirement for a delayed payroll requirement is to protect districts from the risk of loss. To determine if a district has a delayed payroll system, the USFR states that before prorated payments begin, districts should determine the annual compensation amount that will be prorated and divide it by the selected number of pay periods.

(Continued on P.4)

Arbitrage Rebate vs Yield Reduction Payments

by Cherie R. Wright, CPA, CFE, CGFM, Partner

While many have heard of arbitrage rebates, yield reduction payments are lesser known. Yet, the yield reduction payments under the yield restriction rules have been in existence longer. The rebate rules were implemented with the 1986 Tax Reform Act and have been revised several times over the years, but the yield restriction rules began in 1979.

In general, arbitrage rebate rules mandate when arbitrage must be remitted to the IRS and yield restriction rules govern when arbitrage may legally be earned. The thing to keep in mind is that tax-exempt bonds are subject to both sets of rules, and both constitute different forms of taxation on arbitrage.

The dictionary definition of arbitrage is the purchase of currencies, securities, or commodities in one market for immediate resale in others in order to profit from unequal prices. In the realm of tax-exempt bonds, arbitrage occurs when entities use proceeds from tax-exempt obligations to acquire higher yielding investments. In other words, if the interest received on the proceeds held during the project construction exceeds the interest payments ultimately made to the bondholders, arbitrage has been earned.

Of course, it's never as simple as it sounds. There are very complex rules and exceptions that go into the calculations and, of course, there are different rules and various exceptions for arbitrage rebate and yield restriction. Calculations under both sets of rules must be performed and evaluated to determine which payment should be made.

One of the areas that seems to be most misunderstood is the small issuer exception. Under the arbitrage rebate rules, there is an exception for "small issuers." For those familiar with the arbitrage rebate, this small issuer exception is often relied upon to avoid arbitrage calculations.

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Surplus Property Disposal

(cont'd from P.1)

For **competitive sealed bids**, a notice for sale bids shall be made available to the public for a *minimum* of 10 days prior to the date of opening the bids. The notice for sale bids shall be mailed to prospective bidders, and it shall list the materials offered for sale, instructions and other important information including any terms and conditions. Bids shall be opened publicly, and the District shall award the bid to the highest responsive and responsible bidder.

For **auctions**, the event shall be advertised in the District's county newspaper at least twice before the auction date, ensuring the advertisements are at least seven days apart. The District should also ensure that any terms and conditions of the sale are made available to the public at least 24 hours before the event.

If the District is considering **trade-ins**, it is important to make some assessment on trade-in values. The value obtained from a trade-in should be greater than the value the District could obtain from a sale.

Finally, the District can enter into an agreement with the **State Surplus Property Manager** to dispose of surplus property.

When the District has identified certain assets for disposal, an authorization form should be completed. This form should list the items identified for disposal and the proposed method of disposal. The USFR manual has a sample form for authorization to dispose District property.

It is also important to note that an employee of the District or a governing board member shall not purchase surplus property from the District if the employee or board member has been involved in the purchase, maintenance, disposal, or planning for sale of the surplus property.

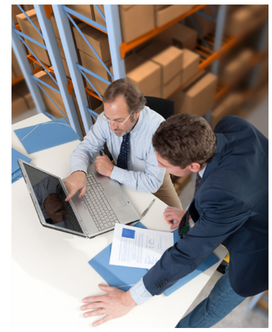
After disposing of the assets, the District should update their capital asset records or stewardship listing accordingly. Any proceeds from

(Continued on P.7)

Is Your Stewardship Listing Up-to-Date?

by Eugene Park, CPA, Audit Manager

According to the Uniform System of Financial Records (USFR) manual, Arizona school districts should maintain a stewardship list for all equipment with unit costs of $1,000 or more but less than the District's adopted cost threshold for capitalization (generally $5,000). The stewardship list should include the description of the item, the location of the item, an identification number, and the month and year the equipment was acquired.



Are the answers to the following questions at your District a yes?

- Did the District maintain a stewardship list for items costing at least $1,000 but less than $5,000 (or the District's capitalization threshold if less than $5,000)? Did the list include the description, identification number (tag number), location of the item, and the month and year of acquisition?
- Did the District update the stewardship and capital assets lists at least annually for acquisitions and disposals?
- Were equipment items recorded on the stewardship and capital assets list identified by a tag, marked with an identifying number, or specifically identified by some other means?
- Was a physical inventory of items taken at least every 3 years and reconciled to the stewardship and capital assets lists?
- Did the District follow R7-2-1131(C) when disposing of stewardship and capital asset items?

Every year these questions are asked in the USFR Compliance Questionnaire. As stewards of items purchased with public monies, your District

(Continued on P.6)

Delayed Payroll Systems

(cont'd from P.2)

Districts should then compare the cumulative anticipated amount earned to the prorated amount paid as of each pay period. If at any point during the year the cumulative amount paid would exceed the cumulative amount earned, districts should adjust the prorated payment amount to ensure prepayment of compensation does not occur.

Districts need to ensure they have the appropriate controls in place to protect their district from loss and implement a delayed payroll system. They should also consider the requirements under Fair Labor Standards Act (FLSA) and the requirements for exempt and non-exempt employees to ensure they do not apply non-exempt employee rules to exempt employees. Districts should review their pay calendars for all employee groups and employee work calendars to verify the pay calendars do not advance payment to any employee prior to the work is performed. Special attention should be considered for employees whose contracts begin mid-payroll cycle, who start mid-year, and who are paid continuously during non-paid school breaks.

Further information and FAQs regarding the requirement for a delayed payroll system can be found on the Arizona Auditor General's website at http://www.azauditor.gov/Reports/School_Districts/FAQs/SD_FAQ_PR.htm ■

Legal and Tax Advice Disclaimer: The information presented in this newsletter does not constitute legal advice or tax advice. Heinfeld, Meech & Co., P.C. makes no claims about its accuracy, completeness, or currency of information presented, including any external references provided. Legal and tax advice, including tax advice, must always be tailored to your circumstances, and no content of this newseltter should be viewed as a substitute for the advice of a competent attorney. Please consult legal counsel for advice pertaining to your specific organization.

Arbitrage Rebate vs. Yield Reduction Payments

(cont'd from P.2)

When a public school district issues tax-exempt debt of up to $15 million in a calendar year ($5 million plus the lesser of $10 million or the amount of bonds issued for construction of public school facilities), it is exempt from the arbitrage rebate rules for the debt issued during that year. This threshold must be evaluated for all tax-exempt debt, which may include bonds, certificates of participation, etc.

However, just because your district qualifies for the small issuer exception, does not mean you are off the hook. The yield restriction rules still apply, and this small issuer exception is one of the reasons that the older yield restriction rules have not gone away. The yield restriction calculations must still be performed regardless of the small issuer status under the arbitrage rebate rules, and, if an amount is owed, a yield reduction payment must be made.

Under the yield restriction rules, during "temporary periods" the yield on the investment of proceeds is unrestricted, and no yield reduction liability will be incurred. Of course, the bonds are still subject to the arbitrage rebate rules, and barring any qualifying exceptions, an arbitrage rebate liability can still be incurred during these "temporary periods." A few of the "temporary period" exceptions include:

- Project funds – generally 3 years with certain exceptions
- Debt service funds – 13 months
- Interest earnings – 1 year
- Reserve funds – unlimited temporary period as long as certain qualifications are met
- Replacement proceeds (certain other revenues) – 30 days

After the "temporary periods" are ended, the investment yield is restricted. If the investment yield is "materially higher" than the bond yield,

(Continued on P.6)

Client Spotlight - Kirk Waddle

Kirk Waddle is the Business Manager of Mingus Union High School District.

What are your hobbies?

My hobbies include camping, cooking and following the district's various athletic teams.

How long have you been in school finance?

I've been in school finance for 13 years and have worked in two school districts.

What was your professional experience prior to working in school finance?

I worked in corporate finance and accounting for 20 years prior to my school finance career. Directly out of Northern Arizona University, I worked as a corporate auditor and senior accountant for Union Pacific Corporation for 4 years. I then spent 8 years with Crowley Maritime Corporation as manager of management accounting and reporting. My last ten years was spent at Microsoft Corporation in their corporate accounting department working in corporate planning and management reporting as a senior finance manager.

What do you feel are the biggest challenges you face in school finance?

My biggest challenge in school finance is likely that of nearly all finance directors and that is managing a district with ever shrinking funding from the State. In Mingus Union High School District, we've been challenged with maintaining a rich offering of advanced placement courses and extracurricular activities for our students. This has become particularly difficult in today's economy. Closely following funding challenges is the ever increasing state and federal reporting requirements.

What are your biggest challenges working in a rural District?

Transportation, technology and professional development come to mind. Our district covers a fairly large area which makes student transportation very important both in the routine daily routes and extracurricular activities such as athletics. The cuts in capital funding over the last few years has made it very difficult to invest in new buses and technology equipment. For professional development, the fact that most opportunities are in the metropolitan areas of Phoenix and Tucson, travel and lodging costs often exceed the cost of the professional development events.

What do you recommend to people entering the profession?

First and foremost, join the Arizona Association of School Business Officials (AASBO) and take advantage of their education opportunities, bi-monthly meetings and various conferences. This is the single best way to network with other school finance officials and stay current with best practices in the industry. Second and no less important, work closely with your auditor to build a strong system of internal controls aligned with GAAP and the USFR. Your job is to protect the assets of the district and a strong system of internal controls keeps you and the district out of trouble.

H&M News

Michael A. Hoerig, CPA, was recently promoted to Partner. Michael has been with our firm since 2001 and specializes in providing auditing services to governmental and non-profit clients from our Tucson office.

We are also happy to announce the following recent staff promotions: *Eugene Park, CPA*, to Audit Manager; *Kaleigh Hotchkiss, CPA*, and *Michael Paul Rohr, CPA,* to Senior Associate; and *Anthony St. George* to Staff Associate II.

Brittney Williams Spross, Audit Manager, has joined the Financial Management Standards Board of the Association of Government Accountants.

Stewardship Listing

(cont'd from P.3)

should ensure that it has written instructions that clearly indicate the procedures for taking a physical inventory. These instructions should be reviewed with employees participating in the inventory process.

One of the most common areas of noncompliance among districts is that physical inventories of stewardship items are not completed timely. What can you do to rectify this?

The following are some suggestions:

- Develop a plan ahead of time of when and how the inventory is going to take place. Plan the inventory during a down time of the year. If the inventory is well planned, it can be completed efficiently and effectively.
- Spread the responsibility among multiple employees. Involve individuals that are not responsible for the custody of equipment to compare the equipment to the stewardship listing. Have personnel cover areas that they do not oversee. Ensure that they follow the District's written procedures in performing a physical inventory.
- Finally, look into pages VI-E-10 to VI-E-11 in the USFR manual (http://www.azauditor.gov/ASD/PDF/USFR2.pdf) for additional suggestions on how to take a physical inventory of District's stewardship items.

Implementing these suggestions should help ensure that your District is being the best stewards of public monies as they can be and in compliance with USFR requirements.

Need help with your inventory procedures or a review of your current stewardship listing? Contact CW Payne at (928) 744-4201, ext 204 or cwp@heinfeldmeech.com. ■

Arbitrage Rebate vs. Yield Reduction Payments

(cont'd from P.4)

a yield reduction payment is owed. Depending on the circumstances, "materially higher" is defined as either 0.001% or 0.125%. In other words, if the bond yield is 4% and is subject to the 0.125% restriction, the investment yield must be less than 4.125% to avoid a liability.

The end result is that your district may incur a rebate liability or a yield reduction liability. If both calculations indicate an amount is owed, the IRS requires payment of the larger of the two. If nothing is owed under either set of rules, there are no filing requirements with the IRS. However, your district is still subject to a potential audit, during which the IRS will request the calculations verifying no liability was incurred.

For IRS purposes, the calculations must be performed each "installment computation date," which is typically every fifth year since the bonds were issued, and at the "final computation date," when all the bonds have been retired whether matured or redeemed early. However, annual calculations are recommended for financial statement and other bond disclosure purposes.

To ensure compliance with these and other arbitrage requirements, the district's debt management policy should include a section on arbitrage compliance. The arbitrage compliance policy may include a variety of topics including definition of bond years, rules for establishing appropriate accounts and the treatment of commingled accounts, frequency of calculations, record retention, etc.

Questions? Contact Cherie Wright at (602) 277-9449, ext 376 or cheriew@heinfeldmeech.com. ■

HMU Events

Details and links to online registration can be found at www.heinfeldmeech.com/hmu. For more help, contact Susan at 520-742-2611, x107 or hmu@heinfeldmeech.com.

The Ins and Outs of the FLSA - How to Keep Your Organization Out of Trouble

Location: Mesa, AZ (Mesa Convention Center)

Date: Tuesday, August 20 *(registration ends 8/12/13)*

Financial Coding - Understanding the Chart of Accounts (workshop)

Location: Phoenix, AZ (Hilton Garden Inn)

Date: Tuesday, September 10 *(registration ends 9/3/13)*

The School District Guide to Completing the Annual Financial Report (workshop)

Location: Phoenix, AZ (Hilton Garden Inn)

Date: Wednesday, September 11 *(registration ends 9/3/13)*

Best Practices on Working with Parent-Teacher Organizations (webinar)

Date: Tuesday, September 24 (times TBA) *(registration open by early August)*

Best Practices in Student Activities and Auxiliary Operations (workshops)

Locations/Dates: *(registration open by mid-August)*

Vail (Tucson area) - Tuesday, October 8

Mesa - Wednesday, October 9

Welcome to Our New Clients

H&M welcomes our new clients:

Continental Elementary

Peach Springs Unified

Kayenta Unified

Cartwright Elementary

Clifton Unified

We are excited that you have chosen H&M and look forward to helping you achieve new levels of accounting and managerial success!

Puzzler

Decipher the hidden meaning: (Answer on p. 8)

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Property Surplus Disposal

(cont'd from P.3)

the sale of assets should be recorded in the School Plant Fund (Fund 506) unless required to be remitted to a federal or state agency.

Proper disposal of district property requires understanding the available methods for property disposition. Before taking action, your district should determine the appropriate method of disposal that would be most advantageous and ensure compliance with the USFR.

Need help with developing surplus property procedures at your district? Contact CW Payne at 928-774-4201, x204 or cwp@heinfeldmeech.com.

Recent and Upcoming School District Deadlines

Due Date	Item
July 5	Proposed budget due Copy of the proposed budget and a notice of the public hearing and board meeting must be published in a newspaper or mailed to each household (A.R.S. §15-905.C). Districts that maintain a website must also provide a link on their website to ADE's website (A.R.S. §15-905(A)(2)). Districts must also e-mail ADE the direct link to the location of the proposed budget link on their website. (Districts should also retain a copy of the e-mail and a screen shot of their website for audit purposes.)
July 15	Adopted budget must be approved by the Board
July 15	Bus Inventory Due to ADE
July 18	Adopted Budget must be uploaded to ADE Advice of encumbrande due to the CSS
July 31	Employer's Quarterly Federal 941 Tax Form due to IRS Arizona Quarterly Withholding Tax Return (A1-QRT) due
August 20	Amount to be raised from primary and secondary property taxes must be fixed, levied & assessed (A.R.S. §§15-992 and 42-304.B)
Before Aug 31st	PEA/LEA calendar due to ADE
September 28	Deadline for completion reports to be submitted to ADE for projects ending June 30

About H&M

Heinfeld, Meech & Co., P.C., CPAs and Business Consultants, has offices in Tucson, Phoenix and Flagstaff, Arizona. With more than 27 years of experience, we are the recognized leaders in the State of Arizona in the field of school district accounting and auditing.

Our active involvement with national and state associations keep us up-to-date about emerging issues affecting your school district. We offer this free newsletter as part of our commitment to providing resources and training to school district business personnel.

For more about our firm, please visit our web site at www.heinfeldmeech.com.

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Answer to Puzzler (Page 7): I'll be there in a minute