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MEMORANDUM

DATE: October 22, 2021

TO: County Auditors

FROM: Tammy White, CPA
Deputy State Examiner

RE: Reporting taxes receivable and related revenues in fiduciary financial statements for Indiana Counties

The following guidance under the heading of *Property Taxes* was provided in the Indiana State Board of Accounts (SBOA) memorandum dated February 25, 2021, and is still applicable. However, we did not clearly state at that time that this treatment is applicable to the presentation of property taxes levied for other governments within the County for presentation in the fiduciary (custodial funds) financial statements. This memorandum is to clarify the guidance as it is applicable to the fiduciary financial statements and the presentation of custodial funds.

This memorandum also clarifies our position on reporting of taxes receivable and related revenues for taxes collected by the State of Indiana and distributed to Counties.

<u>Property Taxes</u>

Property tax revenue is recognized in the fiscal period for which it was levied, and the assets (receivables) in the period when an enforceable legal claim to the assets arises or when the resources are received, whichever occurs first. In Indiana, the enforceable legal claim date occurs in the year prior to the year for which the taxes are levied. Deferred inflows of resources should be reported when resources are received or reported as a receivable before the period for which property taxes are levied. (GASB Cod. N50.114-.115)

In full accrual financial statements counties should report a receivable for property taxes to be levied in the subsequent calendar year with an offset to deferred inflows of resources both in the proper county funds for the county's share of property taxes and in fiduciary funds for the property taxes due other governmental units. Counties should also report a receivable in the proper county funds and in fiduciary funds with an offset to a liability for those taxes billed in the current and prior years that were uncollected. The fiduciary fund in which these property taxes are accounted for should only report the additions and deductions for those amounts received for and distributed to other governmental units. (GASB Comprehensive Implementation Guide 7.81.1)

Taxes Distributed by the State to Counties

Indiana Counties receive and distribute to themselves and other governmental units within their county, a variety of other taxes, the largest of which are: Financial Institutions Tax, Excise Taxes, Riverboat Wagering, County Wheel and County Surtax, and Unified Local Income Taxes.

The State imposes the tax which is the basis for all the distributions except for Unified Local Income Taxes and County Wheel and County Surtax. Unified Local Income Taxes and County Wheel and County Surtax are imposed at the county level even though they are collected by the State.

All the distributions, except for Unified Local Income Taxes and County Wheel and County Surtax, are government mandated or voluntary nonexchange transactions. By statute, the State is sharing a portion of its own derived tax revenues or imposed nonexchange revenue with other local governments; up to 100% of some collection types. (GASB Cod. N50.125) The State has not specified a time requirement for these distributions that states: when the resources are required to be used; or when use is first permitted has begun, or the resources are begin maintained intact, as specified by the provider. (GASB Cod N50.117) As a result, counties should recognize receivables and revenue for the entire amount expected to be received during the State's fiscal year in accrual based financial statements. (GASB Cod. N50.121) This would result in the amount of receivable at the end of the County's fiscal year of December 31 being the expected amount to be received the following January through June to correspond with the remaining State fiscal year. For modified accrual (governmental fund statements) revenue will be recognized when they become available and measurable. (GASB Cod. N50.126) The term available means "collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period."

Unified Local Income Taxes are derived tax revenues. County Wheel and County Surtax are imposed nonexchange revenues. All three are imposed by counties but collected by the State and they do not have time requirements. A receivable should be recognized in the period when the exchange transaction on which the tax is imposed occurs or when an enforceable legal claim arises or when resources are received, whichever occurs first. (GASB Cod. N50.113-114) Revenue is recognized in the same period the receivable is recognized in accrual based financial statements. (GASB Cod. N50.113, .115) For modified accrual (governmental fund statements) revenue will be recognized when they become available and measurable.

Per the Indiana Handbook of Taxes, Revenues, and Appropriations, the amount of local income tax revenue distributed during an ensuing calendar year equals the amount of tax the State Budget Agency determines was received from the county for a taxable year ending in a calendar year preceding the calendar year in which the determination is made and was reported on an annual or amended return processed by the Department of State Revenue in the fiscal year ending before July 1 of the calendar year in which the determination is made. The State Budget Agency provides an estimated distribution amount before August 1 and certifies the distribution amount before October 1. This means the Unified Local Income Taxes distributed were based on wages two year prior however only the current year's collections are to be recognized as receivable and revenue in accrual based financial statements.

County Wheel and County Surtax distributions are for the prior month's vehicle registrations. Only the December collections by the Bureau of Motor Vehicles, that are remitted in January to the county, would need to be recognized as receivable and revenue in accrual based financial statements.

From a practical standpoint, governments may use the amount of total taxable activities reported or estimated during their fiscal year or actual receipts adjusted for accruals as a practical means to recognizing nonexchange transactions. The use of this practical approach to revenue recognition must demonstrate that the effects do not materially misstate the revenue that would be recognized using the underlying event standard established by GASB. (AICPA SLG 2021 ¶ 6.26 and GASB Cod. N50.902 Example 5)

The revenue and asset recognition described above must be recorded in the proper county fund as of the county's fiscal year end for the portion of the state distributions that will ultimately be distributed to the county with the portion due other governmental units recognized as receivable and an offsetting liability in the appropriate custodial funds. Also, the fiduciary fund in which these state distributions are accounted for should only report the additions and deductions for those amounts received for and distributed to other governmental units. (GASB Comprehensive Implementation Guide 7.81.1 and GASB Cod. 1300.134)

Per GASB 84 ¶ 21, a liability to the beneficiaries of a fiduciary activity should be recognized in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources. Events that compel a government to disburse fiduciary resources occur when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets. For example, a county government should recognize a liability when it collects taxes for other governments, even though it may not be required to distribute the taxes to those governments until a specified time in the future.

<u>Applicable Authoritative Literature</u>

Full accrual basis - Fiduciary financial statements

Derived Tax Revenue Transactions

GASB Cod. § N50.113: "Governments should recognize *assets* from derived tax revenue transactions in the period when the exchange transaction on which the tax is imposed occurs or when the resources are received, whichever occurs first. *Revenues* should be recognized, net of estimated refunds and estimated uncollectible amounts, in the same period that the assets are recognized, provided that the underlying exchange transaction has occurred. Resources received in advance should be reported as liabilities until the period of the exchange. Derived tax revenues generally do not have time requirements. However, if they apply, asset and revenue recognition should be consistent with the requirements for imposed nonexchange revenue transactions. [GASBS 33, ¶16, as amended by GASBS 65, ¶31; GASBS 33, fn8]"

Receivable Recognition

GASB Cod. § N50.114: "Governments should recognize assets from imposed nonexchange revenue transactions in the period when an enforceable legal claim to the assets arises or when the resources are received, whichever occurs first. For property (ad valorem) taxes, the date when an enforceable legal claim to taxable property arises generally is specified in the enabling legislation. Many governments refer to this date as the 'lien date,' even though a lien is not formally placed on the property at that date. Some governments, however, use a different term, such as the 'assessment date.' (For some governments, the enforceable legal claim does not arise until the period after the period for which the taxes are levied. Those governments should recognize property taxes receivable in the same period that revenues are recognized in accordance with paragraph .115.) [GASBS 33, ¶17]"

GASB Cod. § N50.115: "Governments should recognize revenues from property taxes, net of estimated refunds and estimated uncollectible amounts, in the period for which the taxes are levied, even if the enforceable legal claim arisesor the due date for payment occurs in a different period. All other imposed nonexchange revenues should be recognized in the same period that the assets are recognized unless the enabling legislation includes time requirements. If so, revenues should be recognized in the period when the resources are required to be used or when use is first permitted. Deferred inflows of resources associated with imposed nonexchangerevenue transactions should be reported when resources are received or reported as a receivable before (a) the period for which property taxes are levied or (b) the period when resources are either required to beused or when use is first permitted for all other imposed nonexchange revenues in which the enabling legislation includes time requirements. [GASBS 33, ¶18, as amended by GASBS 65, ¶9; GASBS 65, ¶9]"

Government-Mandated Nonexchange Transactions and Voluntary Nonexchange Transactions

GASB Cod. § N50.116: "Providers of resources in government-mandated or voluntary nonexchange transactions frequently establish eligibility requirements. Eligibility requirements are conditions established by enabling legislation or the provider that are required to be met before a transaction (other than the provision of cash or other assets in advance) can occur. That is, until those requirements are met, the provider generally does not have a liability, the recipient generally does not have a receivable, and expenses and revenues for resources transmitted in advance should not be recognized until those eligibility requirements are met. [GASBS 33, ¶19, as amended by GASBS 65, ¶10; GASBS 65, ¶10]"

Eligibility Requirements

GASB Cod. § N50.117: "Eligibility requirements for government-mandated and voluntary nonexchange transactions comprise one or more of the following:

a. *Required characteristics of recipients*. The recipient (and secondary recipients, if applicable) has the characteristics specified by the provider. (For example, under a certain federal program, recipients are required to be states and secondary recipients are required to be school districts.)

b. *Time requirements*. Time requirements specified by enabling legislation or the provider have been met. (The period when the resources are required to be used [sold, disbursed, or consumed] or when use is first permitted has begun, or the resources are being maintained intact, as specified by the provider.)

c. *Reimbursements*. The provider offers resources on a reimbursement ('expenditure-driven') basis and the recipient has incurred allowable costs under the applicable program.

d. *Contingencies* (applies only to voluntary nonexchange transactions). The provider's offer of resources is contingent upon a specified action of the recipient and that action has occurred. (For example, the recipient is required to raise a specific amount of resources from third parties or to dedicate its own resources for a specified purpose and has complied with those requirements.) [GASBS 33, ¶20]"

Recognition of a Deferred Inflow of Resources

GASB Cod. § N50.118: "Providers should recognize liabilities (or a decrease in assets) and expenses from government-mandated or voluntary nonexchange transactions, and recipients should recognize receivables (or a decrease in liabilities) and revenues (net of estimated uncollectible amounts), when all applicable eligibility requirements, including time requirements, are met. Resources transmitted before the eligibility requirements are met (excluding time requirements) should be reported as assets by the provider and as liabilities by the recipient. Resources received or recognized as a receivable before time requirements are met, but after all other eligibility requirements have been met, should be reported as a deferred outflow of resources by the provider and a deferred inflow of resources by the recipient. [GASBS 33, ¶21, as amended by GASBS 65, ¶10; GASBS 65, ¶10]"

Receivable Recognition for State Distributions

GASB Cod § N50.121: "Sometimes a provider in a government-mandated or voluntary nonexchange transaction does not specify time requirements. When that is the case, the entire award should be recognized as a liability and an expense by the provider, and as a receivable and a revenue (net of estimated uncollectible amounts) by the recipients, in the period when all applicable eligibility requirements are met (applicable period). When the provider is a *government* (including the federal government), the applicable period for both the provider and the recipients is the *provider's* fiscal year and begins on the first day of that year (when, for example, the relevant appropriation becomes effective). The entire award should be recognized at that time. However, if a provider government has a biennial budgetary process, each year of the biennium should be considered a separate applicable period. In those circumstances, the provider and the recipients should allocate one-half of the resources appropriated for the biennium to each applicable period, unless the provider specifies a different allocation. [GASBS 33, ¶24]"

GASB Cod § N50.125: "On the other hand, a government may share its own derived tax revenues or imposed nonexchange revenues with other governments. For example, a state (provider) may share a portion of the revenues resulting from its sales tax with local governments. Both the provider and recipient governments should comply with the requirements of this section for voluntary or government-mandated nonexchange revenues, as appropriate. Because some recipient governments receive these shared revenues through a continuing appropriation, they may rely on periodic notification by the provider government of the accrual-basis information necessary for compliance. If notification by the provider government is not available in a timely manner, recipient governments should use a reasonable estimate of the amount to be accrued. [GASBS 36, ¶2]"

GASB Cod § 1300.134: "For activities not addressed in paragraphs .129–.133, the activity is a fiduciary activity if all of the following criteria are met:

a. The assets associated with the activity are controlled by the government (as described in paragraph .135).

b. The assets associated with the activity are not derived either:

   (1) Solely from the government's own-source revenues (as described in paragraph .136) or

   (2) From government-mandated nonexchange transactions or voluntary nonexchange transactions with the exception of pass-through grants for which the government does not have administrative involvement or direct financial involvement.

c. The assets associated with the activity have one or more of the following characteristics:

   (1) The assets are (a) administered through a trust in which the government itself is not a beneficiary, (b) dedicated to providing benefits to recipients in accordance with the benefit terms, and (c) legally protected from the creditors of the government.

   (2) The assets are for the benefit of individuals and the government does not have administrative involvement with the assets or direct financial involvement with the assets. In addition, the assets are not derived from the government's provision of goods or services to those individuals.

   (3) The assets are for the benefit of organizations or other governments that are not part of the financial reporting entity. In addition, the assets are not derived from the government's provision of goods or services to those organizations or other governments. [GASBS 84, ¶11]"

Reporting Custodial Funds

GASB Comprehensive Implementation Guide 7.81.1. Q—A county tax collector collects property taxes for all taxing bodies in the county, including the tax-levying funds of the county. The county uses a custodial fund as a distribution mechanism for the taxes. At year-end, the collector is holding $3,450,000 in the tax distribution account. Of that total, $750,000 will be distributed to the county funds, and the remaining $2,700,000 represents taxes collected for the other taxing bodies in the county. How should the county report the portion collected and on hand for the county's purposes?

A—In the county's financial statements, the tax collector's custodial fund would report only the $2,700,000 in cash with an equal amount as a liability to other taxing bodies. The $750,000 collected and on hand for the county's funds would be reported as cash (rather than taxes receivable or due from custodial funds) in the appropriate funds. In essence, the collector has a "pooled" cash account, similar to an internal investment pool. The allocation of cash balances to the county funds is consistent with the requirement in paragraph 14 of Statement 31 that requires the "equity position" of each fund in an internal investment pool to be reported as assets in those funds.

AICPA SLG 2021 ¶ 6.26: ". . . from a practical standpoint, governments will likely base the amount to be recognized as sales or other consumption tax revenues on total taxable activities reported or estimated for the weeks or quarters that make up the government's fiscal year. That appendix further indicates that, from a practical standpoint, a government will likely base the amount to be recognized as income tax revenue on the amount of withholding and estimated tax payments made during the government's fiscal year, adjusted for post-fiscal-year final settlements (additional payments and refunds). Those practical explanations do not change the standard for the recognition of those revenues but, rather, recognize the application of materiality considerations. A government that recognizes those revenues following the practical approaches has to be able to demonstrate that the effects do not materially misstate the revenue that would be recognized using the underlying event standard . . ." established by GASB. (GASB Cod. N50.902 Example 5)