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4.01 OVERVIEW

This section of the manual discusses financial policies that are necessary to ensure effective financial management. It includes a discussion of generally accepted accounting principles and the key financial policies required to comply with these principles. In addition, discussion of the need for compliance with outside regulations is included. Specific questions may be directed to the Controller's office.

4.02 UNIVERSITY POLICY

The Board of Trustees and the University administration subscribe to the financial management concepts described in this section of the manual and adopt the policy statements listed below.

- That the University’s financial accounting practices conform to those recommended in the AICPA Audit Guide for Colleges and Universities, Industry Audit Guide.
- That accounting practices be established which insure that funds received from third parties for specific purposes are accounted for separately from unrestricted funds.
- That the University establish policies and procedures that satisfy legal restrictions, regulations and rules imposed by Federal and State government agencies and other third parties.

4.03 DEFINITION OF FINANCIAL POLICIES

Financial policies may be defined as basic guidelines for processing, recording, and reporting financial information in colleges and universities. Appropriate financial policies have been developed and implemented by the University in order to monitor and support successful financial management. The Board of Trustees and the Administration of the University have established policies that assist them in performing their fiduciary responsibilities. The established policies that have been adopted are consistent with policy recommendations promulgated by authoritative bodies.

The significant financial policies relating to educational institutions are established by:

- the accounting profession through generally accepted accounting principles, and
- Federal and State governments as provided in the law and supporting administrative regulations. The remainder of this chapter reviews the policies established by these sources.
4.04 DESCRIPTION OF GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

Generally Accepted Accounting Principles (GAAP) are those methods and conventions of recording and reporting financial information which result in a fair presentation of financial position and results of operations. A fair presentation is one that allows analysis of financial statements and permits comparison with financial information of similar institutions. This ability is important to Federal and State governments and other unrelated sources of funding (including private foundations, individuals, etc.) which need to assess institutional operations. In addition, many government regulations require the examination of financial statements by independent external auditors in order to render an opinion of the fairness of the presentation of the financial information in the statements. Key Generally Accepted Accounting Principles that have been adopted as policy are described in the succeeding paragraphs.

4.04.1 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, or in accordance with regulations, restrictions, or limitations imposed by sources outside the institution, or in accordance with directions issued by the Board of Trustees.

A fund is an accounting entity with a self-balancing set of accounts for recording assets, liabilities, fund balances, and changes in fund balance. Separate accounts are maintained for each fund to ensure the adherence to limitations and restrictions placed on the use of resources.

The following fund groups are used in colleges and universities in accounting and reporting their financial activities:

- Current Funds - separated into:
  - Unrestricted - resources expendable for any purpose in performing the primary objectives of the institution; and
  - Restricted - resources received from donors or other outside agencies and that were restricted by them for specific operating purposes.
- Loan Funds - loans to students, faculty, or staff and the resources available for such purposes.
- Endowment and Similar Funds - consist of endowment funds, term endowment funds, and quasi-endowment funds.
  - Endowment Funds are resources for which the donor has stipulated, as a condition of the gift instrument, that the principal amount would be maintained inviolate and in
perpetuity for investment. Investment earnings may be added to the principal or expended for restricted or unrestricted purposes, based on the donor's request.

- Term Endowment Funds are similar to endowment funds except that, upon the passage of time or the happening of a particular event, all or a part of the principal may be expended.
- Quasi-endowment Funds are funds which the governing board of an institution, rather than an outside source, has determined to be retained and invested. Since this is an internal designation, the governing board has the right to expend the principal of these funds at any time.
- Annuity and Life Income Funds - resources acquired by the institution under agreements to remit stipulated amounts periodically to the donor or other designated individual; the agreement is made to cover a stated, predetermined period of time (annuity) or for the lifetime of the donor or designated individual (life income).
- Plant Funds - composed of four subgroups:
  - Unexpended Plant Funds - unexpended resources that finance the acquisition of physical properties for institutional purposes;
  - Renewals and Replacements - resources which finance the replacement of institutional properties;
  - Retirement of Indebtedness - resources accumulated to finance principal and interest payments relating to indebtedness on institutional properties; and
  - Investment in Plant - funds invested in institutional properties.
- Agency Funds - resources for which the institution is acting only as the agent or custodian for others.

### 4.04.2 Segregation of Restricted and Unrestricted Funds

Clear distinctions between the balances of funds that are externally restricted and those that are unrestricted are maintained in the accounts and in the financial reports of each fund group.

Unrestricted funds may be internally designated for a specific purpose by formal action of the Board of Trustees. This internal designation may be reversed at a later date, at the discretion of the Board.
4.04.3 **ACCRUAL ACCOUNTING**

Financial reports are prepared on the accrual basis of accounting. Revenues are reported when earned, and expenditures when materials or services are received. Included as expenditures are all amounts disbursed for the acquisition of plant fund assets and for plant debt service requirements. Expenses incurred but unpaid are accrued and expenses paid but applicable to future periods are deferred. Revenues and expenditures relating to an academic term that is conducted in parts of two fiscal years (such as a summer session) are reported totally within the fiscal year in which the term is predominantly conducted. Encumbrances represent outstanding purchase orders and other commitments for materials or services not received as of year-end. They should neither be reported as expenditures nor be included as liabilities in the financial statements.

4.04.4 **ACCOUNTING FOR GIFTS, GRANTS AND BEQUESTS**

Gifts, grants, bequests, and other receipts restricted as to their use by outside grantors or agencies are recorded as additions directly in the fund groups appropriate to the restricted purposes of the receipts until such time as they are expended. Unrestricted gifts, bequests, and grants are recorded as unrestricted current funds revenues.

4.04.5 **INVESTMENTS**

Investments purchased are recorded in the financial records at cost, while investments received as gifts are recorded at the fair market or appraised value at the date of the gift. Investments of various funds may be pooled unless prohibited by statute or by terms of the gift. Accounting for pooled investments should demonstrate an equitable method for distribution of income and realized gains or losses on investments, based on each fund’s participation in the pool. Gains or losses on investments of all funds are treated as revenues (expenses) or additions (deductions) to fund balance in the appropriate fund.

4.04.6 **DEPRECIATION OF PHYSICAL PLANT**

Depreciation related to physical plant assets is not reported nor calculated by the University at this time. Effective with FY 2002, the University will calculate and record depreciation in accordance with GASB 34.
4.04.7  INTERFUND BORROWINGS

Interfund borrowings of a temporary nature are to be reported as assets of the fund group making the advances as well as liabilities of the fund group receiving the advances.

4.04.8  FUNDS HELD IN TRUST BY OTHERS

- Funds held in trust by others are those resources that are controlled and administered by outside fiscal agents who remit income earned to the institution. These funds are not to be included in the balance sheet of funds administered by the institution unless:
  - The institution has a legally enforceable right to the funds and their income; or
  - The funds were established under irrevocable trusts without discretionary trustee control of the income distribution.

4.04.9  RELATED ORGANIZATIONS

Many institutions of higher education have separately incorporated but related units for which the institution is fiscally responsible, or which operate for the benefit of the institution (i.e., university presses, intercollegiate athletics, fund raising foundations, medical practice plans, etc.). For adequate disclosure, these units are:

- included in the financial statements,
- adequately disclosed by notes, or
- presented in separate financial statements accompanied by and cross-referenced in the basic financial statements of the institution.

4.05 COMPLIANCE WITH OUTSIDE REGULATIONS REGARDING FINANCIAL ACTIVITIES

In addition to the internal financial policies an institution has established for itself, there is also a need to comply with certain financial regulations promulgated by outside authorities. The major outside financial regulators for an institution of higher education would be:

- Federal Government and its agencies - Institutions must comply with the appropriate regulations of federal agencies (i.e., Department of Education (ED), National Institute of Health (NIH), Department of Defense (DOD), and the Internal Revenue Service (IRS)),
which are applicable to federal gifts, grants, and contracts. Specific rules apply to loan funds (i.e., National Direct Student Loan Programs (NDSL). Government awards, Pell Grants, and Supplementary Educational Opportunity Grants (SEOG)) also contain specific regulations requiring institutional compliance. In addition, compliance with federal regulations, such as Office of Management and Budget (OMB) Circulars A-21 and A-110, is necessary.

- State Government - As the source of tax levy funds to the public institutions of higher education, the State of New Jersey has established certain regulations regarding the use of these funds. Institutions must assure that their practices and procedures comply with these regulations. It is also the obligation of institutions with outstanding debt to assure that all requirements mentioned in the debt instrument are fully satisfied.

- The Public - Beyond the compliance responsibility of institutions of higher education just described, institutions also assume compliance responsibilities of another sort, based on certain actions taken. Such responsibility is most clearly evident in the acceptance of restricted or endowment funds. Institutions have a fiduciary responsibility to assure that such funds are expended in accordance with the restrictions of the donor. In the case of endowment funds, the institution accepts responsibility for assuring that the principal of “pure or true” endowment and term endowment be maintained inviolate and in perpetuity or for the term specified by the donor. In addition, representatives of the institution must assure that these funds are prudently invested for the purpose of producing present and future income. This may either be expended or added to principal, depending on the expressed instructions of the donor.

In the following sections, the major regulations affecting financial activities of colleges and universities are described briefly. With regard to the public, it should be noted that such sources would principally be foundations, corporations, and individual donors. Regulations will be promulgated and must be interpreted on an individual basis.

4.05.1 OMB CIRCULAR A-21

Federal Office of Management and Budget Circular A-21, issued March 6, 1979, established principles for determining costs applicable to grants, contracts, and other agreements with educational institutions. The principles are designed to assure that the federal government assumes its fair share of total project costs. Circular A-21 is applicable to all federal agencies that sponsor research and development, training, and other work at educational institutions. The Circular became effective for fiscal years beginning after October 1, 1979. For complete information and procedures regarding applicable costs pertaining to Federally sponsored programs, refer to Circular A-21, the Department of Health and Human Services (HHS) interpretations of A-21.
The major systems requirements of OMB A-21 are:

- **Effort Reporting** - This is the process of collecting and reporting the effort expended by professorial, professional, and non-professional employees on grants and contracts and other effort categories over a period of time. Signed effort certifications by all covered employees is a major requirement of this system. In addition, an annual summary of signed effort certifications should be used in the preparation of the annual indirect cost proposal.

- **Equipment Inventory** - A physical inventory of equipment is to be performed and a system developed to maintain and update such records. Individual items of inventory should be marked to facilitate identification. Detailed physical inventory records as well as analyses of changes should be available to the Board and senior management for review.

- **Specialized Service Centers** - An institution must identify specialized service centers and establish charge out rates for such services. Costs of these services should be charged directly to all users based on the actual rate of use and by using a uniform pricing structure. Costs should include both direct costs and an appropriate share of indirect costs.

### 4.05.2 OMB CIRCULAR A-110

Office of Management and Budget Circular A-110 established standards for the administration of grants and other agreements between the Federal government and institutions of higher education. Federal agencies responsible for administering such programs must issue the appropriate regulations to implement this Circular. Standards were established for the following areas:

- Cash Depositories
- Bonding and Insurance
- Retention and Custodial Requirements for Records
- Program Income
- Cost Sharing and Matching
- Standards for Financial Management Systems
- Financial Reporting Requirements
- Monitoring and Reporting Program Performance
- Payment Requirements
- Revision of Financial Plans
- Closeout Procedures
- Suspension and Termination Procedures
- Standard Form for Applying for Federal Assistance
Circular A-110 requires an audit of the system and its internal procedures established to meet the terms of federal agreements. The audits are to be conducted at least biennially, by a qualified auditor who is independent from the management and administration of the sponsored programs. The Circular discusses a “single audit approach” for Federal grants and contracts.

**4.05.3 ED FEDERAL AID AUDIT DIRECTIVES**

The Department of Education (ED) requires that federally sponsored student aid programs be audited at least biennially and the results reported to ED for analysis and review. The programs involved are the National Direct Student Loan (NDSL), Pell Grants, and Supplemental Educational Opportunity Grants (SEOG) and University Work-Study (CWS). The objectives of the audit are to determine whether the institution has:

- established procedures for coordinating student aid,
- implemented procedures to discharge management responsibilities effectively,
- implemented procedures to ensure that student aid funds are used for the specified purpose,
- submitted accurate information on annual reports to the Office of Education, and
- fairly presented the financial statement in accordance with generally accepted accounting principles applied on a consistent basis.

The auditor is required to include all findings and recommendations noted, both financial and compliance oriented, and the institution’s response to them in the audit report. Detailed procedures to be performed and report formats to be used are included in the two published audit guides.