State of North Carolina
Department of State Treasurer

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Memorandum #1015

March 31, 2004

To: Finance Officers of Municipalities and Counties and
Certified Public Accountants

From: T. Vance Holloman, Director
Fiscal Management Section

Subject: Recognition of Sales Tax and Other Revenues at Year-End

In order for funds received after the fiscal year end to be accrued as revenues at the end of the fiscal year, two conditions must be met. First, the revenues must have been earned by year-end. Revenues that are taxes upon a transaction are considered earned if the transaction occurs by year-end, even if the tax is not collected until a later date. Second, the revenue must be measurable. Revenues are considered measurable if a unit can make a reasonable estimate of the amount, it is not necessary to know the exact amount. Under the modified accrual basis of accounting, revenue must also be considered available to pay liabilities the unit had at year-end. Currently most local governments report revenues as available if they are received during the first 60 days of the subsequent fiscal year.

Generally accepted accounting principles (GAAP) do not establish the period to be used for determining availability of revenues other than property taxes. (A period no greater than 60 days may be used for property taxes.) Due to the recent change in the distribution of sales taxes, from quarterly to monthly, many local governments have expressed a desire to change the 60-day period for determining if revenue is available and can be accrued by year-end in the governmental funds. Taxes for all June 2004 sales will be distributed on or around September 15, 2004, which is beyond the 60-day period. If units maintain the 60-day period, they would only record 11 months of sales tax revenues in the current year. In order for statements to reflect a full twelve months of sales tax revenues, and to avoid a material adjustment when converting from fund to government wide statements, we encourage all local governments to use a 90 day period for determining if revenues are available for revenue recognition. Our illustrative financial statements will be updated to reflect a 90-day period.

In addition to sales taxes, other revenues will be impacted by this change. Municipalities should also accrue the utility franchise tax, piped natural gas tax and telecommunications tax distribution received from the State in mid September. These taxes are from transactions occurring prior to June. Also, occupancy taxes for transactions occurring prior to June 30 would be accrued if received within 90 days of year-end.

The financial statements for the year ending June 30, 2004 should only reflect twelve months of revenue for any revenue source. Therefore, if the use of the 90-day period results in more than twelve months of revenues being recognized, units will need to make a prior period adjustment if the additional amounts are material to the statements. The adjustment would decrease revenues, to reflect only twelve months of revenues, and increase beginning fund balance in the fund statements. Since availability does not impact the government wide statements, no adjustment will be needed. When determining if a prior period adjustment is needed, units and their auditors should use professional judgment to determine if misstatements are material.

The use of the 90-day rule should not delay issuance of the financial statements. When preparing statements units should use the best estimate of the amounts to be received. Patterns of revenues received during the current and several prior years should be studied and used as a guide. You will need to look at a pattern of sales tax refunds from prior years for routine refund amounts. The Department of Revenue has informed us they can identify units that will have unusually large refunds withheld from their mid September distributions by mid August. We will check with them at that time and alert units that are having larger refunds taken from that distribution.

All funds received during the first 90 days of the fiscal year would not be accrued as revenue at the end of the prior fiscal year. Again, GAAP requires use of an accrual period no longer than 60 days for property taxes. Also, revenues not earned by year-end would not be accrued as revenue at year-end, regardless of when received. Hold harmless revenues do not result from taxes, but are an appropriation from the State to local governments. Although these funds are received in August, they would not be recognized as revenue at June 30th because they are appropriated by the State in the 2005 fiscal year and are not earned by local units as of the end of the fiscal year.

The following table summarizes the distribution and accounting treatment of the State revenues discussed earlier in this memorandum.

Revenue Source	**Distribution Date**	**Earned?**	**Measurable?**	**Available? (Based on unit adopting 90 day period)**	**Accrued at Year End?**
Sales Tax	Mid-September	Yes	Yes	Yes	Yes
Utility Franchise Tax	Mid-September	Yes	Yes	Yes	Yes
Piped Natural Gas Tax	Mid-September	Yes	Yes	Yes	Yes
Telecommunications Tax	Mid-September	Yes	Yes	Yes	Yes
Hold Harmless Funds	Mid-August	No	N/A	N/A	No

Please contact Sharon Edmundson at 919-807-2384 with any questions you may have on this topic.