

ADMINISTRATIVE PRACTICE LETTER

SUBJECT: PREPAID EXPENSES AND DEFERRED REVENUES

Overview

The University of Maine System's audited financial statements must comply with generally accepted accounting principles (GAAP) as established by the Governmental Accounting Standards Board. In accordance with GAAP, expenses are recognized in the period for which the goods or services are received and revenue is recognized in the period in which it is earned.

In the event that goods or services are paid in advance of the fiscal year in which they are received, a '[prepaid expense](#)' is recognized. In the event that revenues are billed or collected in advance of the fiscal year they are earned, a '[deferred revenue](#)' is recognized.

Generally, prepaid expenses and deferred revenues are recorded in the current unrestricted fund in the department responsible for managing the items. A notable exception to this rule is prepaid expenses and deferred revenues associated with a project. In this case, they should be recorded as part of the project.

The University's chart of accounts contains specific account ranges for prepaid expenses and deferred revenues. Literature on the current chart of accounts can be located on the web site of the System's Office of Finance and Treasurer.

Prepaid Expenses - General

Prepaid expenses are an asset and are presented in the University's financial statements on the Statement of Net Assets. They represent the [payment](#) for goods or services in advance of receiving or using (expending) the goods or services. Prepayments sometime occur to take advantage of an offered discount; however, they typically occur because the entire invoice or contract amount is payable up front; however, the service or usage period spans more than one fiscal year. Two items that the University often prepays are airfare for athletics and software maintenance contracts.

Prepaid expenses should be identified at the time an item is paid. The portion of the payment that covers a period falling within the current fiscal year should be recorded as an expense (posted to the applicable expense account from our chart of accounts). The portion that covers a period falling within the next fiscal year or years should be recognized as a prepaid asset (account 15xxx in our chart of accounts). Once the University has entered its new fiscal year, the prepaid expense should be reversed and an expense should be recognized.

ADMINISTRATIVE PRACTICE LETTER

SUBJECT: PREPAID EXPENSES AND DEFERRED REVENUES

Illustration: On April 30, 2007 the University pays \$100,000 for a software maintenance contract that covers the period of May 1, 2007 thru April 30, 2008.

As of June 30, 2007 the \$100,000 would appear in the University's financial statements as follows:

Asset – prepaid expense	(10 months)	\$83,333
Maintenance expense	(2 months)	\$16,667

Assuming that the University does not pay for a new contract during FY08, as of June 30, 2008 the financial amounts would look as follows:

Asset – prepaid expense		\$-0-
Maintenance expense	(10 months)	\$83,333

As part of the annual year-end closing procedures, the System Accounting Department will ask the campuses to identify their prepaid expenses.

Deferred Revenues - General

Deferred revenues are a liability and are presented in the University's financial statements on the Statement of Net Assets. They represent the collection or billing of revenues in advance of earning the revenue (providing a service or goods). Once the University provides the applicable service or goods, the earned amount should be removed from the deferred revenue liability account and recognized as revenue. In the case of certain deposits (e.g., damage deposits) the University may never 'earn' the revenue. Instead, the deposits are returned to the students. In this case, simply reduce the deferred revenue account when payment is made to the student.

Examples of revenues the University typically defers include:

- [Summer session revenues](#)
- Gifts pending acceptance
- Deposits for tuition/fees, room and board, keys, damages, campus cards, etc.
- Grant and contract proceeds received in advance of grant funds being expended

With the exception of [summer session revenues](#) and grant and contract proceeds, the University should recognize deferred revenues at the earlier of billing or receipt of funds.

ADMINISTRATIVE PRACTICE LETTER

SUBJECT: PREPAID EXPENSES AND DEFERRED REVENUES

Grants and contract proceeds should be recognized as revenue as collected. As part of its year-end procedures, the System Accounting Department will identify amounts that should be deferred and post the needed adjustments.

As part of the annual year-end closing procedures, the System Accounting Department will ask the campuses to identify their deferred revenues.

Summer Session Revenues

Summer session runs from May thru August. As noted in the table below, deferral of revenue for a summer session class depends on when it begins and ends.

Class begins and ends before June 30	No deferral – recognize all billed or collected revenue in the current fiscal year
Class begins before June 30 and ends after June 30	Partial deferral – recognize part of the billed or collected revenue in the current fiscal year and defer the remainder to the next fiscal year
Class begins and ends after June 30	Full deferral – recognize all of the billed or collected revenue in the next fiscal year

The University's current student financial system (ISIS) does not provide an efficient method for identifying and deferring the appropriate amount of summer session revenues at the class level. Therefore, the System Accounting Department applies a single deferral percentage to all summer session revenues for an individual campus. Because of materiality, separate deferral percentages must be calculated for UM and USM with an average of these two being allowable for the remaining campuses. The deferral percentages are to be recalculated periodically based on an analysis of summer session class schedules unless another reasonable method is warranted.

As each campus bills and collects summer session revenues during the months of April, May, and June they should record the billed/collected revenue in the appropriate revenue accounts (tuition, fees, room and board, etc.). Prior to April of each year, the System Accounting Department will ask the campuses to identify the general ledger chart field combinations that contain their summer session revenues. At the end of April, May, and June the System Accounting Department will run a process to defer a portion of the revenues recorded in the identified chart field combinations. These deferrals will be based on the calculated percentages mentioned in the preceding paragraph. **If, however, a campus has a mechanism for identifying revenue that should be deferred at a different percentage, they should notify the System Accounting Department who will adjust their deferral process accordingly.**

ADMINISTRATIVE PRACTICE LETTER

SUBJECT: PREPAID EXPENSES AND DEFERRED REVENUES

At the beginning of the new fiscal year, the System Accounting Department will reverse the April – June deferral entries so that the previously deferred summer session revenue is recognized in the new fiscal year.

Summer Session Expenses

Summer session expenses other than salaries, wages, and benefits are deferred in the same manner as summer session revenues: the campuses will identify the chart field combinations containing the expenses and the same percentages used for deferred revenues will be used to calculate deferred expenses.

Salaries, wages, and benefits related to summer session will remain an expense of the fiscal year in which they are paid. We treat these expenses in this manner because the University has incurred an expense at the time the employee works.

At the beginning of the new fiscal year, the System Accounting Department will reverse the April – June deferral entries so that the previously deferred summer session expenses are recognized in the new fiscal year.

APPROVED:

Chief Financial Officer and Treasurer