

### ***Appendix A: OSC Guide to Utilizing the IG 2021-1 Question 5.1 Evaluation Template***

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To implement Implementation Guide 2021-1 Question 5.1, the first step needed is to determine what is considered significant<sup>3</sup>. To determine this, OSC is leveraging an evaluation template and materiality guidance developed by the UNC System, adapted for use by all state reporting entities.

This guidance and template aid in evaluating if capital outlay expenses for the fiscal year below the \$5,000 threshold are significant, and thus, should be capitalized as a grouped asset. The template helps analyze the effectiveness of the \$5,000 capitalization threshold by comparing expensed and capitalized capital outlay for the fiscal year, particularly focusing on machinery and equipment categories<sup>1</sup>.

Below is a summary of the steps that will be performed in the template.

1. Input financial data into the template and calculate the percentage of capitalized vs. expensed amounts.
2. Evaluate the capital outlay expense for significance utilizing the 80/20 rule<sup>2</sup>. The evaluation template automates these calculations based on financial data, materiality, and risk tolerance.
3. Determine if there is significant error by reviewing template results.
  - a. if the machinery and equipment capitalized is less than 80% of the total capital outlay and the remaining portion exceeds the selected materiality, an error exists (i.e. adjustments should be made to capitalize expensed amounts until they fall below the significant threshold).
  - b. As part of this step, you will identify what expensed capital outlay minor category should be reported as a grouped asset.
4. Determine additional information about the grouped asset(s), such as the number of lookback periods (only applicable in the first year of implementation) and useful lives of the grouped assets.
5. Analyze template calculated adjustments and record the grouped asset(s), depreciation amounts, write-offs and other adjustments for the previously expensed capital outlay acquisitions.

While the template and task of evaluating your expensed capital outlay may initially appear overwhelming, rest assured that the template automates the computations and analysis of most of the required information. By utilizing this template, you will find that many of the intricate calculations, assumptions, and assessments are handled seamlessly, allowing you to focus your efforts on interpreting the results and making informed decisions.

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To further assist with this evaluation, below you will find:

- general considerations all reporting entities should consider as they complete their evaluations.
- step by step guidance to completing the threshold evaluation template by reporting entity types.
- an FAQ and glossary of useful terminology.

### **General Considerations for All Reporting Entities**

**<sup>1</sup> Evaluating Capitalization Thresholds by Major Asset Categories:** From OSC's and UNC System office's evaluations and analysis, we determined the most likely area in which we are not capturing a significant<sup>3</sup> portion of grouped assets below the capitalization threshold is equipment. Therefore, all state reporting entities releasing standalone financial statements should evaluate the effectiveness of their capitalized equipment assets.

When we reviewed the other major asset categories, like buildings, general infrastructure, and computer software, we determined the likelihood of this new requirement being significant<sup>3</sup> in these categories is highly unlikely. Therefore, the template is currently designed to evaluate the equipment asset minor categories. However, if there is another asset category you are concerned with, state entities should use their professional judgment and perform an evaluation like this approach for equipment assets. For the most accurate restatements and assessments, major asset categories should not be combined when completing the evaluation.

**Grouped Asset Threshold:** OSC will not be setting a dollar threshold in relation to the implementation of Implementation Guide 2021-1, Question 5.1. Rather, state reporting entities should perform an evaluation to determine when the aggregate of assets having an estimated useful life of more than one year that are below the \$5,000 threshold and not considered repair and maintenance costs are considered significant<sup>3</sup> and should be collectively capitalized on the financial statements.

OSC has updated its capital asset policy 102.1 – Statewide Accounting Policy – Capitalization/Classification to reflect this. Additionally, the following language will be added to the State's ACFR Note 1: Summary of Significant Accounting Policies:

*In addition, assets having an estimated useful life of more than one year that are below the \$5,000 threshold and not considered repair or maintenance costs are collectively capitalized on the financial statements when the aggregate of those assets are considered significant.*

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**Review of expensed items:** Before using the template to perform your evaluation, entities should review and analyze the data that represents the accounts with expenses for capital outlay under the capitalization threshold by major category type. The activity in these accounts should only include capital outlay purchases that would have been capitalized if not for the threshold amount and exclude purchases of library books, art, artifacts, library databases/e-journals, software, leases, SBITAs, intangible assets repairs/maintenance, and/or supplies. If there is evidence of significant<sup>3</sup> amounts that should be excluded, these should be subtracted from the total capital outlay expenses. Moving forward, it is important to continue to accurately report only capital outlay expenses in these accounts to ensure accurate results from the evaluation.

**Retrospective application & Lookback periods:** When reporting entities are considering their lookback periods, we recommend starting with a 4 to 5 year look back period for evaluation purposes. Then adjust as necessary depending on the results of the evaluation, the types of equipment categories being evaluated and adjusted, and determine any adjustments. For example, if computer equipment (which has a shorter useful life than other types of equipment) makes up most of your grouped asset adjustments, the restatement lookback period may be limited to just 4 years as looking back beyond this would have diminishing benefits and/or would not be significant<sup>3</sup> to the restated net position. State reporting entities should document and explain the reason for the look back period selected (note there is a section on the Data Sheet tab in the Evaluation Threshold template).

**Prospective periods:** For fiscal years 2024 and forward, state reporting entities should continue to evaluate the effectiveness of your capitalization thresholds. As the years progress, state reporting entities should begin to sense what is necessary to ensure there are no significant<sup>3</sup> grouped assets not capitalized. Thus, throughout the year, state reporting entities can capitalize grouped assets/purchases as they happen instead of at year-end.

### **Primary Government Reporting Entities (Governmental and Proprietary Funds)** **Implementation**

Since most primary government reporting entities do not issue standalone financial statements, OSC performed a primary government evaluation for the governmental funds and individual proprietary funds for the current year and retrospective application. OSC will be providing the steps and entries needed to be completed in the NCFs fixed asset module for agencies with significant<sup>3</sup> inventoried assets.

Beginning July 1, 2024, state agencies should capitalize grouped purchases that management considers significant<sup>3</sup>. Additional guidance will be published in Appendix B for the steps needed to be completed going forward. In future year-ends, OSC will continue to evaluate and analyze if the effectiveness of our capitalization thresholds for the equipment classification and determine if any additional capital outlay expenses are significant.

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### **Component Unit Reporting Entities Implementation**

Component Units of the State of North Carolina (University System, Community Colleges, and Nonmajor Component Units) should complete an evaluation to determine if each individual CU has significant<sup>3</sup> capital asset grouped purchases that should be capitalized with this implementation. Below you will find step by step guidance to completing the threshold evaluation template.

Note: while the nonmajor component units of the state do not have to report details of their capital assets to OSC for ACFR purposes, they should still perform an evaluation and analyze the effectiveness of their thresholds for the capitalization of equipment classification.

Component units of the state will need the following sources of information and data to perform the evaluation:

- Year-end financial statement trial balance accounts for expensed capital assets. In the State of NC's Chart of Accounts, this activity should be reported in the capital outlay caption (accounts 54xxxxxx).
- Capital asset additions and the support used in the capital asset note disclosures.
- Year-end financial statement data to help determine materiality<sup>4</sup> and significant<sup>3</sup> amounts.
- IG 2021 Question 5.1 Evaluation Template.

Before starting on the steps below, we recommend you take some time to also read the Procedural Guidance Tab in the Evaluation Template. This tab also provides a general overview of what each tab (Data Sheet, CY Template, Restatement Template, and Adjustment Tab) in the workbook represents.

#### **Step 1: Inputting information into the template**

1. Our first step is to input data into the Data Sheet tab for equipment amounts expensed/not capitalized, capital asset note additions and financial statement data. This detail should be found in your trial balance accounts for expensed equipment assets (capital outlay accounts 54xxxxxx); your audited financial note disclosure for equipment capital asset additions; and your audited financial statements.

##### *Section 1 on Data Sheet Tab – Equipment/Machinery Capital Outlay Expenses:*

- a. By each fiscal year, this information should be inputted to section 1 on the Data Sheet tab of the evaluation template lines 6 to 10; additionally, the template is set up to evaluate the minor asset categories of equipment. The lookback period in the template is 6 years; if an entity needs more than this, please contact OSC. Additional details can be found in the General

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Considerations, Retrospective application & Lookback periods section of this document.

- b. If you determine there are expenses reported in your capital outlay accounts that do not meet the definition of a capital asset except for the capitalization threshold, you can remove those amounts from the total capital outlay expense. Those amounts should be added to line 11 below. Additionally, a note/rationale for exclusions should be added to the comments box on line 3. For example, if you are reviewing the capital outlay expense caption for laptops and determine within this account you have recorded laptops as well as flash drives, you would want to exclude the portion related to flash drives as this does not meet the definition of a capital asset; the flash drive should be reported in supplies and materials account.

### *Section 2 on Data Sheet Tab – Equipment/Machinery Capital Outlay Capitalized:*

- c. By each fiscal year, input amounts reported as capital asset additions for the major asset category machinery and equipment on line 15.

### *Section 3 on the Data Sheet Tab – Amounts Reported in the Financial Statements:*

- d. By each fiscal year, input amounts reported from your audited financial statements. The prior year balances may be used as an estimate for the current fiscal year until current fiscal year amounts are available. This should be inputted to lines 19 to 22.
  - i. This information is needed to automate the materiality<sup>4</sup>calculations in the evaluation template.

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	A	B	C	D	E	F	G	H	I	J
	Comments on Excluded Amounts and Estimated Amounts:									
3										
4		Current Year	June 30, 2023	Look Back Period						
5										
6										
7										
8										
9										
10										
11										
12										
13										
14	<b>1c Section 2 - Equipment/Machinery Capital Outlay Capitalized:</b>									
15										
16										
17	<b>Section 3 - Amounts Reported in the Financial Statements</b>									
18	Only the Current Year and Prior Year (FY2023) amounts are necessary. FY2023 balances may be used as an estimate for FY2024 until the FY2024 amounts are available. If "Error" is indicated, review the revenue and expense inputs for errors.									
19										
20										
21										
22										
23										
24										

### Step 2: Evaluation Procedures

2. The next step is to evaluate the effectiveness of the threshold amount for machinery and equipment based on the 80/20 rule<sup>2</sup> with the following steps using the CY Template and Restatement Template Tabs:
  - a. Select the materiality<sup>4</sup> amount for the evaluation of the effectiveness of the threshold amount to determine significance based on the 80/20 in cell A22 on both the CY Template and Restatement Template tabs. Additional materiality<sup>4</sup> guidance on selecting this can be found in the FAQ section of this document.
  - b. Select your qualitative risk factor<sup>5</sup> in cell C34 on both the CY Template and Restatement Template tabs. Additional qualitative risk factors guidance on selecting this can be found in the FAQ and Glossary of Useful Terminology section of this document.
    - i. Both selections in 2a and 2b above will impact the dollar amount that is considered significant. The lower the amount in cell C22, the more conservative your approach will be for this evaluation and implementation. When using professional judgment to make these selections, the amount used should explain the underlying reasons for

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using the different amount and may include cost/benefit decisions as well as other qualitative concerns and considerations.

- c. Once these selections have been made, the template will compare the selected materiality<sup>4</sup> amount to the 80% of total acquisitions of machinery and equipment (i.e. machinery and equipment additions plus expensed amount). The difference between these two is calculated on line 24 of the CY Template and Restatement Template Tab. Cell C25 returns a yes or no value for whether the amount below 80% is greater than the significant amount.
- If cell C25 is **yes**, the entity should make adjustments to record grouped capital assets or potentially go back to the data sheet to consider modifying the exclusions.
  - If cell C25 is **no**, then the entity has no significant assets below the threshold that should be capitalized, meaning no adjustment is needed and can stop the evaluation.

Step 2 - Evaluation Procedures:		
13	This step provides for the evaluation of the effectiveness of the threshold amount for machinery and equipment based on the 80/20 rule. The significant amounts for the evaluation are determined by making a selection in the drop down boxes in cells A22.	
14		
15	(1) Evaluation of the Effectiveness of the Threshold Amount to Determine Significant Capital Machinery and Equipment Assets Based on the 80/20 rule	
16	Machinery and Equipment Additions Reported in the Capital Asset Note (Data Sheet, Section 2)	15,343,708
17	Total Acquisitions - Machinery and Equipment Additions Plus Expensed Amounts	28,485,580
18	% Capitalized	54%
19	% Capitalized below the 80%	26%
20	Amount below the 80%	7,444,756
21	Select the materiality amount for the evaluation of the effectiveness of the threshold amount to determine significance based on the 80/20 rule in the A22 drop-down box.	
22	2a CSV	Conservative Significant Variance Amount 4,332,142
23	2c	
24	Difference in the amount below 80% (row 20) and the significant amount (row 22)	3,112,614
25	Is the amount below 80% (row 20) greater than the significant amount?	Yes
26	If Column C row 25 is: Significance amount or go to the Data Sheet and consider modifying exclusions and/or determine the adjustment necessary to record grouped capital assets under the capitalization threshold. No, adjustment is not necessary, stop	
27		
28		
29	Step 2a - Information Needed for Calculating the Materiality Amount (Amounts Linked to the Data Sheet Tab):	
30	The Financial Statement Information is entered on the Data Sheet, Section 3. For more on calculating materiality see the UNC System BPCP Procedural Guidance for Year End Planning and Procedures for Financial Reporting.	
31	Total Assets on the Financial Statements	2,282,267,047
32	Total Operating and NonOperating Revenue	825,169,979
33	Total Operating and NonOperating Expenses	704,614,331
34	2b Qualitative Risk Factor	70%

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### Step 3: Determining the Significant Error Amount and Making Corrections:

3. Once you determine you have a significant error amount (cell C25 is yes on the CY Template and/or Restatement Template tab), complete the following procedures/steps, which can be found on the Data Sheet tab, Section 4:
  - a. Determine the group(s)/layered group(s) that are significant to the reclassification adjustment.
  - b. Based on Step 2 evaluation template results, address the significant amount of expensed capital outlay. As necessary, obtain the detail transaction reports/analysis of the group(s)/layered group(s) for which adjustment is considered necessary.
    - i. If it is not too administratively burdensome, you should identify large, grouped purchases near the same time for a single purpose and record that grouped asset in your asset management system.
    - ii. If it is too burdensome to identify large, grouped asset purchases, you may use what we are calling a layered approach and apply a composite depreciate rate for each layered group of assets. So, for example, if we analyzed computer/EDP equipment and machinery and equipment and found we have significant errors but can't administratively distinguish large, grouped asset purchases for previous years, you could use this layered group approach on these large account classes and apply that composite depreciation rate for each group.

Review the underlying transactions of the group accounts to understand the activities recorded and identify the transactions considered significant to the reclassification. Your review should also ensure that the adjustment amounts only include capital outlay purchases that would have been capitalized if not for the threshold amount.

- c. If amounts are discovered that should be excluded, summarize and update the exclusion line in this Data Sheet and go back to the evaluation template to see if a significant amount of expensed capital outlay still exists.
- d. If adjustments are made based on step 3c and the evaluation template continues to indicate that a significant amount of expensed capital outlay exists, enter the adjustment amounts in Section 4 of the Data Sheet tab.
  - i. Adjust the group layer names for each group minor machinery and equipment type on the respective lines (rows 34 to 47).

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- ii. Enter the adjustment amounts for each group layer; for the current year, enter the amounts in column B; for the restatement adjustments, enter the amounts as necessary in columns E to J.

Note: Adjustments do not need to be made for each equipment group identified and evaluated in step 1a. Rather you only need to make adjustments to meet what was deemed significant. We recommend starting with the machinery and equipment layered groups with the shortest useful lives, such as computer equipment, to minimize the lookback period.

	A	B	C	D	E	F	G	H	I	J
25	<b>Before completing Section 4 - Complete the YE and Restatement Template.</b>									
26	<b>Section 4 - Adjustments for Significant Amounts</b>									
27	<b>Based on the results of the evaluation in the CY and Restatement Template tabs, if adjustments are necessary complete the following procedures/steps and initial/check column "J"</b>									
28	4.1 Determine the group(s)/layered group(s) that are significant to the reclassification adjustment.									
29	4.2 Based on Step 2 evaluation template results and instructions on line 27 of the Template, address the significant amount of expensed capital outlay. As necessary, obtain the detail transaction reports/analysis of the group(s)/layered group(s) for which adjustment is considered necessary. Review the underlying transactions of the group accounts to understand the activities recorded and identify the transactions considered significant to the reclassification. Your review should also ensure that the adjustment amounts only include capital outlay purchases that would have been capitalized if not for the threshold amount.									
30	4.3 If amounts are discovered that should be excluded, summarize and update the exclusion line in this Data Sheet and go back to the evaluation template to see if a significant amount of expensed capital outlay still exist.									
31	4.4 If the evaluation template continues to indicate that a significant amount of expensed capital outlay exist, follow the instructions on line 27 of the Template to address the significant amount. If adjustments are to be recorded, enter the adjustment amounts in the data entry worksheet below.									
32		Current Year	June 30, 2023	Restatement Adjustment Amounts by Year Acquired						
33	<b>NOTE: DO NOT ADD OR DELETE ROWS 34 through 48 3di</b>	FY2024 (Use FY23 until FY24 is ready)	Restatement Cumulative Amount	FY2023	FY2022	FY2021	FY2020	FY2019	FY2018	
34	<b>Group 1 - EDP Equipment (IT)</b>									
35	a. PC/Workstation/Printer Equipment Non-Cap		-							
36	b. Electronic Data Processing Equipment Non-Cap		-							
37	<b>Group 1 Total</b>	-	-	-	-	-	-	-	-	-
38	<b>Group 2 - Furniture/ Equipment</b>									
39	Audio-Visual Equipment Non-Cap	-	-							
40	<b>Group 3 - Other Furniture/ Equipment</b>									
41	a. Residential/Dorm Furniture Non-Cap	-	-							
42	b. Science Equipment Non-Cap	-	-							
43	c. Athletic Equipment Non-Cap	-	-							
44	d. Office Furniture / Equipment	-	-							
45	<b>Group 3 Total</b>	-	-	-	-	-	-	-	-	-
46	<b>Group 4 - Motor Vehicles</b>									
47	Motor Vehicles Non-Cap	-	-							
48										
49	<b>Total All Groups</b>	-	-	-	-	-	-	-	-	-

- e. Once adjustments have been made, return to the CY Template and Restatement Template tabs to re-evaluate whether the adjustments made address the amount that was previously identified as significant. Step 3 – Closing Review Procedures on these tabs is an update to the initial evaluation performed in Step 2 so that you can determine the adjustment outcomes meet your expectations.

- i. If cell C80 is “No”, then no additional modifications are needed to the adjustments made on the Data Sheet Section 4.
- ii. If cell C80 is “Yes”, either adjust the significant amount, add additional adjustments to the Data Sheet Section 4, and/or modify your

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exclusions as discussed in step 1b. This should be done until cell C80 is “No”.

Note: The percentage capitalized may be under the 80% level, but the amounts expended and amounts under the 80% should not be more than the significant materiality<sup>4</sup>amount.

	A	B	C
67		<b>Step 3 - Closing Review Procedures:</b>	
68	This step provides for a review after applying adjustments for amounts under the threshold. This review provides an update to the initial evaluation in step 2 so that you can determine that the adjustment outcomes meet your expectations. The % capitalized may be under the 80% level but the amounts expended and amounts under the 80% should not be more than the significant materiality amount.		
69		Machinery and Equipment Additions Reported in the Capital Asset Note before Adjustment (row 16)	47,665,423
70		Total Acquisitions - Machinery and Equipment Additions Plus Expensed Amounts (row 17)	91,154,014
71		<b>Adjustments for Machinery and Equipment Additions Under the Capital Asset Threshold (From Data Sheet, Section 4)</b>	<b>16,239,436</b>
72		Adjusted Acquisitions - Machinery and Equipment Additions Plus Adjustment for Significant Amounts	63,904,859
73		Adjusted Expensed Machinery and Equipment	27,249,155
74		<b>% Capitalized (After Adjustment)</b>	<b>70%</b>
75		<b>% Capitalized below the 80% (After Adjustment)</b>	<b>10%</b>
76		<b>Amount below the 80% (After Adjustment)</b>	<b>9,018,353</b>
77			
78	(1) Evaluation of the Effectiveness of the Threshold Amount to Determine Significant Capital Machinery and Equipment Assets Based on the 80/20 rule		
79	<b>ATM</b>	<b>Auditor Trivial Misstatement Amount</b>	<b>11,411,335</b>
80		<b>Is the amount below 80% after adjustment (row 84) greater than the significant amount?</b>	<b>No</b>
81		<b>If Yes, what additional adjustment is needed?</b>	<b>-</b>
82			
83	If Column C row 80 is: Yes, either adjust the significant amount or go to the Data Sheet and consider modifying exclusions and/or the adjustment to ensure that the row 80 is "No". No, modification to the adjustment is not necessary, stop		

### Step 4: Determining the Look Back Period for Restatement Purposes and the Useful Lives of the Groups/Layered Groups

4. Based on the adjustments entered in step 3dii in section 4 of the Data Sheet, entities should identify what the look back period should be for the restatement in years as well as the depreciable lives of the groups/layered groups. You may consider the major layered group years and the diminishing effect of older years especially beyond 4 to 5 years where the aggregate depreciation remaining for those older years at June 30, 2023, is not significant.
  - a. The number of look back years should be entered in cell J52 in Section 5a of the Data Sheet tab.
  - b. Enter an explanation for the lookback period on row 53.
  - c. In section 5b, entities should review and modify as necessary the useful lives by group on rows 58 to 69. Note, you must show an amount for each group to avoid calculation errors on the Adjustment tab.

Some additional considerations: Depreciation may be based on an estimate of the useful life of assets for the group/layered group assets using the simple average or weighted average methods. When considering the useful lives of a group, you should consider your policy for removal and replacement of the assets and its history of

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removal/replacement. The depreciation rate may differ from the rates established for threshold assets since assets below the threshold are being grouped/layered in reporting units. Since the individual assets recorded as a group / layered group are not trackable they are subject to write off procedures when fully depreciated. However, depreciation rates should be within the depreciation ranges established by the Office of State Controller.

For the look back period, start with 4 years and adjust, if necessary, depending on the results of the evaluations and determination of adjustments. Record and explain the reasons for the look back period in the Data Sheet Tab. If considered reasonable, the restatement lookback period may be limited to 4 years when the computer equipment group makes up a majority of the total group adjustment dollars and looking beyond 4 years would have diminishing benefits and/or would not be significant to the restated net position. When the look back period becomes burdensome and difficult and not considered practicable, document the reasons and disclose in the notes to the financial statements.

In the template, the half-year convention is used for calculating depreciation in the first and last year of the layered group asset life.

Based on your removal/replacement period policy and the lack of tracking individual group assets separately, the group acquisitions under the capitalization threshold may be written off in the year they become fully depreciated. When the removal/replacement period changes, the entity should evaluate and make appropriate changes based on the GASB standards for accounting changes.

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	A	B	C	D	E	F	G	H	I	J
50	<b>Section 5 - Determining the Look Back Period for Restatement Purposes and the Useful Lives of the Groups / Layered Groups</b>									
51	<b>Section 5a - Determining the Look Back Period for Restatement Purposes</b>									
52	Based on the adjustments above and review of the Analysis of the Groups / Group Life's / Adjustment Amounts in the Adjustment Tab, what is the look back period for restatement in years? You may consider the major layered group years and the diminishing effect of older years especially beyond 4-5 years were the aggregate depreciation remaining for those older years at June 30, 2023, is not significant. (Explain basis for look back period below)									<b>4a</b>  4
53	4b The layered group is only for group 1 - EDP Equipment, the majority which is for PCs and as a layered group am using 4 years for the look back period.									
54										
55	<b>Section 5b - Determining the Depreciable Life of Groups / Layered Groups (enter number of months for each sub-group)</b> You have to show an amount for each group to avoid calculation errors in the Adjustment Tab. The lives shown are for example only, modify based on your institution's determination of the group life. Before competing, test each group simple average total calculation amount to ensure it is correct. Adjust the calculations as necessary.									
56										
57	<b>Group 1 - EDP Equipment (IT)</b>		<b>4c</b>							
58	a. PC/Workstation/Printer Non-Cap			48						
59	b. EDP Equipment Group			48						
60	<b>Group 1 Simple Average Mths</b>			48						
61	<b>Group 2 - Educational Furniture/ Equipment )</b>									
62	Audio-Visual Equipment Non-Cap			72						
63	<b>Group 3 - Other Furniture/ Equipment</b>									
64	a. Office/Residential/Dorm Furniture Non-Cap			144						
65	b. Science Equipment Non-Cap			96						
66	c. Athletic Equipment Non-Cap			120						
67	<b>Group 3 Simple Average Mths</b>			120						
68	<b>Group 4 - Motor Vehicles</b>									
69	Motor Vehicles Non-Cap			72						
70										
71	<b>Total Groups Simple Average</b>			78						

### Step 5: Computation of Depreciation Amounts, Write Offs and Adjustments for the previously expensed capital outlay acquisitions.

5. Now that you have determined the necessary adjustments needed to address the significant capital outlay previously expensed, the adjustment tab should be used to help compute the depreciation amounts, write-offs and journal entries needed to be done.
  - a. Adjustment worksheet 3 on the Adjustment tab provides automated amounts dependent on the information you entered in section 4 (adjustments for significant amounts), 5a (lookback period), and 5b (useful lives by group) of the Data sheet for the restatement amounts.
    - i. Section 3a.1 provides details of the annual depreciation schedule related to the restatement lookback periods.

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Adjustment Worksheet 3a - Computation of Depreciation Amounts, Write Offs and Adjustments for the < 5000 Acquisition Restatement Amount (Unhide rows 29 - 176)											
3a.1 Annual Depreciation and Depreciation Schedule for < 5000 Acquisition Restatement Amount (Unhide rows 30 - 132)											
Groups	Depr Rate	1/2 Depr Rate	Total	FY23	FY22	FY21	FY20	FY19	FY18		
Group 1 - EDP Equipment (IT)	25.0%	12.5%	4,059,859	1,252,163	1,085,456	835,830	886,409	-	-	-	-
Group 2 - Educational Furniture/ Equipment )	16.7%	8.3%	-	-	-	-	-	-	-	-	-
Group 3 - Other Furniture/ Equipment	10.0%	5.0%	-	-	-	-	-	-	-	-	-
Group 4 - Motor Vehicles	16.7%	8.3%	-	-	-	-	-	-	-	-	-
<b>Total Groups</b>			<b>4,059,859</b>	<b>1,252,163</b>	<b>1,085,456</b>	<b>835,830</b>	<b>886,409</b>				
Combined Groups: (Unhide rows 39 - 60)											
Restatement Amount			16,239,436	5,008,653	4,341,824	3,343,321	3,545,637	-	-	-	-
Annual Depreciation			4,059,859	1,252,163	1,085,456	835,830	886,409	-	-	-	-
FY 18			-	-	-	-	-	-	-	-	-
FY 19			-	-	-	-	-	-	-	-	-
FY 20			443,205	-	-	-	443,205	-	-	-	-
FY 21			1,304,325	-	-	417,915	886,409	-	-	-	-
FY 22			2,264,968	-	542,728	835,830	886,409	-	-	-	-
FY 23			3,433,777	626,082	1,085,456	835,830	886,409	-	-	-	-
Total as of June 30, 2023			7,446,274	626,082	1,628,184	2,089,576	3,102,433	-	-	-	-
Net Book Value / Remaining Depr at June 30, 2023			8,793,162	4,382,571	2,713,640	1,253,745	443,205	-	-	-	-
FY 24			3,616,654	1,252,163	1,085,456	835,830	443,205	-	-	-	-
FY 25			2,755,534	1,252,163	1,085,456	417,915	-	-	-	-	-
FY 26			1,794,891	1,252,163	542,728	-	-	-	-	-	-
FY 27			626,082	626,082	-	-	-	-	-	-	-
FY 28			-	-	-	-	-	-	-	-	-
FY 29			-	-	-	-	-	-	-	-	-
FY 30			-	-	-	-	-	-	-	-	-
FY 31			-	-	-	-	-	-	-	-	-
FY 32			-	-	-	-	-	-	-	-	-
FY 33			-	-	-	-	-	-	-	-	-
Total			16,239,436	5,008,653	4,341,824	3,343,321	3,545,637	-	-	-	-
Remaining Book Value			(16,239,436)	-	-	-	-	-	-	-	-

ii. Section 3a.2 provides the schedule of write-offs related to the restatement amounts.

3a.2 - Schedule of Write Offs for < 5000 Acquisition Restatement Amounts (Unhide rows 135 - 166)											
Group 1 - EDP Equipment (IT)											
FY24			3,545,637				3,545,637				
FY25			3,343,321								
FY26			4,341,824		4,341,824						
FY27			5,008,653	5,008,653							
FY28			-								
FY29			-								

iii. Section 3a.3 provides the restatement adjusting entry related to the retrospective application of this standard.

3a.3 - June 30, 2023 < 5000 Acquisition Restatement Adjusting Entry (Unhide rows 169 - 176)											
Restatement Adjustment:			DR	CR							
Equipment Capital Assets < 5000 (G1 FY23 Restatement)			16,239,436								
Equipment Capital Assets < 5000 (G2 FY23 Restatement)			-								
Equipment Capital Assets < 5000 (G3 FY23 Restatement)			-								
Accum Deprec - < 5000 (G1 FY23 Restatement)					7,446,274						
Accum Deprec - < 5000 (G2 FY23 Restatement)					-						
Accum Deprec - < 5000 (G3 FY23 Restatement)					-						
Net Position					8,793,162						
			16,239,436		16,239,436						

b. Adjustment worksheet 4 on the Adjustment tab provides automated amounts dependent on the information you entered in section 4 (adjustments for significant amounts) and 5b (useful lives by group) of the Data sheet for the current year.

- i. Section 4a.1 provides details of the annual depreciation schedule related to the current year.
- ii. Section 4a.2 provides the schedule of write-offs related to the current year.
- iii. Section 4a.3 provides the adjusting entry related to the current application of this standard. Note, this entry also accounts for the write-offs and depreciation necessary from the retrospective application identified in section 3 of the Adjustment tab.

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		4a.3 - < 5000 Acquisition Current Year (FY2024) Adjusting Entry (Unhide rows 283 - 296)			
Adjustment:		DR		CR	
284	Equipment Capital Assets < 5000 (G1 FY23 Restatement)				3,545,637
285	Accum Deprec - < 5000 (G1 FY23 Restatement)		3,545,637		3,616,654
286	Accum Deprec - < 5000 (G2 FY23 Restatement)				-
287	Accum Deprec - < 5000 (G3 FY23 Restatement)				-
288	Equipment Capital Assets < 5000 (G1 FY24)		5,008,653		
289	Equipment Capital Assets < 5000 (G2 FY24)		-		
290	Equipment Capital Assets < 5000 (G3 FY24)		-		
291	Accum Deprec - < 5000 (G1 FY24)				626,082
292	Accum Deprec - < 5000 (G2 FY24)				-
293	Accum Deprec - < 5000 (G3 FY24)				-
294	Supplies, Materials and Services Expense				5,008,653
295	Depreciation Expense		4,242,736		
296			12,797,026		12,797,026

The information in both sections 3 and 4 should be used to record the necessary adjustments in your accounting systems to properly account for the adjustments to your note disclosures for capital assets and your financial statements. Before making the adjustments, you will need to review and ensure amounts linked are accurate and reliable for your entity and to adjust if necessary for errors detected. For example, verify the template has adequately used the correct useful lives for the grouped assets selected.

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### FAQ and Glossary of Useful Terminology

#### **<sup>2</sup>What is the 80/20 Rule?**

The 80/20 rule is a principle that suggests that roughly 80% of effects come from 20% of causes. This principle is also referred to as the Pareto principle. Management often uses this principle to establish a threshold to reduce cost/effort considered excessive for the administration/control/accounting of capital assets. Using this principle, management asserts that the threshold established will provide 80% of the total value of capital assets acquired based on 20% of the individual capital assets acquired. In other words, that 80% of the individual capital assets under the threshold, in the aggregate would not be significant to the 20% value reported. However, the use of such a threshold has limitations especially when considering that sometimes many individual items considered small and under the threshold can in the aggregate rise to a significant value. Therefore, when using a threshold, an evaluation should be made to ensure that the established threshold is effective. For financial reporting, the effectiveness of the threshold measures (1) if the threshold results in the 80/20 expectation and (2) if the 80/20 rule results show that capital assets under the threshold or expensed are in the aggregate not considered significant.

#### **<sup>3</sup>What is Considered Significant?**

In financial reporting, “significant” refers to information or events that are critical to influencing decisions of users of the financial statements. When applying the 80/20 rule to this evaluation, significant items are those that represent approximately 20% of the transactions or data points that account for roughly 80% of the impact on financial outcomes. This principle, along with assessing risk and using the financial statement materiality<sup>4</sup> selections, will help determine what is significant for this implementation. The evaluation template provides for the automated calculation of the significant amount based on the financial statement information entered and selected in the template.

#### **<sup>4</sup>Understanding materiality and calculation of materiality using your financial statements**

Materiality is a key accounting principle that determines whether a discrepancy, such as an omission or errors, would impact or influence a reasonable user’s decision making. For this evaluation, materiality is determined based on management’s professional judgement on what omissions or errors would be considered tolerable.

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Materiality is not only a consideration for omissions and errors, but also a factor when setting accounting policies. While management strives to record all relevant transactions and adjustments, the use of materiality is essential when faced with timing issues, limited resources, unplanned issues, and when uncertainty arises, a decision must be made as to what is important or not. In making those types of decisions, establishing and defining what is material provides management control over the process to ensure that the financial statements will be materially correct and issued timely.

In developing the materiality methodology for use by the financial statement preparer, due care must be given to ensure that its results will be conservative in relation to the materiality decisions made by the auditors. Additionally, it is important for the financial statement preparer to understand the related qualitative risk factors, as auditors consider these factors when evaluating the risk of misstatement or omissions together with materiality. This understanding ensures that management has taken a conservative approach to ensuring the financial statements are materially correct, considering those factors. A conservative approach should result in materiality amounts that are significantly lower than what the auditors consider material in the audit of the financial statements.

The guidance and calculations in the evaluation template for materiality look at total revenues, expenses, and total assets. If the total assets are less than either the total revenues or total expenses, then total assets are used as the basis for calculating materiality. If the total assets are greater than either the total revenues or total expenses, then the greater of total revenues or total expenses is used as the basis for calculating materiality.

Entities should choose the materiality amount that best meets their tolerance level for uncorrected errors including consideration of the cost/benefit related to the effort to correct the errors. The evaluation template provides automated calculations of the significant amount based on the financial statement information. Both conservative and audit calculation amounts are provided in the template. Below are the following definitions related to the materiality considerations and calculations:

- a. **Auditor Overall Materiality (AOM):** is used by the auditors to assist in the development of the audit plan and procedures necessary to issue an opinion on the accuracy of amounts reported in the financial statements. Like the auditor, you can use overall materiality to assist in developing the year end plan and procedures necessary to ensure accuracy in the preparation of the financial

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statements and to determine significance of amounts reported and related adjustments, accounting changes and variances.

For the AOM measurement, the evaluation template uses 5% of total Assets or the greater of Revenues or Expenses, whichever is lower. For the **Conservative Overall Materiality (COM)** measurement, the evaluation template is 3% of total Assets or the greater of Revenues or Expenses, whichever is lower.

- b. Auditor Performance Materiality (APM):** is used by auditors to evaluate whether the financial statements are materially correct or misstated. In developing this amount, auditors reduce the overall materiality amount based on qualitative risk factors associated with the specific audit engagement. If the auditor's field work finds that the aggregate of known uncorrected misstatements exceeds this amount, they would conclude that the financial statements are materially misstated. Such a condition would generally preclude the auditor from rendering an unmodified opinion unless correction(s) are made. This final evaluation is done using performance rather than overall materiality to account for the risk of further undetected misstatements. Likewise, management may use this amount to determine the aggregate amount of misstatement or omission that would be considered material to the reporting of the financial statements and that would require corrections.

For the APM measurement, the evaluation template takes the AOM and multiplies it by the selected qualitative risk factor<sup>5</sup>, either high (50%), medium (70%), or low (90%). It should be noted that medium risk is the general risk factor selected by the state of NC entities. For the **Conservative Performance Materiality (CPM)** measurement, the evaluation template takes the COM and multiplies it by the selected qualitative risk factor.

- c. Auditor Trivial Misstatement Amount (ATM):** is used by auditors as the cutoff point to determine whether they are required to propose a correction of a given misstatement or omission. Likewise, management may use this amount to determine the amount of a given misstatement or omission that, when above this amount, will result in a financial statement correction/adjustment.

For the ATM measurement, the evaluation template takes the AOM and multiplies it by 10%. For the **Conservative Trivial Misstatement Amount (CTM)** measurement, the evaluation template takes the COM and multiplies it by 10%.

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- d. Conservative Significant Variance Amount (CSV):** This may be used when evaluating significant changes including the comparison of current and prior year financial statement account balances and disclosures. The determination and evaluation of significant variances is key to ensuring that changes on the financial statements and disclosures from one year to the next are understood, explainable and materially accurate. A significant variance amount is generally used together with a 15% change in the balances to ensure that the review is efficient and effective on the account being reviewed. For this evaluation template, CSV is computed by taking CPM and multiplying it by 25%.
  
- e. Professional Judgement (PJ):** This may be used by management by selecting an amount not determined from the calculations above. If used, management should apply relevant training, knowledge, and expertise in making an informed decision on the amount deemed significant for this implementation and explain the rationale for using this amount.

### **<sup>5</sup>What are qualitative Risk Factors and how should I select the correct qualitative risk factor for my reporting entity?**

Qualitative factors related to implementing a standard begin with understanding the nature of the changes being made by the new standard and the probable effect and importance of those changes to the financial statements. Some standards introduce new requirements to financial statements that may be more discrete or noticeable. The more noticeable a new requirement is on the financial statements, the greater the qualitative factor is.

The following guidance provides a definition for determining High, Medium, and Low qualitative risk conditions related to the risk of misstatements and omission and their effect on materiality measurements:

High Qualitative Risk – Is a condition that exists when internal controls may not be sufficient to timely detect errors or omission that could be material to the amounts and disclosures reported on the financial statements. This condition could be caused by internal controls significantly affected by change during the year, and/or there is a history of prior period internal control or management issues, and/or resources provided by management are limited to effectively monitor and/or document monthly and/or year-end activities. Where qualitative risk is assessed as High, it is recommended that 50% be used for determining Performance Materiality. However, professional judgment may be used.

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Medium Qualitative Risk – is a condition that exists when internal controls may be considered acceptable to timely detect error or omissions that could be material to the amounts and disclosures reported on the financial statements; but, there are indicators that raise qualitative risk such as the need for improvements related to the efficiency and effectiveness of related year end processes, including the documentation of year end tasks, procedures, and persons performing work and reviewing work, as well as the complexity of the accounting and reporting environment, and the impact of external entity financial statements. This condition could also be caused by moderate change risk during the year that is still a factor, and/or observations or improvements that have been recommended either internally or externally related to the internal controls over financial reporting. Medium qualitative risk is a qualitative risk that is less than High but greater than Low. Low qualitative risk may not be assessed unless controls are without question or concern relative to their ability to timely detect and correct errors or omission that may be material to the financial statements. We will refer to this in the guidance as the “exceptional rule”. Where qualitative risk is assessed as Medium, the percentage used for Performance Materiality may be adjusted to 70%. In addition, professional judgment may be used.

Low Qualitative Risk – is a condition that exists when internal controls are assessed as meeting the “exceptional rule”, that the internal controls and the related year end processes and assessments are without a doubt, question or concern able to timely detect and correct errors or omission that may be material to the financial statements. This indicates that change risk for the current year has been effectively addressed by management, there has been no history of continued prior period internal control issues, and/or the improvements recommended either internally or externally to the internal controls over financial reporting have been effectively addressed by management or are not material, and resources have been provided by management to effectively monitor and document year-end activities and controls. Where qualitative risk is assessed as Low, the percentage used for Performance Materiality may be adjusted to 90%. In addition, professional judgment may be used.

The percentage used as a measurement of qualitative risk related to the risk of misstatements and omissions affects the value of performance materiality which is the principal amount used to determine what is to be considered significant for the variance analysis. Medium risk is considered conservative for the purpose of determining the significant variance amount and unless risk factors indicate significant issues that may cause undetected errors (High risk) or that the risk is so low it is considered highly unlikely that undetected errors exist (Low risk), it is recommended that medium risk be used.