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Statement of Position
Temporary Interfund Loans

Often local governments will loan resources from one fund to another fund experiencing a temporary cash shortage.[1] The Office of the State Auditor (OSA) has been asked whether, under generally accepted accounting principles (GAAP), funds that account for reserved or dedicated monies (such as TIF funds, park dedication funds, solid waste, road and bridge funds, and others) may make temporary loans to other funds. This Statement of Position addresses the accounting requirements for temporary loans. Local governments with funds that have restricted resources, however, should also consider other applicable legal, regulatory, or contractual requirements before loaning those funds temporarily to other funds of the government. [2]

Interfund loans are addressed in GASB 34, ¶112(a).1:

> Interfund loans—amounts provided with a requirement for repayment. Interfund loans should be reported as interfund receivables in lender funds and interfund payables in borrower funds. This activity should not be reported as other financing sources or uses in the fund financial statements. If repayment is not expected within a reasonable time, the interfund balances should be reduced and the amount that is not expected to be repaid should be reported as a transfer from the fund that made the loan to the fund that received the loan.

Section 1300.120 of the *Codification of Governmental Accounting and Financial Reporting Standards* provides some additional guidance on interfund receivables and payables:

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[1] A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

[2] GASB Codification § 1800.45 identifies restricted resources as resources that have constraints placed on the use that are either:

a. Externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or
b. Imposed by law through constitutional provisions or enabling legislation.

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> Since each fund is a fiscal and accounting entity, the amounts due to one fund from other funds, as well as the amounts owed to other funds, should be reflected in the fund accounts and in fund financial statements. Interfund loans should be reported as interfund receivables in lender funds and interfund payables in borrower funds. Where money is owed from one fund to another fund and money is also owed from the latter to the former, the amounts receivable and payable should not be offset in the accounts. But for purposes of reporting, current amounts due from and due to the same funds may be offset and the net amounts shown in the respective fund balance sheets. Liabilities arising from interfund activities do not constitute general long-term liabilities and therefore should be reported in governmental funds.

These references do not specifically address the temporary use of restricted resources. However, the information above provides some guidance. First, the discussion above indicates that interfund loans should be accounted for as receivables and payables in the applicable funds and that the transaction does not affect the funds' operating statements. Generally, interfund transfers are treated as other financing sources or uses, which are operating statement accounts, but interfund loans are balance sheet only transactions. From an accounting perspective none of the loaning fund's resources have been "used." The impact on the loaning fund is to change its assets from one form (cash) to another form (receivable). Its fund balance remains unchanged.

Second, "[i]f repayment is not expected within a reasonable time, the interfund balances should be reduced and the amount that is not expected to be repaid should be reported as a transfer from the fund that made the loan to the fund that received the loan." Although "reasonable time" is not defined,[3] it is expected that the loan will be repaid in a fairly short time frame or have a defined repayment schedule. The evaluation of a reasonable amount of time is a matter of professional judgment based on known factors. The factors to consider are:

- The borrowing fund's current financial condition;
- Estimates of the borrowing fund's future resources to repay the loan;
- The purpose of the loan;
- The established repayment terms, including whether interest will be paid;
- The loan's current status; and
- The frequency of making loans.

These factors should be considered not only by the government, but also by an auditor in judging fair presentation of the entity's financial statements.

If a loan is not repaid in a "reasonable time," the loan becomes a transfer. Making loans of restricted resources may have other implications. Questions that arise from a temporary loan include: Does the loan affect the ability of the loaning fund to meet its

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[3] Some guidance on evaluating "reasonable time" is provided by ¶9.33 of the American Institute of Certified Public Accountants' Audit and Accounting Guide, *State and Local Governments*.

requirements, including the purpose for which the fund was established? Does having loaned its resources to another fund, limit the loaning fund's ability to pay its own obligations? Are there legal or contractual restrictions that prohibit even the temporary "use" (loan) of these funds? Since a cash asset has been traded for a receivable, is the loaning fund losing interest revenue that it would normally receive? To address these issues, an entity should have an established interfund loan policy governing the requirements, including repayment provisions, for making interfund loans.

Items that could be covered in such a policy include:

- A requirement to analyze the ability of the borrowing fund to repay the loan;
- A limit on the percentage of the loaning fund's fund balance that can be loaned out at any time;
- Whether or not interest will be charged on the interfund loans;[4]
- Length of time for the loan, including a repayment schedule;
- Which funds may make loans;
- Purposes for which loans would be allowed;
- Purposes, if any, for which loans would not be allowed; and
- Whether or not Board/ Council action is specifically required for individual loans and, if not, how individual loans will be authorized.

The following is an example of an interfund loan policy. Each local government should adopt a policy appropriate to its particular situation.

SAMPLE POLICY

It is the policy of the Board/Council that interfund loans between the General Fund, the __________Fund, the Capital Projects Fund, or the Debt Service Fund may be used to alleviate a temporary cash deficiency. The loan shall be accounted for as a temporary borrowing between funds or accounts and shall not be available for appropriation or be considered revenue to the borrowing fund or account. Amounts loaned shall be repaid within _____ calendar days. Borrowing shall occur only when the fund or account receiving the money will earn sufficient revenue during the current fiscal year, to repay the amount borrowed. No more than 75 percent of the maximum of moneys held in any fund or account during a current fiscal year may be loaned.

[4] A common requirement for a restricted resource is that any amounts not yet used earn interest and that interest becomes part of the dedicated resources. Charging interest on the interfund loan would eliminate this loss of revenue.

> Such loans shall not be used to balance the budget of the Borrowing Fund: nor shall they deter any function or project for which the Loaning Fund was established.
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> The Board/Council must adopt a resolution before any interfund loan transaction takes place. The resolution shall contain the exact amount of the loan, the funds involved, the purpose of the loan, the specific source of funds for repayment, the schedule for repayment and the interest rate involved.

In summary, temporary interfund loans, even of restricted funds, are generally not prohibited. However, applicable legal, regulatory, and contractual requirements should be reviewed before an interfund loan is made. In addition, a policy governing the requirements for making interfund loans should be in place.