

Capital Pass-Through Grants

Question:

A city (recipient) receives a federal grant (from a federal agency or through a state agency) and subsequently “passes through” that grant to another government (subrecipient) for capital acquisition/construction purposes. How should this flow of resources be reported in the financial statements? How should this be reflected on the supplemental schedule of expenditures of federal awards and state financial assistance required by the Tennessee *Audit Manual*? What potential OMB *Circular A-133* implications will result?

Answer (Scenario 1):

The city administers¹ the grant and is in charge of purchasing or constructing the capital assets and the capital assets are subsequently transferred to the other government.

- a. The city should report the revenue for the grant as an operating grant (program revenue) on the government-wide statement of activities² and the related construction/purchase of capital assets as current assets until transferred to the subrecipient. A corresponding liability such as “due to other government” should also be reported. The governmental fund basic financial statements should report the grant as intergovernmental revenue and as intergovernmental expenditures. The expenditures should not be classified as capital outlay expenditures because the capital assets will not be used by the city.
- b. When the capital assets are transferred to the other government it should be reported as an expense on the government-wide statement of activities (full accrual basis). The asset and liability will be removed from the statement of net assets. There will be no reporting impact in the governmental fund financial statements under the modified-accrual basis of accounting.
- c. The other government should report the transaction as a capital contribution (program revenue) on the government-wide statement of activities and as capital assets on the government-wide statement of net assets. The donated assets will have no reporting impact for governmental fund financial statements under the modified-accrual basis of accounting because capital assets are not current financial resources.
- d. The city will be subject to the audit and reporting requirements of OMB *Circular A-133*; however, the other government will not be. The grant should be reported on the city’s schedule of expenditures of federal awards and state financial assistance but not on the other government’s schedule.³

Answer (Scenario 2):

The city administers⁴ the grant but is not in charge of purchasing or constructing the capital assets.

¹ “A recipient government [the city] has administrative involvement if, for example, it (a) monitors secondary recipients for compliance with program-specific requirements, (b) determines eligible secondary recipients or projects, even it using grantor-established criteria, or (c) has the ability to exercise discretion in how the funds are allocated.” (Section N50.128, *Codification of Governmental Accounting and Financial Reporting Standards*)

² Refer to Question and Answer 7.34.6 of the GASB *Comprehensive Implementation Guide*.

³ Although unusual, the other government should be aware that any requirements in the grant agreement that would subject them to reporting would prevail.

⁴ See footnote 1.

- a. The city should report the revenue for the grant as an operating grant (program revenue) and the subsequent pass-through to the other government as an expense on the government-wide statement of activities.⁵ The governmental fund basic financial statements should report the grant as intergovernmental revenue and as intergovernmental expenditures. The expenditures should not be classified as capital outlay expenditures because the capital assets will not be used by the city.
- b. The other government should report the financial assistance as part of capital grants and contributions (program revenue) on the government-wide statement of activities and the related purchase or construction of assets as capital assets on the government-wide statement of net assets. The governmental fund basic financial statements should report the grant as intergovernmental revenue and the related purchase or construction of assets as capital outlay expenditures. Any amounts not expended at year end should be reported as deferred revenue.
- c. In this situation, both the city and the other government will be subject to the audit and reporting requirements of OMB *Circular A-133*. The grant should be reported on the schedule of expenditures of federal awards and state financial assistance for both the city and the other government.

Answer (Scenario 3):

The city acts only as a “pass through” entity and gives the grant money to the other government who in turn administers⁶ the grant and is charge of purchasing or constructing the capital assets. It should be noted that this is an infrequent situation as most pass-through grants involve some type of administrative involvement.

- a. An agency fund should be used to account for pass-through grants that are the same as cash conduits. The city qualifies as a conduit if they meet *both* of the following criteria:
 1. The city must have no administrative involvement⁷.
 2. The city must have no direct financial involvement with the grant program (e.g., matching requirements or exposure to liability for disallowed costs).⁸
- b. Same as the answer to Scenario 2b above.
- c. Same as the answer to Scenario 2c above.

⁵ See footnote 2.

⁶ See footnote 1.

⁷ See footnote 1.

⁸ Refer to Section N50.128 of the GASB *Codification of Governmental Accounting and Financial Reporting Standards* and pages 26-27 of the GFOA *Governmental Accounting, Auditing and Financial Reporting*.