

Governmental Accounting 101

Friday, November 14, 2014

*A 30,000 Foot
Overview of
Governmental Accounting*



Show of Hands

- How many Accounting majors in the room?

- How many took a class that focused on governmental accounting?
 - Undergraduate level?
 - Graduate level?

- How many took more than 3 hours of governmental accounting?



Lack of Formal Training

- Small to medium governments
 - Too many hats to wear
 - Limited training budgets

- Large governments
 - Limited government-specific CPE
 - Travel budgets often keyed to upper level employees



GASB Today

- 71 Standards to learn
- 6 Concept Statements to consider
- 6 Interpretations of Standards to be aware of
- 14 Technical Bulletins to remember

Uses/Users of Financial Statements

Three Categories of Users

- Those to whom you are accountable
 - Citizens, media, and advocacy groups/public finance researchers*
- Those who represents the citizens
 - City councils, and other legislative/oversight bodies
- Those who lend you money
 - Creditors, individual/institutional investors, rating agencies/analysts*, underwriters

Basic Needs of Users

- Citizens/City Councils
 - How do you demonstrate accountability and interperiod equity?
 - How did actual results compare to budget?
 - What financial condition are you in – are tax/fee increases on horizon?
 - Did you comply with all applicable rules/regulations?
 - Are services being provided efficiently?
- Creditors
 - Will you have the resources to repay them?



Limitations on Needs of Users

□ Citizens

- Want to obtain the maximum amount of service for the minimum amount of taxes
- Amount of taxes paid (property taxes/sales tax) rarely relates to proportion of services received from government
- Perceived value of services generally doesn't match the cost of services



Limitations (cont.)

- City Councils
 - May try to satisfy service needs by deferring other services
 - Can delay cash impact of transactions to future periods
 - Can pay for increased level of services with non-recurring revenues

Limitations (cont.)

□ Creditors

- May not have a direct relationship with the government
- Often hope for cookie-cutter approach to comparing individual governments
- Want unlimited financial information about past performance and future potential performance

Framework for Financial Statements



Financial Statement Characteristics

- Understandability
- Reliability
- Relevance
- Timeliness
- Consistency
- Comparability



Characteristics

- Understandability
 - Information should be expressed as simply as possible
 - Acknowledges that users have different levels of knowledge about governmental accounting
 - Don't exclude information just because it is difficult, and seek to explain or interpret where possible



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Characteristics (cont.)

- Reliability
 - Information should be verifiable and free from bias
 - Information should be comprehensive and cover all material transactions
 - Include narrative explanations about assumptions and methodology for obtaining estimates

Characteristics (cont.)

- Relevance
 - Encompasses many other characteristics
 - Won't be relevant if not timely, etc.
 - Should be a logical relationship between information provided and the purpose for which it is needed

Characteristics (cont.)

- Timeliness
 - Reports have to be issued soon enough after reported events to affect decisions
 - Use of timely estimates may be more beneficial than waiting for precise information
 - GFOA Recommendation – 6 months



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Characteristics (cont.)

- Consistency
 - Reports should be consistent over time
 - Once an accounting principle is adopted, it should be used for similar transactions
 - If accounting principles are changed, the nature of the change and reason for the change should be explained



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Characteristics (cont.)

- Comparability
 - Reports should be similar across similar governments
 - Differences should be due to services offered or structure of governments rather than selection of differing accounting practices

Fund Accounting

- A fund is a fiscal and accounting entity with a self-balancing set of accounts
 - Records cash and other financial resources
 - Includes all related liabilities and residual balances (net assets/position)
 - Records the changes in these accounts
 - Is segregated for the purpose of carrying on specific activities

Fund Accounting (cont.)

- Governments should maintain the funds required by law and sound financial administration
 - Only the minimum number of funds consistent with legal and operating requirements should be used
 - Unnecessary funds result in undue complexity and inefficient administration
 - Smaller funds can be combined for presentation purposes



Fund Categories

- Governmental Funds
 - Activities primarily supported by taxes, grants, or similar revenue sources
- Proprietary Funds
 - Activities primarily supported by fees and charges for services
- Fiduciary Funds
 - Resources that a government holds as trustee or agent on behalf of an outside party

Governmental Fund Types

- General Fund
 - Chief operating fund of the government
- Special Revenue Funds
 - Revenues *restricted* or *committed* to a specific use (other than capital projects or debt service)
 - May include *assigned* amounts but *restricted* or *committed* should make up a substantial portion

Governmental Fund Types (cont.)

- Debt Service Funds
 - Resources *restricted, committed, or assigned* to expenditures for debt repayment
- Capital Project Funds
 - Resources that are *restricted, committed, or assigned* to expenditures for capital outlays and acquisition and construction of capital assets
- Permanent Funds
 - Resources that are *restricted* such that only earnings can be used for operations

Proprietary Fund Types

□ Enterprise Funds

- Activities for which a fee is charged to external parties
 - Required for activities for which debt backed solely by fees and charges has been issued
 - Required where laws or regulations mandate that all costs including capital be recovered through fees
 - Required when pricing policies are in place mandating that fees be set to recover costs including capital

□ Internal Service Funds

- Activities that benefit the government and are essentially break-even over time



Fiduciary Fund Types

- Pension (and OPEB) Trusts
 - Resources held in trust for members and beneficiaries for which the government has managerial responsibility
- Investment Trusts
 - Investment pools when reported by the sponsor
- Private-purpose Trusts
 - Principal and income benefit individuals, private organizations or other governments
- Agency Funds (custodial funds)

Revenues & Expenses/Expenditures

Measurement Focus

- Measurement Focus – what you are looking to measure in a transaction
 - Current Financial Resources – assets and liabilities that affect near-term liquidity
 - Cash, accounts payable, etc.
 - Governmental funds
 - Economic Resources – all assets and liabilities
 - Cash, accounts payable, capital assets, long term debt
 - Proprietary funds, Fiduciary funds, Government-wide

Basis of Accounting

- Basis of Accounting – when the transaction should be recorded
 - Modified Accrual basis – transactions are recognized when they impact near-term liquidity
 - Revenues should be both measurable and available
 - Measurable – amount reasonably determined
 - Available – collectible within the current period or soon enough thereafter to finance current period expenditures
 - Expenditures are recognized when they are incurred
 - Except for – debt not currently payable, accrued interest payable, inventories & prepaids, accrued liabilities not expected to be liquidated with currently available resources

Basis of Accounting (cont.)

- Basis of Accounting – when the transaction should be recorded
 - Accrual basis – transactions are recognized when they occur or are incurred
 - Regardless of when cash is received or disbursed
 - Governmental funds use the modified accrual basis
 - Proprietary funds, Fiduciary funds, and Government-wide presentations use the accrual basis

Measurement Focus/Basis

	Governmental Funds	Proprietary/ Fiduciary Funds/ Government-wide presentation
Measurement Focus	Current Resources	Economic Resources
Basis of Accounting	Modified Accrual	Full Accrual

Transaction Categories

- Exchange and exchange-like transactions
 - Each party gives and receives equal or nearly equal value
 - Example – facility rentals
- Nonexchange transactions
 - One party gives or receives value to another party without giving or receiving equal value in return
 - Four categories of nonexchange transactions

Nonexchange Transactions

- Derived tax revenues
 - Revenue generated from events unrelated to the government's operation
 - Example – Sales tax receipts
- Imposed nonexchange transactions
 - Assessments made by a government that do not involve exchanges
 - Example – Property taxes, court fines

Nonexchange Transactions (cont.)

- Government-mandated nonexchange transactions
 - Services required by another level of government for which the other level will offer at least partial funding (funded mandates)
 - Not common in Texas
- Voluntary nonexchange transactions
 - All other nonexchange transactions
 - Example - grants

Transaction Recognition

Transaction	Receivable	Revenue
Exchange	At time of exchange	At time of exchange
Derived tax revenue	When sale takes place	When sale takes place
Imposed nonexchange	Assessment date	Start of period for which levied
Government-mandated	When qualifying expenditures incurred	When qualifying expenditures incurred
Voluntary nonexchange	When qualifying expenditures incurred or eligibility requirements met	When qualifying expenditures incurred or eligibility requirements met



Revenue Rules for Modified Accrual

- Revenue recognition should be delayed until amounts are available
 - Offset receivable with a deferred inflow of resources

- If payment is received prior to an exchange, governments should record unearned revenue (liability) until eligible for recognition

Expenditure Rules for Modified Accrual

- Expenditures are recognized when they are incurred
 - Except for – debt not currently payable, accrued interest payable, inventories & prepaids, accrued liabilities not expected to be liquidated with currently available resources

- Debt and interest payable
 - Record as expenditure when due

Expenditure Rules (cont.)

- Accrued liabilities not expected to be liquidated with currently available resources
 - Record as expenditure when payment made
 - Except, record if amount was due at end of reporting period but not made due to timing of payables or payroll cycle
 - Compensated absences, pension contributions

Expenditure Rules (cont.)

- Inventories & prepaids
 - Can expense entire amount in current period (purchases method)
 - Can recognize portion over period of service (consumption method)



Other Financing Sources/Uses

- Governmental Funds report Other Financing Uses/Sources for transactions that are not based on operations
 - Issuance of long-term debt
 - Inception of capital leases
 - Sale of capital assets
 - Insurance recoveries
 - Transfers

Financial Position



Elements of Financial Position

- There are five elements of financial position
 - Assets
 - Liabilities
 - Deferred Outflows of Resources
 - Deferred Inflows of Resources
 - Fund Balance/Net Position

Assets/Liabilities

- Assets – resources with present service capacity that the government presently controls
 - Enables the government to provide services
 - The government has the right to determine how to use the capacity of the asset

- Liabilities – present obligations to sacrifice resources that the government has little to no discretion to avoid
 - Obligation created through a social, legal or moral requirement
 - Consequences for avoidance are more than insubstantial



Deferred Resources

- Deferred Outflows of Resources – consumption of net assets by the government that is applicable to a future reporting period
 - Positive impact on financial position

- Deferred Inflows of Resources – acquisition of net assets by the government that is applicable to a future reporting period
 - Negative impact on financial position

Fund Balance/Net Position

- Fund Balance/Net Position – the residual of all elements in the financial statement
 - Fund Balance – Governmental funds
 - Net Position – Proprietary funds, Fiduciary funds, and Government-wide presentations

- (Assets plus Deferred Outflows) less (Liabilities plus Deferred Inflows) equals Fund Balance/Net Position



Fund Balance Classifications

- Classifications
 - Non-spendable
 - Restricted
 - Committed
 - Assigned
 - Unassigned

- Hierarchy based on constraints on the specific purposes for which resources can be spent

Fund Balance Definitions

- Non-spendable
 - Resources that cannot be spent or must be maintained intact
 - Inventories, prepaid amounts, corpus of a permanent fund

- Restricted
 - Resources with external enforceable legal restrictions
 - Bond holders, grantors, constitutional, legislative

Fund Balance Definitions (cont.)

- Committed
 - Resources that have formal constraints imposed by governing body
 - Action such as ordinance or resolution occurs prior to year-end

- Assigned
 - Resources with an *intended* use set by governing body or management
 - Cannot exceed total fund balance less nonspendable, restricted, and committed balances



Fund Balance Definitions (cont.)

- Unassigned
 - All other resources
 - Positive balances only allowed in the General Fund
 - Negative balances allowed in any governmental fund

Net Position Classifications

- Classifications
 - Net investment in capital assets
 - Restricted
 - Unrestricted

- Previously called “net assets”

Net investment in capital assets

- Basically, capital assets net of depreciation, less the outstanding balance of capital-related debt
 - Debt shouldn't include unspent proceeds
 - Debt should be net of unamortized amounts for premiums, discounts, and deferred amounts on refundings
 - Debt shouldn't include amounts not used to finance capital assets of your government
 - Can be negative

Restricted/Unrestricted Net Position

- Restricted
 - Parties outside the government
 - Creditors
 - Granting agencies
 - Enabling legislation
 - Constitutional
- Unrestricted
 - All other resources and obligations
 - Not a measure of current liquidity
 - Can be negative

Financial Statements



Major Fund Presentation

- Basic financial reporting emphasizes major funds by presenting them individually
- Nonmajor funds are presented in the aggregate
- General fund is always major
- Can promote fund to major based on other qualitative factors

Major Fund Criteria

	10% Test – Like Funds	5% Test – All Funds
Assets + Deferred Outflows	$\geq 10\%$	$\geq 5\%$
Liabilities + Deferred Inflows	$\geq 10\%$	$\geq 5\%$
Revenues	$\geq 10\%$	$\geq 5\%$
Expenses	$\geq 10\%$	$\geq 5\%$

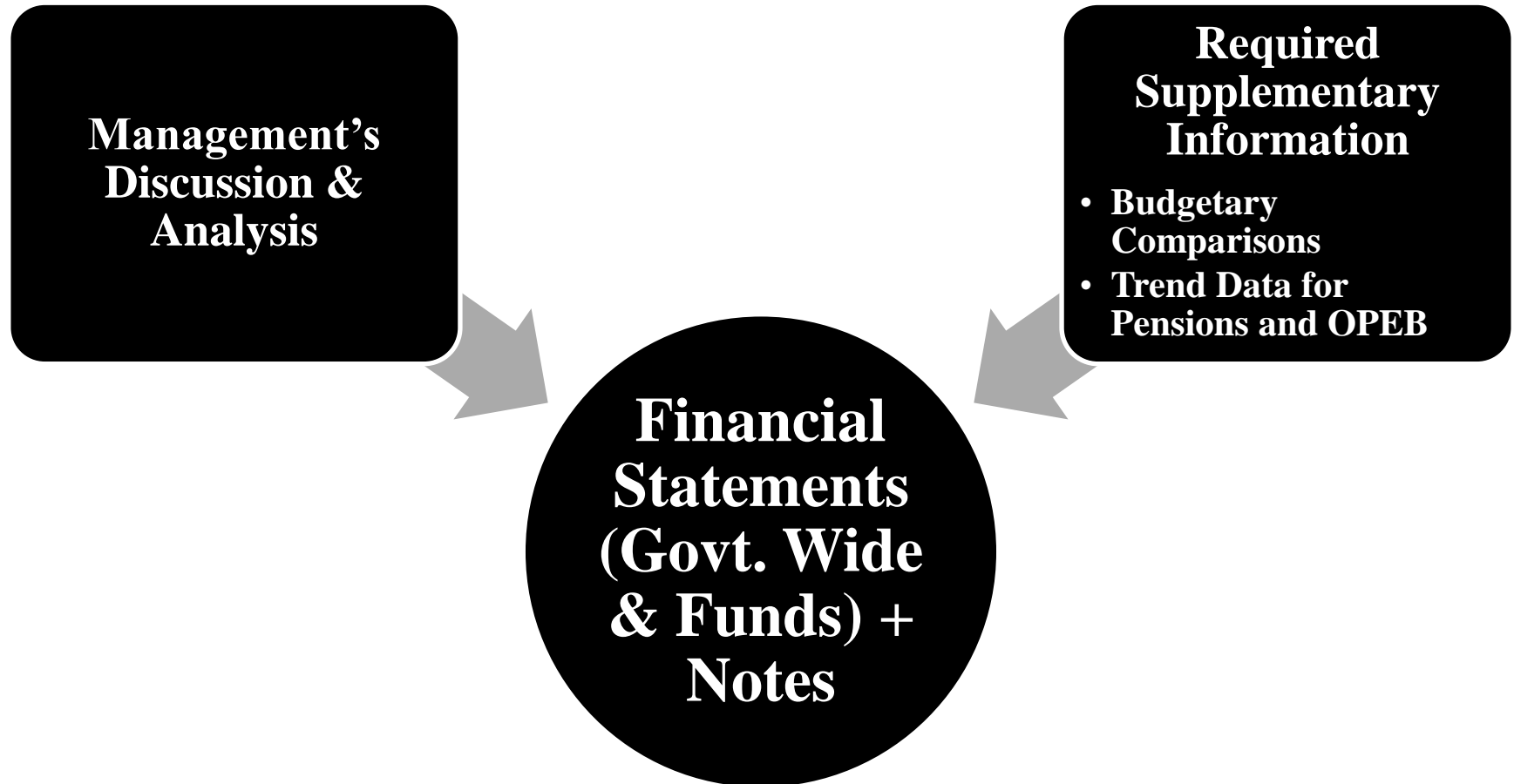
- Major fund if both 10% and 5% test positive for one of four groupings



Government-wide Presentation

- Governmental funds are converted to proprietary funds
 - Long-term liabilities and capital assets included
 - Revenues and expenses recognized using full accrual basis of accounting

Basic Financial Statements



Management's Discussion and Analysis (“MD&A”)

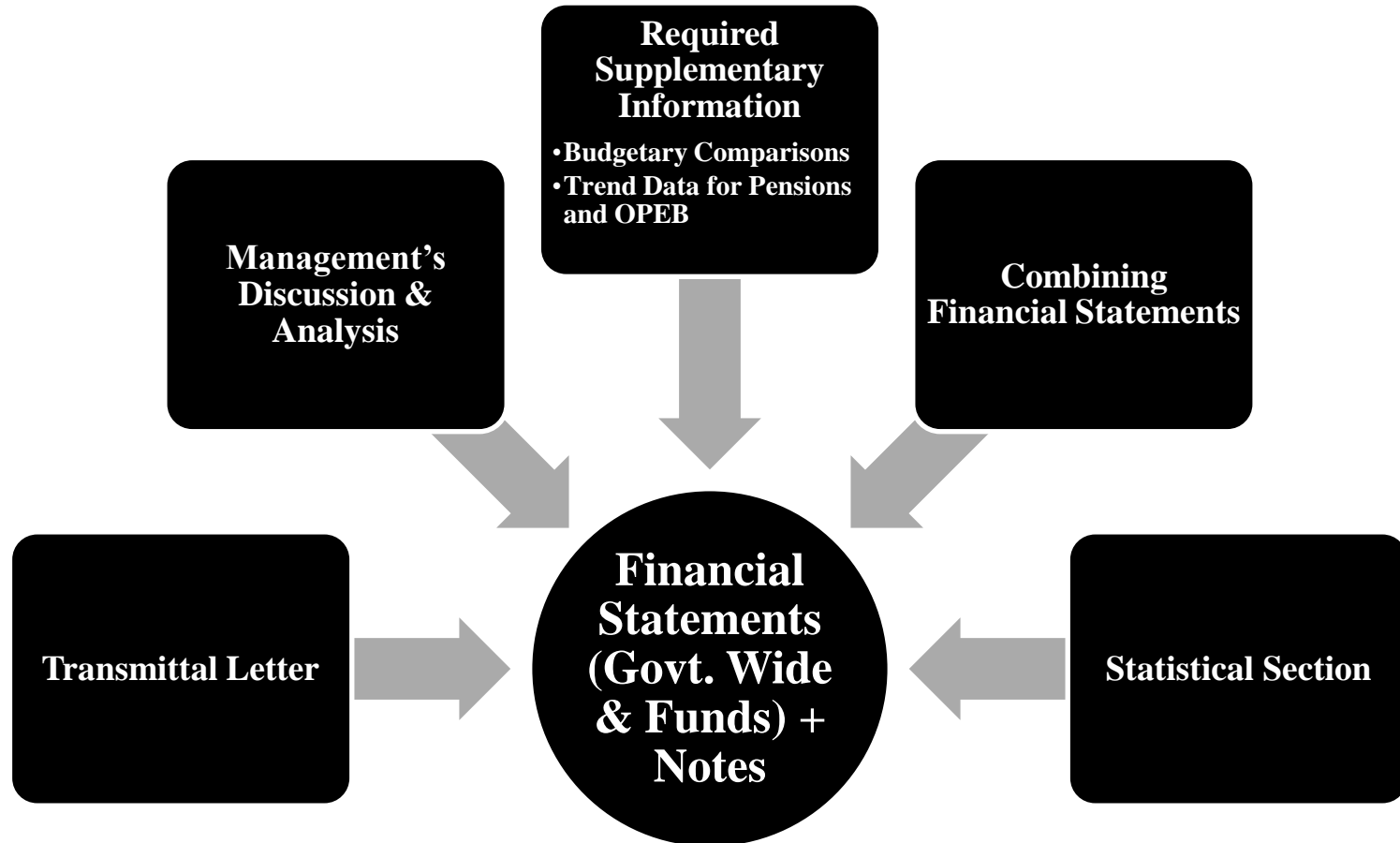
- Provide an Objective and Easily Readable analysis of the government's Financial Activities
 - Currently known facts (as of audit report date)
 - Focus on both short and long-term analysis
 - Serves as an introduction to the numbers
 - Avoid “boilerplate” language
- “The minimum is the maximum”



Location of MD&A

- Immediately following the Independent Auditor's Report
 - Precedes the basic financial statements
- Contrast with location of other types of RSI
 - Following Notes

Comprehensive Annual Financial Report (“CAFR”)



Upgrading to a CAFR

- Transmittal Letter
 - Basic description of government and chance to let users know positive things about your community
- Combining financial statements
 - Detail of nonmajor funds that were aggregated on fund financial statements
- Statistical Section
 - History of key facts and figures about your community



CAFR Stats

- For FY 2012, GFOA's Certificate of Achievement program awarded 399 Certificates to Texas governments
 - Second only to California (457)

- This represents 15% of cities and 20% of counties in the state

Next Steps

- If you only prepare basic financial statements, work towards upgrading to a CAFR
- If your auditor prepares your financial statements, work towards preparing them in-house
- If you prepare a CAFR but don't submit to GFOA, do so
- If you aren't part of the GFOAT FRRR committee, get involved

*No Debits or Credits
Were Harmed in this Presentation*

Questions?
