I. GOVERNMENTAL ACCOUNTING OVERVIEW

A. Governmental financial reporting is designed to demonstrate both operational accountability for the entity as a whole and fiscal accountability for specific funds. Fiscal accountability generally relates to compliance with laws and fund requirements, and operational accountability generally relates to economic performance.

B. Standards for accounting are established by the Governmental Accounting Standards Board (GASB). The Government Accountability Office (GAO) governs audits under Generally Accepted Government Auditing Standards (GAGAS), also referred to as the Yellow Book.

C. Funds are separate, independent self-balancing sets of accounts, similar to a "checkbook." The three major categories of funds are governmental (GRaSPP), proprietary (SE), and fiduciary (PAPI).

D. Government-wide financial statements are prepared using the full accrual basis of accounting to permit an economic resources measurement focus. This method is essentially the same as used in "for profit" accounting and is covered in more detail in F9.

E. Governmental funds use the modified accrual basis of accounting and provide a current financial resources measurement focus. Revenues are recognized when measurable and available. Expenditures (not "expenses") are generally recognized when resources are spent. There are no non-current assets in governmental funds' balance sheets.

The five governmental (GRaSPP) funds are the **general**, special revenue, debt service, capital projects, and **permanent** funds.

1. Governmental fund balances are classified in one of five ways.

2. The following table lists the possible classifications within GRaSPP fund balances in the order of their limitations (constraint) and the likely funds in which the classifications would be used.

<table>
<thead>
<tr>
<th>Classification</th>
<th>General</th>
<th>Special Revenue</th>
<th>Debt Service</th>
<th>Capital Projects</th>
<th>Permanent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nonspendable</td>
<td>✓</td>
<td>✓</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Restricted</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Committed</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td></td>
<td>✓</td>
</tr>
<tr>
<td>Assigned</td>
<td>✓</td>
<td></td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unassigned, Pos. (Neg.)</td>
<td>✓</td>
<td>(✓)</td>
<td>(✓)</td>
<td>(✓)</td>
<td>(✓)</td>
</tr>
</tbody>
</table>

F. Proprietary (SE) funds use full accrual accounting and the economic resources measurement focus. The internal service and enterprise funds are the two proprietary funds. Proprietary fund accounting is similar to commercial accounting.

G. Fiduciary (trust) funds use full accrual accounting and the economic resources measurement focus. The "PAPI" funds are pension, agency, private purpose, and investment trust funds.
II. APPLICATIONS OF MODIFIED ACCRUAL ACCOUNTING

A. Most governmental (GRaSPP) funds record budgets, activity and encumbrances during the year and close them out at the end of each year (BAE BAE).

B. Recording a budget that is formally integrated with a government’s accounting system involves journalizing budgeted transactions using the following accounts at the start of the year: Estimated revenues, appropriations, and estimated other sources/uses. Natural account balances for budgetary accounting are the opposite of actual activity: Estimated revenues are “debits” and appropriations (estimated expenditures) are credits. Any excess, or projected surplus, is credited to budgetary control (a budgetary equity account). A projected shortfall, or deficit, would be debited to that account. This entry is closed (reversed) at the end of the year.

C. Government fund revenues are recorded in the real accounts when they are measurable and available. "Available" is generally defined as collected within 60 days of year-end. Real property taxes (imposed non-exchange revenues) are accrued when billed to property owners with related revenue recognition subject to the measurable and available criteria. Derived tax revenues (sales taxes) are accrued if measurable and collected within 60 days after fiscal year-end (available).

D. Expenditures are recognized when the vouchers payable (or cash outlay) is recorded. Capital purchases, debt service payments, and operating expenditures are treated as a current year’s expenditures. Both operating and capital transactions are handled the same way.
   1. Modified accrual accounting generally recognizes expenditures consistently with commercial accounting (when incurred).
   2. The current financial resources measurement focus changes how the expenditure is recognized. Non-current assets are not recognized.
   3. Some current assets are recognized. Expenditures for supplies, (prepaid) insurance, and inventory can be accounted for by the purchase method or consumption method.

E. Transfers out to other funds, or interfund transfers, represent a use of financial resources, not an expenditure item.

F. For external reporting, governmental fund expenditures are first classified according to the appropriate fund. Within the fund, there may be further classification by function or program. For internal or analytical purposes, expenditures may also be classified by organizational unit, activity, or object class.

G. Fixed assets purchased, constructed, or leased are not capitalized; however, they are reported on the government-wide financial statements (F9). Likewise, long-term debt is not recorded as debt in a governmental fund. Instead, long-term debt is classified as other financing source on the government-wide financial statements.

H. Open purchase orders represent an encumbrance or commitment of the available appropriations of a governmental fund. For purposes of internal accounting, an encumbrance (debit) is set up with a credit to budgetary control. When the order is filled, the encumbrance J/E is reversed for the amount originally recorded and the actual expenditure is recorded in a separate J/E.
   1. Encumbrances are not identified on the face of a governmental fund’s external financial statements, but may be disclosed.
III. DEFERRED OUTFLOWS AND INFLOWS OF RESOURCES

A. Certain transactions under GASB 63 that do not qualify for treatment as either an asset or liability may be reported as either a deferred outflow or deferred inflow of resources. A deferred outflow of resources is a consumption of net assets that is applicable to a future reporting period, whereas a deferred inflow of resources is an acquisition of net assets that is applicable to a future reporting period.

B. Deferred outflows of resources have a positive effect on net position and are reported following assets but before liabilities. In contrast, deferred inflows of resources have a negative effect on net position and are reported following liabilities but before equity.

C. Service concession arrangements and derivative instruments used for hedging are types of transactions classified as deferred outflows and inflows of resources. Additionally, accounting and reporting for pensions uses the concepts of deferred outflows and inflows to account for changes in a government's pension liability.

IV. GOVERNMENTAL FUNDS (MODIFIED ACCRUAL BASIS)—GRASPP

A. There is only one general fund in a particular governmental entity. The general fund accounts for activities of a government that are not accounted for by any other fund.

B. Special revenue funds contain funds "earmarked" for particular purposes. Special revenue funds are typically restricted or committed to specific purposes other than debt service or capital projects. Expendable trusts and grants are special revenue funds with unique accounting issues.

C. Debt service funds (DSF) pay for the principal and interest related to general obligation debt. This is debt incurred by governmental funds. Other (SE-PAPI) funds service their own debt.

D. Capital projects funds are created for each project underway for better accountability of resources budgeted for each project. Only projects for governmental funds are accounted for within a capital projects fund. Financing sources may be long-term debt issues, fund transfers, capital grants, government grants, or special assessments charged to property owners benefited by the project.

E. Permanent funds are legally restricted. Only income can be spent with the principal amounts "permanently" restricted from spending.

V. PROPRIETARY FUNDS (FULL ACCRUAL BASIS)—SE

A. Internal service (IS) funds primarily serve other funds or departments within the government (internal customers). The financial statements of an IS fund are the statement of net position; a statement of revenues, expenses, and changes in net position; and a statement of cash flows.
B. Enterprise funds are used to account for operations that are financed or operated in a manner similar to private business enterprise. Activities are recorded in the enterprise fund if any of the following criteria are met: 1) the activity is financed with debt that is secured solely by a pledge of the net revenue from fees and charges; 2) laws and regulations require that the cost of providing services be recovered through fees; or 3) the pricing policies of the activity establish fees and charges designed to recover its costs. The financial statements and net asset classifications of an enterprise fund are the same as those for an internal service fund.

C. The enterprise and internal service funds are distinguished by their customer; enterprise funds serve external customers and internal service funds serve the government.

VI. FIDUCIARY FUNDS (FULL ACCRUAL BASIS)—PAPI

A. Pension trust funds account for government-sponsored pension and postretirement plans. Additions and deductions replace revenues and expenses as activity classifications in the statement of changes in fiduciary net position.

B. Agency trust funds are custodial funds. The current assets equal the current liabilities in the statement of fiduciary net position, with no fund balance reported.

C. Private purpose trust funds, such as an escheat property fund, contain resources for the benefit of other parties or entities.

D. Investment trust funds represent investments held on behalf of others and its assets are generally reported using fair value.