
UNIT 3: GENERAL FUND & SPECIAL REVENUE FUNDS

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3.0 AIMS AND OBJECTIVES

In this unit, the two type of funds in the governmental funds category i.e general fund and special revenue fund are discussed, it gives a clear detail how the two fund operate, how their financial operations are accounted and recorded, theoretical as well as accounting illustrations are given to give the reader a clear detail understanding of the two funds.

3.1 INTRODUCTION

3.1.1 General Fund

As it can be recalled from chapter two, the general fund is used for general governmental activities such as police, administration and the like. To distinguish the general fund adversely, it can be said that the general fund should account for all financial resources for which a

separate fund is not required. All governmental entities have a general fund (GF). Although it may be called the operating fund, the current fund or something similar, the general fund will exist as long as the entity exists. A governmental entity will have only one general fund. The general fund of a state or local government unit is the entity that accounts for all the assets & resources used for financing the general administration of the unit & the traditional services provided to the people.

3.1.2 Special Revenue Fund

Special revenue fund (SRF) in contrast to GF are used to account for resources, which are collected for a specified purpose. Whenever a tax or other revenue source is authorized by legislative body to be used for specific purpose, only a governmental unit availing itself of that source may create a Special Revenue Fund in order to be able to demonstrate that all revenue from the source was used for the specified purpose, only separate special revenue funds are established by governmental units, as mandated by legislative enactments to account for the receipts and expenditures associated with specialized revenue sources that are earmarked by law or regulation to finance specified governmental operations. Fees for rubbish collection, state taxes on diesel fuel that is required to be used only for road maintenance, tax on hotel rooms to be used to improve tourist facilities, traffic violation fines are examples of governmental units revenues that may be accounted for in a separate special revenue fund.

- Comparison:

The general fund should account for all financing sources for which a separate fund is not required. Special revenue funds are necessary when they are required by law or contract. A governmental entity will have several special revenue funds at any time & these funds are opened & closed according to need.

The general funds and the special revenue funds have different purposes, but they are both revenue funds, and the accounting and reporting procedure is the same for both. They are similar in that all or almost all of their resources are expended each year. They are then filled up (replenished) again for the next year.

3.2 ACCOUNTING CHARACTERISTICS

Fixed assets are not capitalized in either fund. Their purchase is considered as expenditure, the same as for salaries or utilities. Such fixed assets are not accounted for by these funds. Because they are not normally converted into cash. Similarly the same categories of funds account for only those liabilities incurred for normal operations that will be liquidated by use of fund assets.

The arithmetic difference between the amount of financial resources and the amount of liabilities recorded in the fund is called the **fund equity**. Residents of the governmental unit have no legal claim on any excess of liquid assets over current liabilities. therefore the fund equity is not analogous to the capital accounts of an investor owned entity. Accounts in the fund equity category of general funds & special revenue funds consist of reserve accounts established to disclose that portion of the equity are not available for appropriations. The portion of equity available for appropriation is disclosed in an account called **Fund Balance**. General funds & special revenue funds account for financial activates during a fiscal year in accounts classified as **Revenues, Other Financing Sources, Expenditures & Other Financing Uses**.

Revenue: - is the increase in the fund financial resources other than from inter fund transfers & debt issue proceeds.

Other financing sources- are classified as an increase in the fund financial resources as a result of operating transfers into a fund and debt issue proceeds received by a fund.

Expenditure is defined as decrease in fund financial resources other than through inter fund transfers, operating transfers out of a fund and debt issue proceeds are classified as other financing uses. It is a term which replaces both the terms **costs** and **expenses** used in accounting for profit seeking entities.

Other Financing uses - a decrease in the fund financial resources as a result of operating transfers out of a fund.

An example of the use of transfer accounts occurs in those jurisdictions where a portion of the taxes recognized as revenue by the general fund of a unit is transferred to a debt service fund which will record expenditures for payment of interest and principal of general obligation debt. the general fund would record the amounts transferred as operating transfers out; the debt service fund would record the amount received as operating transfers in. Thus the use of transfer accounts achieve the desired objective that revenues be recognized in the fund which levied the taxes and expenditures be recognized in the funds which expends the revenue.

In few jurisdictions taxes must be collected in the year before the year in which they are available for expenditure. In such jurisdictions tax collection should be credited, deferred revenue should be debited & revenue should be credited.

Under accrual basis, expenditure is recognized when a liability to be met from fund asset is incurred. It is important to note that an amount of a liability incurred whether the liability is for salaries (an expense) for supplies (a current asset) ,or for a long lived capital assets such as land building or equipment.

3.3 BUDGET & BUDGETARY ACCOUNTS

The fact that budgets are legally binding upon administrators has led to the incorporation of budgetary accounts in the general fund and in the special revenue funds and in all other funds required by law to adopt a budget.

Budgeting is the process of allocating scarce resources to unlimited demands budgeting has a great role in governmental accounting than in profit making business.

Budgeting is a key elements of legislative control over governmental units. The two classifications of budget for governmental units are the same as those for business enterprises. Annual budgets and long term or capital budgets. Annual budgets include the estimated revenues & appropriations for expenditures for a specific fiscal year of the governmental unit. Annual budgets are appropriate for the general fund & special revenue funds. They sometimes are used for other governmental funds. An expendable trust funds also may have an annual budget, depending upon the terms, the terms of the trust indenture. Capital budgets, which are used to control the expenditures for construction projects or other plant asset acquisitions, may be appropriate for capital projects funds. The annual or capital budgets often are recoded in the accounts of all these funds, to aid in act for compliance with legislative authorities.

The operations of the two proprietary funds are similar to those of business enterprises. Consequently, annual budes are used by these funds as a managerial planning & control device rather than as a legislative control tool. Thus annual budgets of enterprise funds & internal service funds generally are not recorded in ledger accounts by these funds.

In order to facilitate preparation of budgets and preparation of the combined statement of revenues, expenditures and changes in fund Balance-Budget and Actual required for GAAP conformity, accounting systems of funds for which budgets are required by law should incorporate budgetary accounts. Only three general ledger control accounts are needed to provide budgetary control; Estimated Revenue, Appropriations and Encumbrances.

i **Estimated Revenues** – resources expected to be received

i **Appropriations** – is both an authorization to spend and limitation of spending.

i **Encumbrances** – Purchase orders(P.O.) in governmental entities have the function of keeping track of coming expenditures so that the budget is not exceeded. this is done by actually recording the P.O in the ledger account as an **Encumbrance**

All the three must be supported by subsidiary ledger accounts whatever detail is required by law or by sound financial administration. Budgeted interfund transfers and debt issue proceeds may be recorded in **Estimated Other Financing Sources** and **Estimated Other Financing Uses** control accounts supported by subsidiary accounts as needed.

3.3.1 Recording the Budget

At the beginning of the budget period, estimated revenue control account is debited for the total amount of revenues expected to be recognized, as provided in the revenues budget and the limitation of spending or authorized expenditures will be recorded with a credit in the appropriations control account. The amount of revenue expected from each source specified in the revenues budget is recorded in a subsidiary ledger account so that the total of subsidiary ledger detail agrees with the debit to the control account and both agree with the adopted budget. The same way will also be used for the appropriation.

The entry to record the budget is simple. It is normally done on the first day of the fiscal year. Estimated revenue is debited, Appropriations is credited, and fund balance is debited or credited for the difference. Appropriation could be further subdivided- by month or other periods; this subdivisions are called **Allotments**.

Recording encumbrance helps the one managing the finances to know that money has been committed to some purpose and is no longer available for expenditure. There is often a delay between placing the purchase order and receiving the goods ordered. Therefore it is possible for the administrators to forget about the purchase orders that have been placed and to think that the money is still available to be used. This is especially true in a large entity where dozens of purchase orders are placed each week. To ensure that outstanding purchase orders are not overlooked in the on going commitment of resources, purchase orders are recorded in the *Encumbrance* account. An encumbrance differs from an expenditure in that the encumbrance is an estimate of liability to be incurred while expenditure is an actual liability which has been incurred. the reason that encumbrance is only an estimate is that invoiced amounts sometimes differ from purchase order amounts. for example a particular item may be out of stock, and either backordered, or substituted by a similar item.

Example- when a purchase orders for goods or services is issued to a supplier by one of those funds, a journal entry similar to the following is prepared for the fund.

Encumbrance	150,000	
		Fund Balance Reserved for Encumbrances
150,000		

= to record encumbrances for purchase order no. **001**
issued to **X** company.

When the suppliers invoice for the ordered merchandise or services is received by the governmental unit, it is recorded and the related encumbrance is reversed as seen below:

Expenditures 180,500

Vouchers payable 180,500

= to record an invoice received from Wilson company under purchase

order no. **001**

Fund Balance reserved for Encumbrances 150,000

Encumbrances 150,000

=To reverse encumbrance for purchase order no. **001** issued to X company

Two journal entries are needed for encumbrances, one when the order is placed and another when the goods are received. When the order is placed, encumbrance is debited and **Reserve for Encumbrance** (a fund balance account) is credited. When the order is received, the entry is reversed. As indicated by the example above the invoice amount may differ from the amount of the governmental units purchase order because of such items as shipping charges, Sales Taxes, and price changes.

Regardless of which types of annual budgets are used by government unit, the final budget adopted by the governmental units legislative body will include estimated revenue other financing sources, appropriations and other financing uses. If the estimated revenue and other financing sources of the budget exceed appropriations and other financing uses (as required by law for many governmental units), there will be budgetary surplus, if vice-versa, there will be budgetary deficit.

3.4 ACCOUNTING FOR GENERAL FUND AND SPECIAL REVENUE FUND

Illustration

Below is the Balance Sheet of town of X General fund on June 30, year 5 and the annual budgets adopted for the year ended June 30, year 6.

Town of X General Fund
Balance Sheet June 30, year 5

Assets

Cash	1,600,000	
Inventory of supplies	<u>400,000</u>	
	Total	Assets
	2,000,000	

Liabilities and Fund Balance

Vouchers payable	800,000	
Fund balance:		
Reserved for encumbrance	400,000	
Unreserved and undesignated	<u>800,000</u>	<u>1,200,000</u>
	Total liabilities and fund balance	
	2,000,000	

Below are the approved budget by the town council for the fiscal year ended on June 30, year 6.

Estimated revenues:

- General property taxes	7,000,000	
- Licenses and permits	400,000	
- Charges for services	500,000	
- Fines and for fits	300,000	
- Miscellaneous revenues	<u>200,000</u>	8,400,000
Estimated other financing sources (transfer from EF)		100,000

Appropriation:

- General government	4,700,000
- Public safety	1,900,000
- Health and welfare	1,100,000

- Culture and recreation	<u>400,000</u>	8,100,000_
Estimated other financing uses (transfer to DSF)		100,000

* The journal entry to record the annual budget for the town of X General fund on July 1,
year 5 was as follows:

Estimated revenues	8,400,000	
Estimated other financing sources	100,000	
Appropriations		8,100,000
Estimated other financing uses		100,000
Budgetary fund balance		300,000

An analysis of each of the ledger accounts in the forgoing journal entry follows:

1. Estimated Revenues and Estimated Other financing Sources ledger account may be considered **Pseudo Asset** controlling accounts because they reflect resources expected to be received by the General Fund during the fiscal year. These accounts are

Not actual assets because they do not fit the accounting definition of an Asset as a probable economic benefit obtained or controlled by a particular entity as a result of past transactions or events. Thus the two accounts in substance are **memorandum accounts**, useful for control purposes only, that will be closed after the issuance of Financial statements for the General fund for the fiscal year ending June 30 year 6.

2. The Estimated other Financing source **ledger** accounts includes the budgeted amounts

of such non Revenue items as proceeds from the disposal of plant assets and operating transfers from other funds.

3. The Appropriations and Estimated Other Financing Uses Ledger Account may be considered **Pseudo Liability** controlling accounts because they reflect the legislative body's commitment to expend General

fund resources as authorized in the Annual Budget. These accounts are not genuine liabilities because they do not fit the definition of a liability as a probable future sacrifice of economic benefits arising from present obligation of a particular entity to transfer assets to provide services to other entities in the future as a result of past transactions or events. The appropriations and Other Financing uses are **memorandum accounts**, useful for control purposes only, that will be closed after issuance of year end financial statements for the general fund.

4. The Estimated Other Financing Uses accounts include budgeted amount of operating transfers out to other funds, which are not expenditures.

5. The Budgetary Fund Balance Ledger Account, as its title implies is an account that balances the debit and credit entries to accounts of a budget journal entry. Although similar to the owners' equity accounts of a business enterprise in this balancing feature, does not purport to show an ownership interest in the General funds assets. At the end of the fiscal year, the budgetary fund balance account is closed by a journal entry that reverses the original entry for the budget.

The journal entry to record the town of X general funds annual budget for the year ending June 30 year 6 is accompanied by detailed entries to subsidiary ledgers for Estimated Revenues, Estimated other financing Sources, Appropriations and Estimated Other Financing Uses. the budget of the town of X general fund purposely was condensed; in practice the general fund estimated revenues and appropriations would be detailed by source and function, respectively into one of the following widely used subsidiary ledger categories:

Estimated Revenues:

- Taxes

Appropriations:

- General government

- Licenses and permits
- Intergovernmental revenues
- Charges for Services
- Fines and Forfeits
- Miscellaneous
- Public safety
- Public works
- Health and Welfare
- Culture - recreation
- Conservation of natural resources
- Debt service
- Intergovernmental expenditures
- Miscellaneous

Such details will be discussed in the next topic; Classification and terminology of governmental funds budgets and accounts.

In summary, budgets of a governmental unit are often recorded in the accounts of the four governmental funds. An expendable trust fund may also record a budget if required to do so by the trust indenture. The recording of the budget initiates the accounting cycle of each for each of the funds listed above. Recording the budget also facilitates the preparation of financial statements that compare budgeted and actual amounts of revenues and expenditures.

Encumbrances and budgetary control- because of the need for expenditures of governmental units to be in accordance with appropriations of governing legislative bodies, an a encumbrance Accounting techniques are used for the general fund and the special revenue funds and sometimes for capital projects funds. The Encumbrance is a memorandum method for assuring that total expenditures for a fiscal year do not exceed appropriations. The encumbrance technique is used in accounting for governmental units have no counterpart in accounting for business enterprises.

Assume that in addition to the budget illustrated earlier, the town of X general fund had the following summarized transaction and events for the fiscal year ended June 30, 19x6

1. Property taxes were billed in the amount of 7,200,000 of which 140,000 was of doubtful collect ability.

Property tax receivable- current	7,200,000	
Allowance for uncollectibles current taxes		
140,000		
		Revenue
7,060,000		

= To accrue property taxes billed and to provide for estimated uncollectibles portion.

Explanation- The modified accrual basis of accounting for a general fund permits the accrual of property taxes, because they are billed to the property owners. The estimated uncollectibles property taxes are offset against the total assets billed in order to measure actual revenues from property taxes for the year.

2. A total of 6,500,000 amount of Property tax were collected and a total of 1,020,000

Amount of cash from other revenue sources like licenses and permits, fines and forfeits, Miscellaneous sources were also collected.

Cash	7,520,000
Property taxes receivable-current	6,500,000
Revenue	1,020,000

= To record collection of property taxes and other revenues for the year.

Exp- Under the modified accrual basis of accounting, revenues not susceptible to accrual are recognized on the cash basis like self-assessment basis tax revenue (Eg. Income tax, Sales Tax, Gross receipts Tax,) and miscellaneous revenues (Eg. Annual business licenses, construction and home improvement permits, Fines and forfeits etc.)

3. Property tax in the amount of 130,000 were uncollectibles.

Allowance for uncollectable current taxes

130,000

Property taxes receivable- current 130,000

= To write off receivables for property taxes that are uncollectable

Explanation- The forgoing journal entry represents a shortcut approach. in an actual situation , uncollectibles property taxes first would be transferred together with estimated uncollectibles amounts, to the Taxes Receivable- Delinquent ledger account from the Taxes Receivable- Current account. Any amounts collected on these delinquent taxes would include revenues for interests and penalties required by law. Any uncollected delinquent taxes would be transferred, together with estimated uncollectibles amounts to the Tax-Liens Receivable ledger Account. After the passage of an appropriate statutory period, the governmental unit might satisfy its tax lien by selling the property on which the delinquent taxes were levied.

4. Purchase orders for non recurring expenditures were issued to outside suppliers in the total amount of 3,600,000.

Encumbrances 3,600,000

Fund Balance reserved for Encumbrances

3,600,000

= To record purchase orders for non-recurring expenditures issued during the year.

Explanation- encumbrance journal entries are used to prevent the over expending of an appropriated amount in the budget. This journal entry to the encumbrances ledger account is posted in detail to reduce the unexpended balances of each applicable appropriation in the subsidiary ledger for appropriation. The unexpended balance of each appropriation is thus reduced for the amount committed by the issuance of purchase orders.

5. Expenditures for the year totaled 7,600,000 of which 900,000 applied to the acquisitions of supplies and 3,500,000 applied to 3,550,000 of the purchase orders in the total amount of 3,600,000 issued during the year. (assume consumption method).

a) Expenditures	6,700,000	
Inventory of supplies	900,000	
Vouchers payable		7,600,000
= To record expenditures for the year.		

Explanation- the expenditure ledger account is debited with all expenditures regardless of purpose except for **Additions to the Inventory of Supplies, Principal and Interest Payments on Debt, Additions to the Governmental Unit's Plant Asset, Payments for Goods or Services to be Received in the Future**, - all are debited to expenditure or other financing uses rather than to asset or liability ledger account. (Expenditure for debt principal and interest and plant asset additions are also recorded on a memorandum basis in the general long-term debt and general fixed assets account group respectively.

b) Fund Balance reserved for Encumbrance	3,550,000	
Encumbrance		3,550,000

= To reverse encumbrances applicable to vouchered expenditures,

Explanation- Recording actual expenditures of 3,500,000 (included in the 6,700,000 total in entry **5a** above) applicable to purchase orders totaling 3,550,000 makes this amount of the previously recorded encumbrances no longer necessary. Accordingly 3,550,000 of encumbrances is reversed. Encumbrances of 50,000 (3,600,000 - 3,550,000) remain outstanding.

6. Billings for services and supplies received from enterprise fund and internal service fund totaled 300,000 and 200,000 respectively.

Expenditures	500,000
Payable (Due) to Enterprise fund	300,000
Payable (Due) to Internal Service fund	200,000

= To record billings for services and supplies received from other funds.

Explanation- Billings from other funds of the governmental unit are not vouchered for

payment as are billings from outside suppliers. Instead billings from other funds are

recorded in a separate liability ledger account. the related debit is to the expenditure accounts if the billings are for **Quasi- external transaction** , such as providing services and supplies.

7. Cash payments on vouchers payable totaled 7,700,000. Cash payment to the Enterprise fund and the Internal service fund were 250,000 and 140,000 respectively.

Vouchers payable	7,700,000
Payable to Enterprise fund	250,000

Payable to Internal service fund	140,000
Cash	8,090,000

= To record payment of liabilities during the year

8. The town of X general fund made an operating transfer of 110,000 to the debt service

Fund for the matured principal and interests.

Other financing uses	110,000
Cash	110,000

= To record transfer to debt service fund for maturing principal and interest on

General obligation serial bond.

Explanation- The other financing uses ledger account is debited because the payment to the debt service fund is an **operating transfer** rather than **quasi-external transaction**.

9. A payment of 400,000 in lieu of property taxes and a subsidy of 100,000 were

Received from the Enterprise fund.

Cash	500,000
Revenue	400,000
Other Financing Sources	100,000

= To record payment in lieu of property taxes (400,000) and subsidy (100,000)

Received from Enterprise fund.

Explanation- amounts transferred to the general fund from other funds are recognized as revenues if they are **quasi-external transactions**, such as payment in lieu of property taxes; otherwise they are recognized as other financing sources if they are **operating transfers**, such as subsidies.

10. Supplies at a cost of 800,000 were used during the year.

Expenditures	800,000
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Inventory of supplies	800,000
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= To record cost of supplies used during the year.

Unreserved and undesignated fund balance	100,000
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Fund balance reserved for inventory of supplies	100,000
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= To increase inventory of supplies reserve to 500,000 to agree with
balance of inventory of supplies ledger account at end of year
(500,000 - 400,000 = 100,000)

Explanation- the immediately preceding journal entry represents a restriction of the portion of the fund balance account to or event its being appropriated improperly to finance a deficit annual budget for the general fund for the year ending June 30, year 7. Only cash and other monetary assets of a general fund are available for appropriation to Finance authorized expenditures of the succeeding fiscal year.

11. All uncollected property taxes on June 30 year 6 were delinquent.

Taxes Receivable- Delinquent	570,000
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Allowance for uncollectable Current Taxes	10,000
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	Taxes	Receivable-	Current
570,000			

Allowance for Uncollectable Delinquent Taxes	10,000
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= To transfer delinquent taxes and related estimated uncollectable amounts from the current classification

Explanation- The forgoing journal entry clears the Taxes Receivable-Current ledger account and the related contra account for uncollectable amounts so that they will be available for accrual of property taxes for the fiscal year ending June 30, year 7.

Unreserved and Undesignated Fund Balance	250,000
Fund Balance Designated for -	
Replacement of Equipment	250,000
= To designate a portion of the fund balance for the replacement	
of equipment during the year ending June 30, year 7.	

Is similar to a retained earnings appropriation of a business enterprise. It indicates that the annual budget for the town of X General fund for the year ending June 30, year 7 Must include an appropriation of 250,000 for new equipment and estimated revenue For the proceeds from the disposal of the replaced equipment. The designated Fund balance of 250,000 will be closed to the unreserved and undesignated fund balance Ledger account on July 1, year 6, when the annual budget for the year ending June 30 year 7 is recorded.

After all the forgoing journal entries (including the budget entry) have been posted to the general ledger of the town of X General Fund, the trial balance on June, 30 year 6 is as illustrated below.

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Allowance	for	Uncollectable	Delinquent	Taxes
10,000				
Inventory of Supplies			500,000	
Vouchers				Payable
700,000				
Payable	to		Enterprise	Fund
50,000				
Payable	to	Internal	Service	Fund
60,000				
Fund	Balance	Reserved	for	Encumbrances
50,000				
Fund	Balance	Reserved	for	Inventory of Supplies
500,000				
Fund	Balance	Designated	for	Replacement of Equipment
250,000				
Unreserved	and	undesignated	fund	balance
450,000				
Budgetary		Fund		Balance
300,000				
Estimated Revenues			8,400,000	
Estimated Other Financing Sources			100,000	
Appropriations				
8,100,000				
Estimated	Other	Financing		Uses
100,000				
Revenues				
8,480,000				
Other		Financing		Sources
100,000				
Expenditures			8,000,000	
Other Financing Uses			110,000	

Encumbrances	<u>50,000</u>
Total	<u>19,150,000</u>
	<u>19,150,000</u>

Financial statements for a General Fund

The results of operation (i.e, net income or net loss) are not relevant for a General Fund. Instead, two financial statements- a Statement of Revenues, Expenditures and Change in Fund Balance and a Balance Sheet are appropriate.

Assuming that the total revenue for the town of X is composed of the following sources,

General Property Tax	7,060,000
Licenses and Permits	450,000
Charges for Services	470,000
Fines and Forfeits	310,000
Miscellaneous Revenue	190,000

Also assume that the total expenditures is composed of the following items.

General Government	4,590,000
Public safety	2,000,000
Health and Welfare	1,200,000
Culture and Recreation	210,000

Town of X General fund

**Statement of Revenues, Expenditures and Change in Fund
Balance**

for the Year ended June 30, 19x6

	Budget	Actual
Variance- Favourable		
Revenues:		
(Unfavourable)		
General Property Tax	7,000,000	7,060,000
Licenses and Permits	400,000	450,000
Charges For Services	500,000	470,000
(30,000)		
Fines and Forfeits	300,000	310,000
Miscellaneous Revenue	<u>200,000</u>	<u>190,000</u>
(10,000)		
Total Revenues	<u>8,400,000</u>	<u>8,080,000</u>
Expenditures:		
General Government	4,700,000	4,590,000
110,000		
Public Safety	1,900,000	2,000,000
100,000		
Health an Welfare	1,100,000	1,200,000
(100,000)		
Culture and Recreation	<u>400,000</u>	<u>210,000</u>
190,000		
Total Expenditures	<u>8,100,000</u>	<u>8,000,000</u>
100,000		
Excess of Revenue over Expenditures-		
Other Financing sources (Uses):		
Operating Transfers In	100,000	100,000

Operating Transfers Out (10,000)	(100,000)	(110,000)
Excess of Revenue and O.F.S.- Over Expenditures and O.F.U.	300,000	470,000
170,000		
Add: Fund Balance, July 1, 19x5	<u>1,200,000</u>	<u>1,200,000</u>
—		
Fund balance June 30, 19x6	<u>1,500,000</u>	<u>1,670,000</u>
<u>170,000</u>		

**Town of X General Fund
Balance Sheet,
June 30, Year 6**

Assets

Cash		1,420,000
Taxes Receivable- Delinquent	570,000	
Less: Allowance for Uncollectable Taxes	<u>10,000</u>	560,000
Inventory of Supplies		<u>500,000</u>

Total Assets

2,480,000

Liabilities and Fund Balance

Liabilities

Vouchers Payable	700,000
Payable to Enterprise Fund	50,000
Payable to Internal Service fund	<u>60,000</u>
Total Liabilities	<u>810,000</u>

Fund Balance:

Reserved for Encumbrance	50,000	
Reserved for Inventory of Supplies	500,000	
Designated for Replacement of Equipment	250,000	
Unreserved and Undesignated	<u>870,000</u>	<u>1,670,000</u>
Total Liabilities and Fund Balance		<u>2,480,000</u>

Closing Entries for a General Fund

After the financial statements have been prepared for the town of X General fund, the budgetary and actual revenues, expenditures and encumbrance ledger accounts must be closed to clear them for the next fiscal year activities.

Unreserved and Undesignated Fund Balance	50,000	
Encumbrances		50,000
= To close encumbrance ledger account		
Appropriations	8,100,000	
Estimated Other Financing Uses	100,000	
Budgetary Fund Balance	300,000	
Estimated Revenues		8,400,000
Estimated Other Financing Sources		100,000
= To close budgetary ledger Accounts		
Revenue	8,480,000	
Other Financing Sources	100,000	
Expenditures		8,000,000
Other Financing Uses		110,000
Unreserved and undesignated Fund Balance		470,000
= To close Revenues, Expenditures, Other Financing Sources and Uses Ledger Accounts		

Explanation- The forgoing journal entries do not close the Fund Balance Reserved for Encumbrance Ledger account. Thus, the reverse represents a restriction on the fund balance on June 30 year 6 because the town of X General fund is committed in the fiscal year 7 to make estimated expenditures of 50,000 attributable to budgetary appropriations carried over from the fiscal year 6. If the fund balance reserved for encumbrance account had been closed, the unreserved and undesignated fund balance account would have been overstated by 50,000. The unreserved and Undesignated Fund Balance Ledger account balance must represent the amount of the General fund's Assets that is available for appropriation for a deficit budget in fiscal year 7. When expenditures applicable to 50,000 outstanding encumbrances on June 30 year 6 are vouchered for payment in the succeeding fiscal year, the fund balance reserved for encumbrance ledger account is debited for 50,000, the vouchers payable is credited for the amount to be paid, and the balancing debit or credit is entered in the unreserved and undesignated fund balance account.

The budgetary accounts are closed at the end of the fiscal year because they are no longer required for control over revenues, expenditures, and other financing sources and uses. The amounts in the journal entry that closed the budgetary accounts were taken from the original journal entry to record the budget at the beginning.

After June 30, year 6, closing entry for the town of X general Fund are posted, the unreserved and undesignated Fund Balance Ledger Account appears as shown below.

Unreserved and Undesignated Fund Balance

<u>Date</u>	<u>Explanation</u>	<u>Debit</u>	<u>Credit</u>
<u>Balance</u>			
Year 5			

	June 30	Balance
800,000		

Year 6		
June 30	Increase in the amount reserved	100,000
700,000		
	for Inventory of supplies	

30	Designation for replacement of equipment	250,000
450,000		

30	Close encumbrances ledger account	50,000
40,000		

30	Close Excess of Revenue and Other Financing Sources over Expenditures and Other Financing Uses	47,000
87,000		
=====		
=====		

Accounting for Special Revenue Funds

The distinguishing feature of a special revenue fund is that its revenues are obtained primarily from tax and non-tax sources not directly related to services rendered or facilities provided for use. Separate special revenue funds are established by governmental units as mandated by legislative enactments., to account for the receipts and expenditures associated with specialized revenue sources that are earmarked by law or regulation to finance specified governmental operations. Ledger account titles, budgetary processes and financial statements for a special revenue funds are similar to those of General funds.

Illustration

To illustrate the accounting for a Special Revenue Fund, Assume that on July 1, year 6, The town council of the town of X authorized the establishment of a special Revenue Fund- its first such fund- to account for Special Assessment against certain residents of the neighboring village of Y. Because the property tax revenue of the town of X, which among other services financed street cleaning and street light maintenance for residents of the town only, could not be used for such services elsewhere, the town council authorized special assessment to finance comparable services for the requesting residents of the village of Y. the town council adopted a budget for the special revenue fund for the year ending June 30 year 7, providing for estimated revenues (from the special Assessments) of 800,000 and appropriations for reimbursement to the General fund for expenditures made by that fund for the services provided to the village of Y residents) of 75,000.

Following are additional transactions or events of the town of X special revenue fund for the year ending June 30 year 7.

1. On July 1, year 6, the town recorded the adopted budget in the books.

Estimated Revenues	800,000
Appropriations	750,000
Budgetary Fund Balance	50,000

= To record the annual adopted budget for fiscal year ending June 30 year 7.

2. Special Assessments tax totaling 820,000 were levied which are to be paid in full in sixty days.

Special Assessment Tax Receivable- current	820,000
Revenues	820,000

= To record special assessments billed, all of which are estimated to be collectable

3. Cash Receipts from Special Assessment Taxes of 820,00 were collected in full.

Cash	820,000
Special Assessment Tax Receivable- current	820,000

= To record collection of special assessment tax in full during the year.

4. Of the cash receipts, 630,000 was invested in Treasury bills with face amount of

650,000. The treasury bills mature on June 30 year 7 and were redeemed in full on that date.

Short Term Investments	630,000
Cash	630,000

= To record acquisition of 65,000 face amounts of treasury bills,

Cash	650,000
Short Term investments	630,000

Revenues 20,000

= To record receipts of cash for matured U.S treasury bills.

Maturity June 30, year 7.

5. Billings from the town of X General fund, requesting reimbursement of expenditures of that fund, totaled 760,000; of that amount, 620,000 was paid to the General Fund by

June 30, year 7.

Expenditures 760,000

Payable to General Fund 760,000

= To record billings from general fund for reimbursement of expenditures for street cleaning and street light maintenance for residents of the village of Y

Payable to General Fund 620,000

Cash 620,000

= To records payments of general fund during the year.

6. On June 30, year 7, the town council of the town of x designated the fund balance

of the Special revenue fund(80,000) for reimbursement of the General Fund during

the year ending June 30, year 8.

Unreserved and Undesignated fund balance 80,000

Fund Balance Designated for -

Reimbursement of General Fund 80,000

= To designate the entire fund balance for reimbursement of General Fund during the year ending June 30 year 8.

Because of the 760,000 billings of the town of X General Fund to the Special Revenue Fund were for reimbursement of General fund expenditures, the general fund credited its expenditures ledger account

in the journal entry in which it debited receivable from Special Revenue fund.

Closing Entries

Appropriations	750,000	
Budgetary Fund Balance	50,000	
Estimated Revenues		80,000

= To close budgetary ledger accounts.

Revenue	840,000	
Expenditures	760,000	
Unreserved and Undesignated- fund balance	80,000	

= To close revenue and expenditures ledger account

Financial Statements for a special revenue funds

The financial statements for a special Revenue funds is the same as that of a General fund-a statement of Revenues, Expenditures and change in Fund Balance and a Balance sheet. Following are the financial statements for the town of X Special Revenue fund for the year ended June 30, year 7:

Town of X - Special Revenue Fund

Statement of Revenues, Expenditures and Changes in Fund Balance

For the year ended June 30, year 7

Favourable

	Budget	Actual	Variance
(Unfavourable)			
Revenues:			
Special Assessments	800,000	820,000	20,000
Other	<u>-</u>	<u>20,000</u>	<u>20,000</u>

Total Revenues	<u>800,000</u>	<u>840,000</u>	<u>40,000</u>
Expenditures			
Reimbursement of General Fund-			
expenditures	<u>750,000</u>	<u>760,000</u>	<u>(10,000)</u>
Excess of Revenues over Expenditures	<u> .</u>	<u> .</u>	<u> .</u>
(Fund Balance End of year)-----	<u>50,000</u>	<u>80,000</u>	<u>30,000</u>

Town of X Special Revenue fund

Balance Sheet

June 30, year 7

Assets

Cash ----- 220,000

Liabilities and Fund Balance

Payable to General fund ----- 140,000

Fund Balance Designated for Reimbursement of General fund ----- 80,000

Total Liabilities and Fund Balance ----- 220,000

3.5 TERMINOLOGY AND CLASSIFICATION FOR GOVERNMENTAL FUND BUDGETS AND ACCOUNTS

I. Classification of Appropriations and Expenditures

The term, appropriations and expenditure, both have to do with resources, which are used by a governmental entity. The relation between the two is that an appropriation is the authorization to make expenditure. In reality, an appropriation is actually both an authorization to spend and at the same time a limitation on spending. An appropriation, when enacted by law is an authorization to incur on behalf of the governmental unit liabilities for, goods, services and facilities to be used for purposes specified in the appropriation ordinance, or statute, in amounts not in excess of those specified for each purpose. The budgeted appropriations are often called ***estimated expenditures***, and the appropriation budget is called ***expenditure budget***.

According to GASB's Principles, Expenditures should be classified by: -

1. Fund
2. Function or program
3. Organization unit
4. Activity
5. Character
6. Object

1. Classification by Fund

The primary classification of governmental expenditure is by fund, since funds are the basic fiscal & accounting entity of governmental unit.

Eg. G, F, SRF, CPF, DSF

2. Classification by Function or Programme

Functions are group related activities that are aimed at accomplishing a major service or regulatory responsibility. Programmes are group

activates, operation on organizational units that are directed to the attainment of specified purposes or objectives generally speaking, function refers to what is done programme refers to the means by which it is done.

E.g. The G.F. may -have the following programmes or functions.

- General Governmental
- Public safety
- Health & welfare
- Culture & recreation

3. Classification by organization unit

To carry out the broad functions or programmes, responsibility is divided to smaller units or departments. This helps with affixing specific accountability.

E.g. - Police dept

- Fire dept
- Public works dept
- Parks & recreation dept

The key distinction between the classification of expenditures by organizational unit & Classification by programmes or functions is that responsibility for a dept is fixed, where as a number of depts. may be involved in the performance of a programme or a function.

4. Classification by activity

An activity is a specific & distinguishable line of work performed by an organizational unit to fulfill the overall goals of the programme or function. For example, within the police dept, activities such as the following may be performed.

- Crime control by -- Foot patrol
Car Patrol
- Traffic control by -- Traffic

5. Classification by character

This classification has to do with the expenditure itself than the department or fund in which it is incurred. the character of an expenditure is either.

- Current expenditure - meant to benefit the current period only.
- i Capital expenditure - benefits the current period plus other periods the future.
- i Debt service expend - includes payment of interest or debt & payment of debt principal that arises from past period benefits which may also be expected to benefit the current and future period.

6. Classification by object

Object of expenditure is the thing for which the expenditure was made. It is mainly a concern of current period expenditures.

E.g. Personal services

Other services & charges

Supplies

Capital outlays

Addis Ababa city council G.F

Public safety ——— programmes /function

Police dept ——— organization unit

Crime control ——— activity

Current expend. ——— character

Supplies ——— object

II. Classification of Estimated Revenues & Revenues

Revenues are defined, as all increases in fund net Assets except those arising from inter fund transfers and from proceeds of long-term debt. A governmental unit and the funds thereof, may raise revenue only from sources available to them by law.

The primary classification of governmental revenues is by fund. Within each fund, the major classification is, by source. Major revenue source classes are: -

1. Taxes
 2. Licenses & permits
 3. Inter governmental revenues
- i Charges for services
 - i Fines & forfeits
 - i Miscellaneous revenues

1. Taxes

Taxes are a forced contribution imposed on the citizens by the government. There are a number of different kinds of taxes possible, including property (land use) sales, excise, income, customs, and capital gain etc....

Giving a formal notice of a tax to be paid is called a levy. A tax levy, especially on goods or property also typically creates a Lien, which gives the taxing authority, the power to confiscate the goods or property in the event of a non- payment of the tax.

Incorrect calculation of taxes by the tax payer may result in penalties. Taxes, which are not paid on time usually, include accrued interest on any unpaid balance. These penalties & interest create an additional revenue source for the government.

In addition to revenue accounts, the following accounts may also be needed to account for tax collections; Taxes Receivables Current, Taxes Receivable Delinquent, Tax Lien Receivable, Interest & Penalties Receivable on Delinquent Taxes (all four are assets), Deferred Taxes,

Trust for property owners (Both are Liabilities), Allowance for Uncollectable Taxes (contra-Asset). any uncollected taxes are accounted for as a reduction of revenue.

The deferred taxes account is credited for taxes, which are paid in a year before they may legally be used for expenditure. The Taxes Receivable Current account is used to accrue taxes, which are due in the current year. The taxes receivable Delinquent account is used to accrue taxes, which are due in the current year. The Taxes Receivable Delinquent account is used to record any taxes, which are, past due. The Taxes Lien- Receivable account is used to record taking possession of goods on which an owed tax has not been paid. If those possessed goods are sold in an attempt to cover the tax & any additional cost incurred in collecting it, The Trust for Property Owners account is used to record any balance remaining from the selling price after the tax & collection cost are deducted. The Interest & Penalties Receivable on delinquent taxes account is used, obviously, to record interest & penalties due on unpaid taxes.

2. Licenses and permits

Licenses and permits may be divided into two categories.

- i Business - like merchants licenses, customs clearing Agency licenses, professional (physician, attorney)
- i Non business - like driving licenses, hunting license, Residential permits
- i Revenue from licenses & permits are accounted on the cash basis.

i 3. Intergovernmental Revenue

- i Intergovernmental revenues include Grants, Entitlements & Shared Revenues.

- i **a) Grant** is money, which is given for a specific purpose & it should be classified according to both its source & its purpose. A grant could be given from the federal government to regional state government (called a subsidy) or from a foreign government to the federal government. Grants can be divided into two types.
- i b) **Shared revenues** is a revenue levied by one government but shared on a predetermined basis, often in proportion to the amount collected at the local level, with another government or class of government. It should be accrued unless there are matching or specific spending requirements.
- i **Entitlement** is the amount of payment to which a state or local government is entitled as determined by the federal government pursuant to an allocation formula

4. Charges for services

Charges for services include revenue from charges for all activities of a governmental unit, except the operations of enterprise funds.

E.g. court costs, special parking meters.

It should be recognized as revenue when earned, if that is prior to the collection of cash.

5. Fines & forfeits

Fines & forfeits are penalties, which are paid to governmental unit, usually as punishment for violating the law. It is accounted on a cash basis.

6. Miscellaneous revenue

Any revenue types that do not fit one of the above five classifications.

E.g. interest income on investments – should be accrued

- i Sales of fixed assets
- i Insurance claim
- i Contribution from private individuals

3.6 INTERFUND TRANSACTIONS AND TRANSFERS

Inter fund transactions are transactions between different entities within the governmental unit. they need to be recorded in two different sets of books.

i Inter fund loans & advances

Often funds sometimes loan or advance money to each other in order to use idle cash effectively. Short Period (one year or less is commonly used), the borrowing is called **a loan**; For longer periods, the borrowing is called **an advance**.

Due from SRF	xxx
Cash	xxx
Cash	xxx
Due to the GF	xxx

2) Quasi -external transaction

These are transactions that would be treated as Revenue, Expenditures or Expenses if they involved organizations external to the governmental unit. They are the type of interfund transactions which are considered as revenue & expenditure within the entity. The most meaningful form of reporting for such transactions is to report expenditure in the fund receiving the services & report revenues in the fund providing the services, b/c the fund receiving the services would have had to change expenditures if it had obtained the services for an organizations external to the governmental unit.

GF

Expenditure	xxx
Due to ISF	xxx

SRF

Due from GF	xxx
Revenues	xxx

3) Reimbursements

Are transactions that reimburse a fund for expenditures made by it on behalf of another fund i.e. one fund pays a bill on behalf of another & is then reimbursed.

Expenditure	xxx
Cash	xxx

= To record payment of bill on behalf of ---

Cash	xxx
Expenditure	xxx

= To record reimbursement

4) Residual Equity transfers

Residual Equity transfers are non-recurring or non-routine transfers of equity between funds made in connection with the formation, expansion, contract or discontinual of a fund. not only are they not Revenues or Expenditures, they are not Other Financing Sources or Uses, even though they are technically increase / decreases in fund financial resources.

Equity transfer out	xxx
Due to ISF	xxx

Due from GF	xxx
Equity transfer in	xxx

5) Operating transfers

Operating transfers are made in connection with the normal operation of the recipient fund. They are legally authorized transfers from a fund, which receives revenue to the fund through which the resources are to be

expended. These transfers are other financing source of the receiving fund, other financing uses of the paying fund.

Other Financing Uses-Operating Transfers Out	xxx
Due to DSF	xxx
Due from GF	xxx
Other Financing Sources-Operating Transfers In	xxx

- 4 & 5 are properly called transfers & 1,2,3 are merely transfers.

Check Your Progress

1. Compare and Contrast General Fund and Special Revenue funds.

2. Discuss the reservation and designation of the fund balance account of the governmental unit's General Fund and special Revenue fund.

3. What are the principal differences between the financial statements of the governmental units general fund and the financial statements of a business enterprise?

4. What does a budget include in a governmental units general fund and special revenue funds.

5. Describe the classification of Governmental funds revenue and expenditures?

6. What revenues of general fund Generally accrue?

7. Discuss the use of Encumbrance as a budgetary control account.

8. Describe how expenditures are recorded and exceptions which are recorded separately.

9. Describe accounting for supplies in governmental entities general fund and special revenue fund.

10. Describe the interfund transfer and transactions in The governmental funds?

3.7 SUMMARY

Even though the General fund and the special Revenue fund have different Purposes, they are both revenue funds and the accounting and reporting procedure is the same for both. They are very similar in that all or almost all of their resources are expended each year and then filled up in the next year. Understanding the accounting and characteristics of General fund with an exception of few points will enable us to have a clearer understanding of both funds.

3.8 ANSWERS TO CHECK YOUR PROGRESS QUESTIONS

- 1 Refer to the topic 3.1
- 1 Refer to the topic 3.4
- 1 Refer to the topic 3.2 & 3.4
- 1 Refer to the topic 3.3
- 1 Refer to the topic 3.5 I & II
- 1 Refer to the topic 3.5 II
- 1 Refer to the topic 3.3 & 3.4
- 1 Refer to the topic 3.2
- 1 Refer to the topic 3.4
- 1 Refer to the topic 3.6