



Chapter 3

Governmental Operating Statement Accounts; Budgetary Accounting

Learning Objectives

After studying Chapter 3, you should be able to:

- ≈ Explain how operating revenues and expenses related to governmental activities are classified and reported in the government-wide financial statements
- ≈ Distinguish, at the fund level, between Revenues and Other Financing Sources and between Expenditures and Other Financing Uses
- ≈ Explain how revenues and expenditures

Learning Objectives (Cont'd)

- ≈ Explain how budgetary accounting contributes to achieving budgetary control over revenues and expenditures, including such aspects as:
- Recording the annual budget.
 - Accounting for revenues.
 - Accounting for encumbrances and expenditures.
 - Accounting for allotments.
 - Reconciling GAAP and budgetary accounts.

Learning Objectives (Cont'd)

- ≈ Describe computerized accounting systems
- ≈ Explain the classification of revenues and expenditures of a public school system

Government-wide Statement of Activities

Expenses should be reported by function or program.

- ❖ *Direct expenses* - those associated with a function or program
- ❖ *Indirect expenses* - those that are not directly linked to an identifiable function

Revenues should be distinguished between

- ❖ *Program revenues* - reported in the program/functions section of the statement
- ❖ *General revenues* - not directly linked to any program/function and reported in a separate section at the bottom of the statement

Government-wide Statement of Activities (Cont'd)

- ❖ Program revenues are reported in three categories: (see III. 3-1 & 1-5)
 - Charges for services
 - Operating grants and contributions
 - Capital grants and contributions

- ❖ A net expense or revenue format is used in the top section of the statement of activities: Expenses - Program Revenues = Net (Expense) Revenue

Government-wide Statement of Activities (Cont'd)

Extraordinary items, special items, and transfers are reported as separate line items near the bottom of the government-wide statement of activities (see Ill. 3-1 and 1-5)

- ❖ *Extraordinary items* are items that are *both* unusual in nature and infrequent in occurrence, and usually are beyond the control of management
- ❖ *Special items* are either unusual or infrequent, and must be *within the control* of management

The General Fund

Purpose

- ❖ Used to account for the general administration and most traditional services of government

Examples of traditional services

- ❖ Public safety (e.g., police and fire)
- ❖ Public works (e.g., maintenance of buildings, roads, and bridges)
- ❖ Culture and Recreation (e.g., promotion of the arts, parks, and youth activities)
- ❖ Health and welfare (e.g., public health, food facilities inspection, and juvenile counseling)



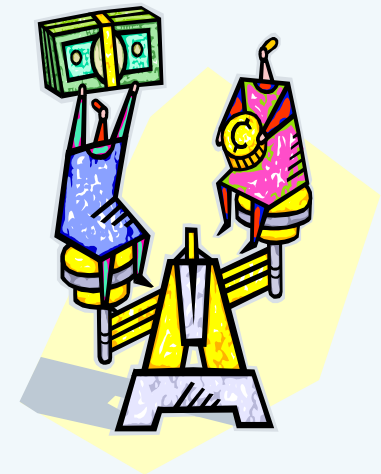
Budgetary Accounts

Purpose

- ❖ Used to record the budgetary inflows and outflows estimated or authorized in the annual budget

Accounts

- ❖ Estimated Revenues, Estimated Other Financing Sources
- ❖ Appropriations, Estimated Other Financing Uses
- ❖ Encumbrances



Fund Equation for the General Fund

$$\text{ASSETS} = \text{LIABILITIES} + \text{FUND BALANCES}$$

Balance
Sheet

Accounts
(permanent)
Budgetary/
Operating
Accounts
Statement
Accounts
(temporary)

Reserved + Unreserved
Fund Balances Fund Balance

Budgetary Accounts Operating

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graph TD; FB[Fund Balances] --> RB[Reserved Fund Balances]; FB --> UB[Unreserved Fund Balance]; UB --> BA[Budgetary Accounts]; UB --> OP[Operating Accounts];
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Budgetary and Operating Statement Accounts (Cont'd)

- Distinguish between *Revenues* and *Other Financing Sources* and *Expenditures* and *Other Financing Uses*
 - *Other Financing Sources* represent operating transfers in from other funds and proceeds of long-term borrowing
 - *Other Financing Uses* represent operating transfers out to other funds

Budgetary and Operating Statement Accounts (Cont'd)

- ❖ *Revenues and Other Financing Sources* increase fund balance when closed. Recognized on the *Modified Accrual* basis—when measurable and available to pay current period obligations
- ❖ *Expenditures and Other Financing Uses* decrease fund balance when closed. Recognized on the *Modified Accrual* basis—when incurred, if expected to be repaid from currently available resources¹²

Budgetary and Operating Statement Accounts (Cont'd)

- ❖ An *appropriation* is a legal authorization granted by the legislative body to incur liabilities for purposes specified in the appropriation act or ordinance
- ❖ An *encumbrance* is an estimated amount recorded for purchase orders, contracts, or other expected expenditures chargeable to an appropriation



Budgetary Control—Expenditures

- ❖ Budgetary control of expenditures is achieved by:
 - ensuring that a valid appropriation exists prior to recording an encumbrance or expenditure, and
 - periodically comparing encumbrances and expenditures to appropriations to prevent overspending
- ❖ Comparison is enhanced by using the same account classification scheme for appropriations, encumbrances, and expenditures

Classification of Expenditures and Appropriations

- ❖ Fund
- ❖ Function or Program
- ❖ Organization Unit
- ❖ Activity
- ❖ Character (Current, Capital, Debt Service)
- ❖ Object

What Purpose is Served by Each Classification?

- ❖ **Fund**—Denotes which fiscal and accounting entity was affected
- ❖ **Function or Program**—Assists in budgeting resources for carrying out major areas of service activities or goals
- ❖ **Organization Unit**—Assists in enhancing managerial control and responsibility accounting

What Purpose is Served by Each Classification? (Cont'd)

- ❖ **Activity**—Assists in assessing performance on specific lines of work and determining cost of activities
- ❖ **Character**—Assists in evaluating which period is benefited by an expenditure: past, current, or future
- ❖ **Object**—Assists in determining how much was expended for specific things, such as personnel and equipment

Budgetary Control— Expenditures (Cont'd)

Accounting Control over Expenditures

- ❖ Three *control* accounts (Appropriations, Encumbrances, and Expenditures) are used to control similarly named columns of the detail budget accounts in the subsidiary ledger (see Ill. 3-8)
- ❖ The detail account totals for Appropriations, Encumbrances, and Expenditure in the subsidiary ledger must equal the corresponding general ledger control account balances

Budgetary Control—Revenues

- ❖ Periodically compare actual revenues (or actual other financing sources) to estimated revenues (or estimated other financing sources)
- ❖ Use a common classification scheme for revenues and estimated revenues

Budgetary Control—Revenues (Cont'd)

Accounting Control over Revenues

- ❖ Two *control* accounts (Estimated Revenues and Revenues) are used to control similarly named columns in the detail accounts in the revenue subsidiary ledger (see III. 3-7)
- ❖ The sum of the Estimated Revenues and Revenues account balances of the subsidiary ledger must equal the general ledger control account balances for those accounts

Classification of Revenues and Estimated Revenues

- ❖ By fund
- ❖ By source
 - Taxes (Ad-valorem and self-assessing)
 - Special Assessments
 - Licenses and Permits
 - Intergovernmental Revenues
 - Charges for Services
 - Fines and Forfeits
 - Miscellaneous Revenues

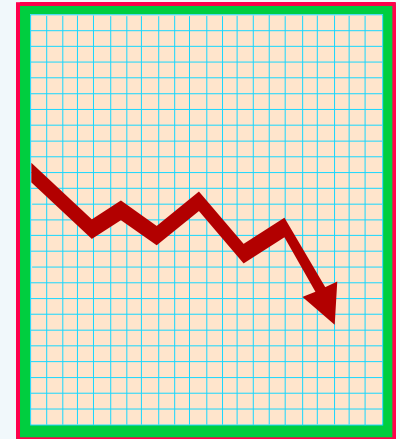
Revenues–Taxes (Ad valorem and Self-assessing)



- ❖ Ad valorem taxes are assessed on the value of underlying property—e.g. personal and real property taxes
- ❖ Self-assessing taxes are based on income or sales. Taxes due on sales or earnings that have occurred but are not yet reported at the end of an accounting period are usually estimated and accrued

Revenues—Property Taxes (Cont'd)

- ❖ If rates are below the statutory limit, property taxes may be viewed as a residual source of revenues (see Ill. 3-6)
- ❖ The gross tax levy is calculated as the amount of revenue required from property taxes divided by the estimated collectible portion of the levy (e.g., .96)



Revenues—Special Assessment Taxes

- ❖ Levied against certain properties that receive a particular benefit that not all taxpayers receive.
- ❖ Examples include street repair, street cleaning, or snow plowing for taxpayers who live outside the normal service area



Revenues—Licenses and Permits

- ❖ Includes items such as vehicle licenses, business licenses, liquor licenses, marriage licenses, animal licenses, building permits, zoning variances, etc.
- ❖ Ordinarily not measurable in advance of transactions; thus, recorded when received in cash



Revenues—Intergovernmental

- ❖ Includes grants and other financial assistance from higher levels of government
- ❖ Intergovernmental revenues such as grants are normally not recognized until all time and eligibility requirements have been met. Expenditure-driven (reimbursement-type) grants typically require qualifying expenditures be made before recognizing



Revenues—Charges for Services

- ❖ Many governments have shifted much of their revenues from taxes on all taxpayers to charges to recipients of services, including charges for recreational services, building inspections, etc.
- ❖ Accrue if billings for service occur before receipt of cash



Revenues—Fines and Forfeits

- ❖ *Fines* are amounts assessed by the courts against those guilty of statutory offenses and neglect of official duties
- ❖ *Forfeits* arise from deposits or bonds made by contractors, accused felons, and others to assure performance on contracts or appearance in court
- ❖ Accrue if the amount is known prior to the receipt of cash



Revenues—Miscellaneous

- ❖ These are revenues that do not fall into one of the other categories, such as:
 - proceeds from the sale of government assets (if small in amount; OFS otherwise)
 - investment income
- ❖ Accrue if the amount is known prior to the receipt of cash

Examples of Budgetary Journal Entries

Budget Approved on 1-1-2008:

Dr.

Estimated Revenues	500,000
Appropriations	450,000
Fund Balance	50,000

Estimated Revenues Ledger:

Taxes	300,000
Licenses and Permits	50,000
Intergovernmental Revenues	50,000
Charges for Services	50,000
Fines and Forfeits	25,000
Miscellaneous Revenues	25,000

Appropriations Ledger:

General Government	120,000
Public Safety	150,000
Public Works	100,000
Culture and Recreations	80,000

Subsidiary Ledgers for Budgetary Control

Revenue Subsidiary Ledger

Acct No. XXX

Account Name: Charges for Services

Estimated Actual
Revenues Revenues Balance

<u>Date</u>	<u>DR (CR)</u>	<u>Explanation</u>	<u>Folio</u>	<u>DR</u>	<u>CR</u>
1-1-2008	Budget authority	GJ71	50,000		50,000
1-31-2008	Various items	CR82		4,000	46,000
2-28-2008	Various items	CR87		5,000	41,000

Examples of Budgetary Control

Example: City Clerk's office orders a new printer on January 2, 2008 which had a list price in the vendor's catalog of \$500.

Entry in the General Fund General Journal:

Dr.

Cr.

Encumbrances—2008

500

Reserve for Encumbrances—2008

500

Examples of Budgetary Control

Printer is received on 1-15-2008, including shipping charges of \$15:

Entry in GF General Journal:

<u>Dr.</u>	<u>Cr.</u>	
Reserve for Encumbrances—2008		500
Expenditures—2008	515	
Encumbrances—2008		500
Vouchers Payable	515	

Subsidiary Ledgers for Budgetary Control

Appropriations/Encumbrances/Expenditures Subsidiary Ledger

Acct No. XXX

Account Name: General Government, City Clerk ,

Equipment

Available

		Appropriations	Expenditures	Encumbrances	
Balance					
Date	Explanation	CR (DR)	DR (CR)		
DR (CR)	CR (DR)				
1-1-08	Budget authority		1,500		1,500
1-2-08	P.O. No. 98-41		500	1,000	
1-15-08	Voucher No. 1125 985		515		(500)

Accounting for Allotments

- ❖ Allotments are internal allocations of funds by executive management to quarters or other time periods
- ❖ Some modification of the appropriations subsidiary ledger is required to add an Unallotted Appropriations column in each detail account (See text)



Computerized Accounting Systems

Computerized accounting systems have evolved to meet the fund accounting needs of government



- ❖ Revenue and expenditure classifications are achieved through the use of an account number having different segments or fields
- ❖ A current challenge is redesigning fund-based accounting information systems to accommodate the government-wide accounting and financial reporting required by *GASBS*

Concluding Comments

- ❖ The General Fund and special revenue funds usually require a legally adopted budget before the government can collect revenues from taxes and other sources and incur expenditures
- ❖ Legal penalties may exist for failure to comply with the budget, so it is imperative that the accounting system facilitate accounting for the budget as well as all other operating transactions.