Accounting for Governmental & Nonprofit Entities

Seventeenth Edition

Jacqueline L. Reck, Ph.D., CPA
James E. and C. Ellis Rooks Distinguished Professor in Accounting
University of South Florida

Suzanne L. Lowensohn, Ph.D., CPA, CGMA
Associate Professor of Accounting
Colorado State University

McGraw Hill Education
# Table of Contents

**Preface vi**

**Chapter 1**

**Introduction to Accounting and Financial Reporting for Governmental and Not-for-Profit Entities 1**

Welcome to Governmental and Not-for-Profit Accounting 1
What Are Governmental and Not-for-Profit Organizations? 2
Distinguishing Characteristics of Governmental and Not-for-Profit Organizations 3
Sources of Financial Reporting Standards 4
Objectives of Financial Reporting 5
Overview of Financial Reporting for State and Local Governments, the Federal Government, and Not-for-Profit Organizations 7

*Financial Reporting of State and Local Governments* 7

*Financial Reporting of the Federal Government* 10

*Financial Reporting of Not-for-Profit Organizations (NFPs)* 11

Expanding the Scope of Accountability Reporting 12
Overview of Chapters 2 through 17 12

*GASB Principles, Standards, and Financial Reporting* 12

Accountability for Public Funds 13
Not-for-Profit Organizations and the Federal Government 13

A Caveat 13
Key Terms 14
Questions 14
Cases 15
Exercises and Problems 16

**PART ONE**

State and Local Governments 21

**Chapter 2**

**Principles of Accounting and Financial Reporting for State and Local Governments** 23

Activities of Government 24
Financial Reporting Model 25

*Elements and Measurement* 25

Government-wide Financial Statements 27
Fund Financial Statements 29
Fund Reporting 31

*Fund Categories* 31

Classification of Fund Balances 35

Major Fund Reporting 36

Summary of Government-wide and Fund Characteristics 38
Appendix A: Illustrative Financial Statements for City and County of Denver, Colorado 40
Appendix B: Summary Statement of Governmental Accounting and Financial Reporting Principles 54

Key Terms 58
Selected References 59
Questions 59
Cases 59
Exercises and Problems 62

**Chapter 3**

**Governmental Operating Statement Accounts; Budgetary Accounting** 67

Classification and Reporting of Expenses and Revenues at the Government-wide Level 68

Reporting Direct and Indirect Expenses 68

Program Revenues and General Revenues 70

Reporting Special Items and Transfers 71

Structure and Characteristics of the General Fund and Other Governmental Funds 72

Governmental Fund Balance Sheet and Operating Statement Accounts 72

Reporting Budgeted and Actual Results 75

Terminology and Classification for Budgetary and Operating Statement Accounts 78

Classification of Appropriations and Expenditures 78

Classification of Estimated Revenues and Revenues 81

Budgetary Accounting 86

Recording the Budget 86
Chapter 4
Accounting for Governmental Operating Activities—Illustrative Transactions and Financial Statements 111

Illustrative Case 112
Measurement Focus and Basis of Accounting 112
Dual-track Accounting Approach 114
Illustrative Journal Entries 115
Recording the Budget 115
Encumbrances and Purchasing Transactions 115
Payment of Liabilities 117
Payrolls and Payroll Taxes 118
Accounting for Property Taxes 120
Other Revenues 124
Tax Anticipation Notes 125
Forecasting Amount of Tax Anticipation Borrowing 126
Repayment of Tax Anticipation Notes 126
Special Topics 127
Correction of Errors 127
Receipt of Goods Ordered in Prior Year 128
Revision of the General Fund Budget 129
Exchange Transactions with Proprietary Funds 130
Supplies Purchased from an Internal Service Fund 130
Services Provided by an Enterprise Fund 132
Adjusting Entries 133
Pre-Closing Trial Balance 135
Closing Entries 136
Reclassification of Fund Balances 137
General Fund Financial Statements 138
Special Revenue Funds 141
Accounting for Operating Grants 141

Chapter 5
Accounting for General Capital Assets and Capital Projects 167

Accounting for General Capital Assets 168
Required Disclosures about Capital Assets 169
Classification of General Capital Assets 170
General Capital Assets Acquired under Capital Lease Agreements 174
Costs Incurred after Acquisition 176
Reduction of Cost or Asset Disposal 176
Asset Impairments and Insurance Recoveries 178
Service Concession Arrangements 178

Capital Projects Funds 179
Illustrative Transactions—Capital Projects Funds 180
Illustrative Financial Statements for a Capital Projects Fund 185
Alternative Treatment of Residual Equity or Deficits 186
Bond Premium, Discount, and Accrued Interest on Bonds Sold 186
Retained Percentages 188
Claims and Judgments Payable 189
Bond Anticipation Notes Payable and the Problem of Interest Expenditures 189
Investments 191
Multiple-Period and Multiple-Project Funds 191
Capital Projects Financed by Special Assessments 192
Financial Reporting for Capital Projects Funds 193
Key Terms 194
Selected References 194
Questions 194
Cases 195
Exercises and Problems 196

Chapter 6
Accounting for General Long-term Liabilities and Debt Service 205

General Long-term Liabilities 206
  Accounting for Long-term Liabilities 206
  Long-term Liability Disclosures 207
  Debt Limit and Debt Margin 207
  Overlapping Debt 211
Debt Service Funds 216
  Number of Debt Service Funds 216
  Use of General Fund to Account for Debt Service 217
  Budgeting for Debt Service 217
  Types of Serial Bonds 218
  Debt Service Accounting for Term Bonds 224
  Financial Reporting 228
  Accounting for Bond Premiums and Accrued Interest 229
Valuation of Debt Service Fund Investments 231
Deposit and Investment Disclosures 232
Debt Service Accounting for Special Assessment Debt 233
Use of Debt Service Funds to Record Capital Lease Payments 235
Accounting for Debt Refunding 237
Advance Refunding of Debt 237
Other Long-term Liabilities 238
  Compensated Absences 239
  Pollution Remediation Obligations 239
  Claims and Judgments 240
Key Terms 240
Selected References 240
Questions 240
Cases 241
Exercises and Problems 244

Chapter 7
Accounting for the Business-type Activities of State and Local Governments 253

Proprietary Funds 254
  Assets Acquired under Lease Agreements 254
  Financial Reporting Requirements 255
Internal Service Funds 257
Illustrative Case—Supplies Fund 258
Illustrative Statements Using Supplies Fund 263
External Financial Reporting of Internal Service Funds 265
Dissolution of an Internal Service Fund 266
Special Topics Associated with Internal Service Funds 266
Enterprise Funds 269
Water Utility Funds 270
  Current and Accrued Assets 271
  Restricted Assets 272
  Utility Plant 272
  Current Liabilities 273
  Liabilities Payable from Restricted Assets 273
  Long-term Liabilities 273
  Net Position 274
Illustrative Case—Water Utility Fund 274
Illustrative Statements Using Water Utility Fund 280
External Financial Reporting of Enterprise Funds 282
Appendix: Special Topics in Accounting for the Business-type Activities of State and Local Governments 284
Key Terms 288
Selected References 288
Questions 288
Cases 288
Exercises and Problems 292

Chapter 8
Accounting for Fiduciary Activities—Agency and Trust Funds 303

Agency Funds 304
  Agency Fund for Special Assessment Debt Service 304
Tax Agency Funds 305
  “Pass-through” Agency Funds 311
Financial Reporting of Agency Funds 312
Trust Funds 312
Investment Pools 312
  Creation of an Investment Pool 313
  Operation of a Cash and Investment Pool 316
Withdrawal of Assets from the Pool 320
Closing Entry 321
Illustrative Financial Statements 322
Private-purpose Trust Funds 322
Pension Trust Funds 323
Contents

General Characteristics of Governmental Pension Plans 324
Required Financial Reporting for Defined Benefit Pension Plans 326
Illustrative Transactions for a Defined Benefit Pension Plan 331
Employer's Pension Accounting 334
Employer Recording and Reporting of Pension Expenditure/Expense 336
Other Postemployment Benefits (OPEB) 336
Termination Benefits 337
Appendix: Managing Investments 337
Key Terms 338
Selected References 338
Questions 339
Cases 339
Exercises and Problems 340

Chapter 9
Financial Reporting of State and Local Governments 351
Providing Useful Financial Reports 351
The Governmental Reporting Entity 352
Defining the Financial Reporting Entity 353
Component Units 354
Reporting by Other Government Organizations 357
Governmental Financial Reports 357
Need for Periodic Reports 358
Interim Financial Reports 358
Annual Financial Reports 359
Preparation of Basic Financial Statements 361
Fund Financial Statements 368
Required Reconciliations 369
Intra-entity Transactions 372
Other Financial Reporting Issues and Topics 372
Popular Reporting 373
Other Comprehensive Basis of Accounting (OCBOA) 374
International Accounting Standards 374
Appendix A: Converting Accounting Information from the Modified Accrual to the Accrual Basis of Accounting 375
Appendix B: Management's Discussion and Analysis (MD&A)—City and County of Denver 379
Key Terms 390
Selected References 391
Questions 391
Cases 391
Exercises and Problems 397

PART TWO
Accountability for Public Funds 405

Chapter 10
Analysis of Governmental Financial Performance 407
The Need to Evaluate Financial Performance 407
Government Financial Performance Concepts 408
Financial Position and Financial Condition 409
Economic Condition 410
Internal Financial Trend Monitoring 410
Environmental Factors 412
Organizational Factors 415
Financial Factors 415
Analyzing Government-wide Financial Statements 418
Financial Position Ratios 418
Financial Performance Ratios 418
Financial Capability Ratios 418
Use of Benchmarks to Aid Interpretation 420
Sources of Governmental Financial Data 422
Electronic Municipal Market Access 423
Credit Analyst Models 424
Key Terms 425
Selected References 425
Questions 426
Cases 426
Exercises and Problems 431

Chapter 11
Auditing of Governmental and Not-for-Profit Organizations 441
Financial Audits by Independent CPAs 442
Generally Accepted Auditing Standards 442
Format of the Audit Report 443
Types of Opinions 445
The Audit Process 446
Materiality for Government Audits 449
Required Supplementary and Other Information 449
Government Auditing Standards 450
Types of Audits and Engagements 450
GAGAS Financial Audits 452
Ethics and Independence 454
Appendix: Budget and Cost Issues in Grant Accounting 502
Key Terms 502
Selected References 507
Questions 507
Cases 508
Exercises and Problems 509

PART THREE
Accounting and Financial Reporting for Not-for-Profit Organizations and the Federal Government 521

Chapter 13
Accounting for Not-for-Profit Organizations 523
Defining the Not-for-Profit Sector 524
Determining Whether an NFP Organization Is Governmental 525
GAAP for Nongovernmental NFP Organizations 526
Financial Reporting 526
Statement of Financial Position 527
Statement of Activities 529
Statement of Cash Flows 530
Statement of Functional Expenses 530
Notes to the Financial Statements 533
Accounting for NFP Organizations 533
Revenues and Gains 533
Accounting for Expenses 539
Accounting for Assets 541
Consolidations and Combinations 543
Consolidations 543
Combinations 544
Illustrative Transactions—Voluntary Health and Welfare Organizations 544
End-of-the-Year Adjusting Journal Entries 549
End-of-the-Year Reclassification Journal Entries 550
End-of-the-Year Closing Journal Entries 551
Appendix: Optional Fund Accounting 557
Key Terms 558
Selected References 558
Questions 559
Cases 559
Exercises and Problems 563
<table>
<thead>
<tr>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Generally Accepted Accounting Principles for the Federal Government</td>
</tr>
<tr>
<td>Hierarchy of Accounting Principles and Standards</td>
</tr>
<tr>
<td>Conceptual Framework</td>
</tr>
<tr>
<td>Objectives</td>
</tr>
<tr>
<td>Reporting Entity</td>
</tr>
<tr>
<td>Management’s Discussion and Analysis (MD&amp;A)</td>
</tr>
<tr>
<td>Intended Audience</td>
</tr>
<tr>
<td>Elements and Recognition Criteria</td>
</tr>
<tr>
<td>Communicating Information</td>
</tr>
<tr>
<td>Measurement of Elements after Initial Recording</td>
</tr>
<tr>
<td>Funds Used in Federal Accounting</td>
</tr>
<tr>
<td>General Fund</td>
</tr>
<tr>
<td>Special Funds</td>
</tr>
<tr>
<td>Revolving Funds</td>
</tr>
<tr>
<td>Trust Funds</td>
</tr>
<tr>
<td>Deposit Funds</td>
</tr>
<tr>
<td>Required Financial Reporting—U.S. Government-wide</td>
</tr>
<tr>
<td>Required Financial Reporting—Government Agencies</td>
</tr>
<tr>
<td>Agency Head Message</td>
</tr>
<tr>
<td>Management’s Discussion and Analysis</td>
</tr>
<tr>
<td>Annual Performance Reports (APR)</td>
</tr>
<tr>
<td>Annual Financial Statements (AFR)</td>
</tr>
<tr>
<td>Other Accompanying Information</td>
</tr>
<tr>
<td>Dual-track Accounting System</td>
</tr>
<tr>
<td>Illustrative Transactions and Entries</td>
</tr>
<tr>
<td>Adjusting Entries</td>
</tr>
<tr>
<td>Illustrative Financial Statements</td>
</tr>
<tr>
<td>Summary of Accounting and Reporting for Federal Government Agencies</td>
</tr>
<tr>
<td>Key Terms</td>
</tr>
<tr>
<td>Selected References</td>
</tr>
<tr>
<td>Questions</td>
</tr>
<tr>
<td>Cases</td>
</tr>
<tr>
<td>Exercises and Problems</td>
</tr>
<tr>
<td>Glossary</td>
</tr>
<tr>
<td>Governmental and Not-for-Profit Organizations</td>
</tr>
<tr>
<td>Index</td>
</tr>
</tbody>
</table>