CHAPTER 2
STATE AND LOCAL GOVERNMENT ACCOUNTING AND FINANCIAL REPORTING MODEL: THE FOUNDATION

ANSWERS TO QUESTIONS

Question 2-1

Governments operate in a different environment than businesses. Governments must comply with the many ***finance-related legal and contractual requirements***, ***regulations, restrictions, and agreements*** that affect their financial management and accounting. Such compliance must be demonstrable and be reported regularly. Governments should also prepare financial statements in conformity with generally accepted accounting principles (GAAP), which provide uniform minimum national standards of and guidelines for annual financial reporting to groups and persons outside the government. Therefore, one fundamental feature of a government's accounting system is that it must maintain and provide information that accomplishes multiple purposes.

Whereas business accounting systems must provide data both for GAAP reporting and for income tax reporting, governmental accounting systems must provide data both for external reporting in conformity with GAAP and for controlling and reporting on finance-related legal compliance matters. This necessitates having different accounting systems for businesses and governments.

Question 2-2

The measurement focus for the three fund categories are:

1. ***Proprietary Funds***—economic resources (revenues and expenses) measurement focus, which is the measurement focus used by business enterprises.

2. ***Governmental Funds***—the current financial resources measurement focus.

3. ***Fiduciary Funds***—the same measurement focus as proprietary funds—the economic resources measurement focus.

An **economic resources** measurement focus results in accounting for *all* assets—both *current* and *noncurrent*—and *all* liabilities—both *current* and *long-term*. A **current financial resources** measurement focus results in accounting for financial assets and related liabilities. Noncurrent assets and long-term liabilities are not reported under a current financial resources measurement focus.

The GASB's approach to each measurement focus also includes two financial statement elements not found in accounting for other types of entities—deferred outflows of resources and deferred inflows of resources. These elements arise from changes in net assets that the GASB has determined should not be reflected as changes in fund balance (governmental funds) or net position (proprietary funds and fiduciary funds) until a future period.

Question 2-3

For governmental funds:

1. Revenues must be (1) "*available*"—collectible within the period or soon enough thereafter to be used to pay for the expenditure liabilities incurred during the period, as well as levied or earned—*and* (2) *measurable* to be recognized.

2. Expenditures are financial assets expended during a period for current operations, capital outlay, and debt service including (a) long-term debt principal retirement and (b) interest on both short-term and long-term indebtedness.

For proprietary funds:

1. Revenues are recognized when earned and measurable. There is no "availability" criterion for revenues recognized in proprietary funds.

2. Expenses are costs consumed or expired during a period.

Difficulty: 1
Learning Objective: 2
AACSB: Reflective thinking

Question 2-4

General capital assets are not considered appropriable resources and unmatured general long-term liabilities are not current liabilities. Hence, these assets and liabilities would not appropriately be accounted for within a municipality's governmental (expendable) funds, which are net current financial resource entities. Further, general capital assets are considered to belong to the government as a whole, not to a particular department or enterprise; and unmatured general long-term liabilities are likewise considered obligations of the government, not of a specific fund. Thus, neither fits into the existing fund structure of state and local governmental accounting, and both are accounted for through the General Capital Assets and General Long-Term Liabilities nonfund accounts. They are reported only in the government-wide financial statements.

Question 2-5

Capital assets and long-term liabilities are accounted for in:

General Capital Assets and General Long-Term Liabilities accounts
Enterprise Funds
Internal Service Funds
Trust Funds (some)

Question 2-5 (continued)
General capital assets and general long-term liabilities are accounted for in the General Capital Assets and General Long-Term Liabilities accounts. They are related to general government (governmental) activities.

Question 2-6

A Special Revenue Fund should be used to account for and report the proceeds of specific *revenue sources* that are restricted or committed to expenditure for specified general government purposes other than debt service or capital projects.

A Capital Projects Fund should be used to account for and report financial resources that are restricted, committed, or assigned to expenditure for general government capital outlays, including the acquisition or construction of capital facilities and other capital assets.

A Debt Service Fund should be used to account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest on general long-term liabilities.

Question 2-7

Proprietary funds include Enterprise Funds and Internal Service Funds. Proprietary fund financial statements include a balance sheet (statement of net position), statement of revenues, expenses, and changes in fund net position, and statement of cash flows.

Question 2-8

Governmental funds include the General Fund, Special Revenue Funds, Capital Projects Funds, Debt Service Funds, and Permanent Funds. Governmental fund financial statements include a balance sheet, statement of revenues, expenditures, and changes in fund balance (GAAP basis), and statement of revenues, expenditures, and changes in fund balance - budget and actual (on the budgetary basis of accounting).

Question 2-9

Fiduciary funds include Private-Purpose Trust Funds, Investment Trust Funds, Pension Trust Funds, and Agency Funds. Trust fund financial statements include a statement of net position and a statement of changes in fiduciary net position. Agency Fund financial statements include a statement of net position and a statement of changes in agency fund assets and liabilities. (The latter is required in a comprehensive annual financial report but not in the basic financial statements).

Question 2-10

One only: General Fund and General Capital Assets and General Long-Term Liabilities accounts

One, none, or many—all other fund types:

Special Revenue Funds	Internal Service Funds	Private-Purpose Trust Funds
Capital Projects Funds	Enterprise Funds	Investment Trust Funds
Debt Service Funds		Pension Trust Funds
Permanent Funds		Agency Funds

Question 2-11

Interfund loans are amounts provided by one fund to another ***with*** a ***requirement*** **for and expectation of *repayment***. Interfund loans are the only type of interfund transaction that initially affects only balance sheet accounts. Because interfund loans are expected to be repaid, a loan is reported as a receivable (asset) in the lending fund and as a payable (liability) in the debtor fund. Neither fund balance nor net position of any fund changes because of an interfund loan—whether it is a short-term loan or a long-term loan.

Interfund transfers are flows of assets (such as cash or goods) from one fund to another ***without equivalent flows of assets or services in return*** *and* ***without*** a ***requirement for repayment***.

- In ***governmental*** funds, transfers should be reported as ***other [nonexpenditure] financing uses*** in the funds making transfers and as ***other [nonrevenue] financing sources*** in the funds receiving transfers.
- In ***proprietary*** funds, transfers should be reported as the last item before the subtotal for changes in net position.

Question 2-12

The Basic Financial Statements, which must be accompanied by Management's Discussion and Analysis and certain other required supplementary information, include the government-wide financial statements (Statement of Net Position and Statement of Activities), the three sets of fund financial statements (governmental funds financial statements, proprietary funds financial statements, and fiduciary funds financial statements), and the related notes. The Comprehensive Annual Financial Report (CAFR) of a governmental unit includes the basic financial statements and is much more extensive. A CAFR contains:

1. Introductory materials e.g., letter(s) of transmittal,
2. Management's Discussion and Analysis,
3. Basic Financial Statements and notes as well other required supplementary information,

Question 2-12 (continued)

4. Combining financial statements (for nonmajor governmental funds, nonmajor Enterprise Funds, Internal Service Funds, Trust Funds, and Agency Funds—if there are two or more funds in these categories. These are a minimum. Other combining statements may be presented.),
5. Individual fund financial statements and schedules (where appropriate),
6. Narrative explanations (notes for combining or individual fund financial statements), and
7. Statistical section.

Items 2 through 6, including the auditor's report, are called the financial section of a CAFR.

Question 2-13

Government-wide financial statements are prepared using the same measurement focus and basis of accounting that is used for proprietary funds—the ***economic resources*** measurement focus and the ***accrual*** basis of accounting.

Question 2-14

The accounting equation for a governmental fund is:

(Financial Assets + Deferred Outflows) – (Related Liabilities + Deferred Inflows) = Fund Balance

Question 2-15

The accounting equation for a proprietary fund is:

Assets + Deferred Outflows − Liabilities − Deferred Inflows = Net Position

Question 2-16

Deferred outflows and deferred inflows result from delaying operating statement recognition of certain changes in the net amount of assets less liabilities. The GASB requires these changes to be classified as deferred outflows instead of assets (or as deferred inflows instead of liabilities) when the GASB views the change as related to future periods. (Some recent deferred outflows and deferred inflows—e.g., proprietary fund and government-wide deferred outflows and deferred inflow related to pensions and other postemployment benefits—appear to result more from smoothing of the expense measurement than from being related to future periods.)

Question 2-16 (continued)

Deferred outflows are reported similarly to assets, and changes in deferred outflows affect the operating statement in essentially the same way as changes in assets. Likewise, deferred inflows are reported similarly to liabilities, and changes in deferred inflows affect the operating statement in essentially the same manner as changes in liabilities.

Question 2-17

The primary characteristic that distinguishes Enterprise Funds from Internal Service Funds is who the “customers” are. Enterprise Funds serve primarily individuals and organizations separate from the government. Internal Service Funds serve predominantly other departments and agencies of the government itself.

The primary distinction of a Special Revenue Fund compared to the General Fund is that a Special Revenue Fund’s resources are to be used for a specified purpose(s), whereas most General Fund resources are available for any legitimate need of the government. A Special Revenue Fund is required to have a revenue source that is either restricted or committed to the specified purposes of the fund as opposed to only resources provided to that fund at the discretion of the government. The other governmental funds are not required to have such a revenue source to serve as the foundation of the fund.

Question 2-18

The General Fund is always a major fund. In addition, any other governmental fund or Enterprise Fund that meets both of the following "size" criteria must be reported as a major fund. The quantitative major fund criteria are:

1. Total assets, liabilities, revenues, or expenditures/expenses (excluding extraordinary items) of that individual governmental fund or Enterprise Fund are at least 10% of the corresponding total (assets, liabilities, revenues, or expenditures/expenses) for all funds of that category or type (i.e., total governmental funds or total Enterprise Funds).

2. The same element that met the 10% criterion in (a) is at least 5% of the corresponding element total for all governmental funds and Enterprise Funds combined.

A governmental fund or Enterprise Fund that does not meet the size criteria may still be treated as a major fund if the government deems it of sufficient importance to statement users. Thus, a government must identify as a major fund each governmental fund or Enterprise Fund for which statement users are likely to need individual fund information.

SOLUTIONS TO EXERCISES

Exercise 2-1

1. a
2. b
3. d
4. a
5. b
6. d
7. c
8. d
9. a
10. d

Exercise 2-2

1. b
2. c
3. a
4. d
5. b
6. c
7. c
8. c
9. a
10. c

Exercise 2-3

1. Special Revenue Fund
2. Capital Projects Fund
3. Enterprise Fund
4. General Fund
5. General Capital Assets and General Long-Term Liabilities nonfund accounts
6. General Capital Assets and General Long-Term Liabilities nonfund accounts
7. General Capital Assets and General Long-Term Liabilities nonfund accounts*
8. Debt Service Fund
9. Enterprise Fund
10. Internal Service Fund

*General long-term liabilities do not become governmental fund liabilities until the period in which they mature.

Exercise 2-4

a. Special Revenue
b. Debt Service
c. Capital Projects
d. Special Revenue
e. Internal Service
f. Enterprise, if criteria met; otherwise Special Revenue if the revenues are restricted or committed, or General Fund if the revenues are not restricted or committed
g. Agency
h. General
i. Enterprise
j. Capital Projects
k. Debt Service
l. Permanent
m. Capital Projects
n. Pension Trust

Exercise 2-5

a, b, c, and d

Exercise 2-6

Name of Government
Governmental Fund
Statement of Revenues, Expenditures, and Changes in Fund Balances
Time Period Report Covers

Revenues (by source)	c
Expenditures (by function)	d, e, f, g, h
Excess (Deficiency) of Revenues Over (Under) Expenditures	
Other Financing Sources (Uses)	a, (b)
Special and Extraordinary Items*	j
Net Change in Fund Balance	
Fund Balance (Total), Beginning	
Fund Balance (Total), Ending	

*The amounts reported for special items and extraordinary items would be proceeds received or expenditures incurred for those items, not gains and losses.
Note: Depreciation expense (i) is not recorded in this statement.

Exercise 2-7

Name of Government
Proprietary Fund
Statement of Revenues, Expenses, and Changes in Net Position
Time Period Report Covers

Operating revenues (by source)	c
Total operating revenues	
Operating expenses (detailed)	d, i
Total operating expenses	
Operating income	
Nonoperating revenues and expenses (detailed)	h, k
Income before capital contributions, special and extraordinary items, and transfers	
Capital contributions	
Special and extraordinary items (detailed)	e, j
Transfers	b
Increase (decrease) in net position	
Net position—beginning of period	
Net position—end of period	

Note: Proceeds from issuing bonds (a), Expenditures for purchases of equipment (f), and Expenditures for principal retirement of long-term liabilities (g) are not reported in this statement.

Exercise 2-8

Name of Government
Governmental Fund
Balance Sheet
Fiscal Year End

Assets	**a, d, g**
Liabilities, and fund balance	
Liabilities	j
Fund balance	c, i
Total liabilities and fund balance	

Note: Unrestricted net position (b), Land (e), Bonds payable (f), Current portion of bonds payable (h), and Buildings and equipment (k) are not reported in this statement.

Exercise 2-9

Name of Government
Proprietary Fund
Statement of Net Position
Fiscal Year End

Assets	
Current Assets:	a, d, g
Noncurrent Assets:	
Capital Assets	e, k
Total Assets	
Liabilities	
Current liabilities	h, j
Noncurrent liabilities	f
Total liabilities	
Net Position	**b**
Total net position	

Note: Nonspendable fund balance (c) and Unassigned fund balance (i) are not reported in this statement.

Exercise 2-10

(1) Proprietary fund

Analysis of Transactions for Business-Type Activities

	Proprietary Funds								
	CA	+	NCA	–	CL	–	LTL	=	NP
a.	($5,100)				$200				($5,300)
b.	3,000								3,000
c1.	2,000				2,000				
c2.					150				(150)
d.	(2,200)				(2,150)				(50)
e.	200								$200
f.	1,000						$1,000		
g.	(100)								(100)
h.	(800)						(800)		
i.	(900)		$900						
j.			(280)						(280)
k.	35		(60)						(25)

*Calculations for:

c2. Interest accrual at year end, $2,000 x .10 x 9/12 = $150

d. Liability reduction equals principal of $2000 plus accrued interest payable of $150.

k. Capital asset carrying value at disposal equals $60 (cost of $900 less accumulated depreciation after three years of $840). Proprietary fund loss on sale of the capital asset is $35 (proceeds) less $60 (carrying value) or $25.

Exercise 2-10 (continued)

(2) Governmental fund and nonfund accounts

Analysis of Transactions for General Government Activities

	Governmental Funds					**General Capital Assets and General Long-Term Liabilities Nonfund Accounts**				
	FA	–	**RL**	=	**FB**	**GCA**	–	**GLTL**	=	**NP**
a.	($5,100)		$200		($5,300)					
b.	3,000				3,000					
c1	2,000		2,000							
c2.			150		(150)					
d.	(2,200)		(2,150)		(50)					
e.	200				200					
f.	1,000				1,000			$1,000		($1,000)
g.	(100)				(100)					
h.	(800)				(800)			(800)		800
i.	(900)				(900)	$900				900
j.						(280)				(280)
k.	35				35	(60)				(60)

Legend

Proprietary Funds		Governmental Fund; General Capital Assets and General Long-Term Liabilities Nonfund Accounts	
CA	Current Assets	**FA**	Financial Assets
CL	Current Liabilities	**RL**	Related Liabilities
LTL	Long-Term Liabilities	**FB**	Fund Balance
NP	Net Position	**GCA**	General Capital Assets
NCA	Noncurrent Assets (including capital assets)	**GLTL**	General Long-Term Liabilities
		NP	Net Position

SOLUTIONS TO PROBLEMS

Problem 2-1 (a)

Analysis of Transactions for General Government Activities

	Fund	Governmental Funds FA	–	RL	=	FB	General Capital Assets and General Long-Term Liabilities Nonfund Accounts GCA	–	GLTL	=	NP
E.	*GF*	*8,000*				*8,000*					
1.	GF			$75,000		($75,000)					
2.	CPF	$9,000,000				9,000,000			$9,000,000		($9,000,000)
3.	CPF	(5,000,000)				(5,000,000)	$5,000,000				5,000,000
4.	GF			60,000		(60,000)	60,000				60,000
4*	GF			1,200**		(1,200)					
5.	GF	(8,000,000)				(8,000,000)					
6.									3,000,000		(3,000,000)
7.	DSF	(11,000,000)				(11,000,000)			(10,000,000)		10,000,000
8.	GF	1,500				1,500	(1,000)				(1,000)

*Year-end entry.
**Accrue interest on short-term debt ($60,000 × .06 × 4/12).

Legend

FA	Financial Assets	**GF**	General Fund
RL	Related Liabilities	**CPF**	Capital Projects Fund
FB	Fund Balance	**DSF**	Debt Service Fund
GCA	General Capital Assets	**GLTL**	General Long-Term Liabilities
NP	Net Position		

Analysis of Transactions for Business-Type Activities

Airport Enterprise Fund

	CA	+	NCA	–	CL	–	LTL	=	NP
5.	$8,000,000								$8,000,000

Problem 2-1 (b)

1. Expenditures of $75,000 reported in General Fund.
2. Other Financing Sources—Bond Issuance of $9,000,000 reported in Capital Projects Fund.
3. Expenditures of $5,000,000 reported in Capital Projects Fund.
4. Expenditures of $60,000 reported in General Fund.
   At year end, expenditures of $1,200 interest reported in General Fund.
5. Other Financing Uses (Transfer to Other Fund) of $8,000,000 reported in General Fund.
   Transfers from Other Fund of $8,000,000 reported in Airport Enterprise Fund.
6. No operating statements are prepared for GCA-GLTL accounts.
7. Expenditures of $11,000,000 reported in Debt Service Fund.
8. Other Financing Sources of $1,500 reported in General Fund.

Enterprise Fund Legend

CA	Current Assets
CL	Current Liabilities
LTL	Long-Term Liabilities
NP	Net Position
NCA	Noncurrent Assets (including capital assets)

Problem 2-2 (a)

Governmental Funds

	Fund	Financial Assets	–	Related Liabilities	=	Fund Balance
1.	GF	($500,000)				($500,000)
2.	SRF	(38,000)				(38,000)
4a.	GF	50,000		50,000		
4b.*	GF			2,500		(2,500)
5.	CPF	15,000,000				15,000,000
6.	CPF	(185,000)				(185,000)
7.	CPF	(14,715,000)				(14,715,000)
8a.**	CPF	(100,000)				(100,000)
8b.	DSF	100,000				100,000
9a.	GF	(1,500,000)				(1,500,000)
9b.	DSF	1,500,000				1,500,000
10.***	DSF	(1,200,000)				(1,200,000)
11.****	GF	(53,750)		(52,500)		(1,250)
13.	GF	(100,000)		10,000		(110,000)
14.	GF	4,000				4,000
15.	DSF	(110,000)				(110,000)

* Accrue interest on short-term debt ($50,000 × .10 × 6/12).

** $15,000,000 − $185,000 − $14,715,000

*** $15,000,000 × .08 × 1

**** Balance of interest owed ($50,000 × .10 × 3/12 = $1,250).

General Capital Assets (GCA) and General Long-Term Liabilities (GLTL) nonfund accounts

	GCA	−	GLTL	=	Net Position
2.	$38,000				$38,000
5.			15,000,000		(15,000,000)
6.	185,000				185,000
7.	14,715,000				14,715,000
14.*	(9,000)				(9,000)
15.			(100,000)		100,000

* $15,000 less accumulated depreciation of ($15,000 − $7,000) × 3/4

Proprietary Funds

	Fund	Current Assets (CA)	+	Non-CA	−	Current Liabilities	−	Long-Term Liabilities	=	Net Position
3a.	EF	$5,000,000						$5,000,000		
3b.*	EF					$75,000				($75,000)
12.	EF	1,000,000								1,000,000
13.	EF	110,000								110,000

* Accrue interest at year end ($5,000,000 × .06 × 3/12).

Problem 2-2 (b)

REPORTING in the Statement of Revenues, Expenditures, and Changes in Fund Balance of the:

1. GF—Expenditures, $500,000
2. SRF—Expenditures, $38,000
4b. GF—Expenditures, $2,500
5. CPF—Other financing sources—Bonds $15,000,000
6. CPF—Expenditures, $185,000
7. CPF—Expenditures, $14,715,000
8a. CPF—Other financing uses—Transfer to other funds, $100,000
8b. DSF—Other financing sources—Transfer from other funds, $100,000
9a. GF—Other financing uses—Transfer to other funds, $1,500,000
9b. DSF—Other financing sources—Transfer from other funds, $1,500,000
10. DSF—Expenditures, $1,200,000
11. GF—Expenditures, $1,250
13. GF—Expenditures, $110,000
14. GF—Other financing sources of $4,000
15. DSF—Expenditures, $110,000

REPORTING in the Statement of Revenues, Expenses, and Changes in Fund Net Position

3b. Nonoperating expense (Interest expense), $75,000
12. Operating revenues, $1,000,000
13. Operating revenues, $110,000

Problem 2-3 (1)

Governmental Funds

	Fund	Financial Assets	−	Related Liabilities	=	Fund Balance
1.	CPF	$4,000,000				$4,000,000
2.	CPF	(2,200,000)		600,000		(2,800,000)
3a.	GF	(120,000)				(120,000)
3b.	DSF	120,000				120,000
4.	GF	(315,000)				(315,000)

General Capital Assets (GCA) and General Long-Term Liabilities (GLTL) nonfund accounts

	GCA	−	GLTL	=	Net Position
1.			$4,000,000		($4,000,000)
2.	$2,800,000				2,800,000
4.			(300,000)		300,000

Proprietary Funds

	Fund	Current Assets (CA)	+	Non-CA	−	Current Liabilities	−	Long-Term Liabilities	=	Net Position
5a.	EF	$14,000,000						$14,000,000		
5b.*	EF					$210,000				($210,000)

*** Accrue interest at year end ($14,000,000 × .06 × 3/12).**

Problem 2-3 (2)

REPORTING in the Statement of Revenues, Expenditures, and Changes in Fund Balance of the:

1. CPF—Other financing sources—Bonds, $4,000,000
2. CPF—Expenditures, $2,800,000
3a. GF—Other financing uses—Transfer to other funds, $120,000
3b. DSF—Other financing sources—Transfer from other funds, $120,000
4. GF—Expenditures, $315,000

REPORTING in the Statement of Revenues, Expenses, and Changes in Fund Net Position

5b. Nonoperating expense (Interest expense), $210,000

Problem 2-4 (a)

Governmental Funds

	Fund	Financial Assets	−	Related Liabilities	=	Fund Balance
1.*	GF	($3,000,000)		($18,000)		($2,982,000)
2.	CPF	10,000,000				10,000,0000
3. **	DSF	(400,000)				(400,000)
4.	CPF	(5,000,000)		346,500		(5,346,500)
5a.***	GF	(1,400,000)				(1,400,000)
5b.	DSF	1,400,000				1,400,000
5c.****	DSF	(1,400,000)				(1,400,000)
6.	GF	(500,000)				(500,000)
7.	GF	1,500,000				1,500,000
8.	GF	15,000				15,000

*Related Liabilities: $50,000 − $32,000 = $18,000 decrease during year.
**While not an accrual, interest will be paid by DSF at mid-year ($10,000,000 × .08 × .5 = $400,000). Although not indicated in the problem, sufficient funds will be transferred from the General Fund to the Debt Service Fund for the payment.
***Interest Paid ($10,000,000 × .08 × 1/2 = $400,000).
****Principal ($1,000,000) + Interest ($400,000).

General Capital Assets (GCA) and General Long-Term Liabilities (GLTL) nonfund accounts

	GCA	−	GLTL	=	Net Position
2.			$10,000,000		($10,000,000)
4.	$5,346,500				5,346,500
5c.			(1,000,000)		1,000,000
6.			7,000,000		(7,000,000)
7. *	(500,000)				(500,000)
8.	(20,000)				(20,000)

*The problem does not state explicitly that the land sold is a general capital asset. If not, there are two possibilities for the accounting for this land. Most likely, the land is accounted for in an enterprise activity, in which case neither the GF nor the GCA are affected. As an EF transaction, the analysis would be CA (+ $1,500,000), NCA (−$500,000), and NA (+$1,000,000). The $1,000,000 increase in net position would be reported in the EF operating statement as a nonoperating gain unless determined to qualify as a special item. Alternatively, the land could have been held for resale by the General Fund (see the discussion of Nonspendable Fund Balance on page 133 of the textbook). In this event, there would have been a corresponding decrease in Financial Assets and Fund Balance in the GF of $500,000. There would have been no impact on GCA in this case.

Problem 2-4 (b)

REPORTING in the Statement of Revenues, Expenditures, and Changes in Fund Balance of the:

1. GF—Expenditures, $2,982,000
2. CPF—Other financing sources—Bonds, $10,000,000
3. No effect. (There is no accrual. Interest expenditures of $400,000 are reported for interest paid on the semiannual interest payment date.)
4. CPF—Expenditures, $5,346,500

5a. GF—Other financing uses—Transfer to other funds, $1,400,000
5b. DSF—Other financing sources—Transfer from other funds, $1,400,000
5c. DSF—Expenditures, $1,400,000

6. GF—Expenditures, $500,000
7. GF—Other financing sources of $1,500,000 unless it qualifies as a special item
8. GF—Other financing sources of $15,000

Problem 2-5 (a)

Although the statement presented could be modified to present the sources and uses of financial resources of a governmental (expendable) fund such as the General Fund, the operation of this bus line service is a long-term "business-type" undertaking. All assets, liabilities, and equity associated with the bus line should be accounted for through an Enterprise Fund. All expenses (not expenditures)–including depreciation, inventories consumed, and interest–should be reported in order for the operating results of such an activity to be assessed validly.

While the General Fund-based operating statement shown reports a "net profit," an accrual basis statement would reflect different information once depreciation expense, inventory consumption, and interest expense are included.

Problem 2-5 (b)

Mobiline County Enterprise Fund Bus Line
Statement of Revenues, Expenses, and Changes in Fund Net Position
For the Nine-Month Period Ending October 31, 20X3

Operating Revenues:			
Passenger fares—routine route service		$77,000	
Special charter fees (1)		4,000	
Total Operating Revenues			$81,000
Operating Expenses:			
Salaries (superintendent, drivers, mechanics)		52,000	
Depreciation -			
Buses (2)	$21,000		
Building (3)	6,000		
Shop equipment (4)	1,125	28,125	
Fuel and lubrication		12,000	
Tires and parts (5)		13,000	
Contracted repairs and maintenance		8,000	
Miscellaneous		1,000	
Total Operating Expenses			114,125
Operating Loss			(33,125)
Nonoperating Revenues and Expenses:			
Interest expense (6)			13,500
Decrease in Net Position			(46,625)
Net Position, February 1, 20X3			–
Net Position, October 31, 20X3			$(46,625)

Computations:
(1) $3,000 collected + $1,000 accrued = $4,000
(2) 3/4($140,000/5) = $21,000
(3) 3/4($80,000/10) = $6,000
(4) 3/4($15,000/10) = $1,125
(5) $15,000 acquired 2/1/X3 + $1,000 purchased − $3,000 on hand = $13,000
(6) .06(10 × $30,000) 3/4 = $13,500

Problem 2-6 (a)

	Cash Basis		Modified Accrual Basis		Accrual Basis	
	Dr.	**Cr.**	**Dr.**	**Cr.**	**Dr.**	**Cr.**
1-1 Accounts Receivable			4,000		4,000	
Revenues				4,000		4,000
1-3 Expenditures			500			
Inventory of Supplies					500	
Accounts Payable				500		500
1-5 Expenditures			30,000			
Truck					30,000	
Accounts Payable				30,000		30,000
1-11Cash	2,000		2,000		2,000	
Accounts Receivable				2,000		2,000
Revenues		2,000				
1-15 Expenditures			3,000			
Expenses					3,000	
Wages Payable				3,000		3,000
1-17 Expenditures	500					
Accounts Payable			500		500	
Cash		500		500		500
1-21 Expenditures	3,000					
Wages Payable			3,000		3,000	
Cash		3,000		3,000		3,000
2-3 Expenditures	30,000					
Accounts Payable			30,000		30,000	
Cash		30,000		30,000		30,000
2-5 Expenses					200	
Inventory of Supplies						200
2-6 Depreciation Expense					500	
Accumulated Depreciation						500

Problem 2-6 (b)

The modified accrual and accrual bases are similar in that accruable revenue is recognized prior to cash receipt. They are also similar in that liabilities are recognized when incurred. However, the accrual basis measures expenses (costs expired) while the modified accrual basis measures expenditures (net financial assets expended for current operations, capital outlay, long-term debt principal retirement, and interest).

SOLUTION TO CASES

Case 2-1

1. Special Revenue Fund
2. Internal Service Fund
3. Debt Service Fund
4. Enterprise Fund
5. Capital Projects Fund
6. Special Revenue Fund
7. Capital Projects Fund
8. Internal Service Fund
9. Agency Fund
10. Internal Service Fund
11. Enterprise Fund
12. Pension Trust Fund
13. Special Revenue Fund

Students' discussion and questions may demonstrate that they have made good progress on mastering the fund structure even when an answer is incorrect. For instance, a student who notes that item 10 does not explicitly state the charges are intended to reimburse the costs of services provided might give a response other than an Internal Service Fund. Raising this point reflects that the student has learned the Internal Service Fund definition. However, the fact that it is named a revolving fund suggests the "capital maintenance" notion, which is a primary consequence of cost-reimbursement based charges.

Case 2-2 (a)

Governmental Funds

	Fund	Financial Assets	-	Related Liabilities	-	Deferred Inflows of Resources	=	Fund Balance
1.	GF	($67,000,000)		$1,240,000				($68,240,000)
2.*	GF	133,110,000				2,610,000		130,500,000
3.	CPF	121,750,000						121,750,000
4.	CPF	(68,818,000)		12,400,000				(81,218,000)
5.	GF	(17,600,000)						(17,600,000)
6a.**	SRF	(690,000)						(690,000)
6b.***	SRF	690,000						690,000
7a.	GF	(6,077,000)						(6,077,000)
7b.	DSF	6,077,000						6,077,000
8.	DSF	(7,400,000)						(7,400,000)

* Financial Assets: Taxes Receivable ($135,000,000) less Allowance for Uncollectible Taxes ($1,890,000)
Revenues: Financial Assets ($133,110,000) less Deferred Inflows ($2,610,000)
** To record expenditures by school district for deaf and hearing-impaired program.
*** To record grant proceeds from federal government.

General Capital Assets (GCA) and General Long-Term Liabilities (GLTL) nonfund accounts

	GCA	-	GLTL	=	Net Position
3.			$121,750,000		($121,750,000)
4.	$81,218,000				81,218,000
8.			(1,400,000)		1,400,000

Case 2-2 (b)

REPORTING in the Statement of Revenues, Expenditures, and Changes in Fund Balance of the:
1. GF—Expenditures, $68,240,000
2. GF—Revenues, $130,500,000
3. CPF—Other financing sources—Bonds, $121,750,000
4. GF—Expenditures, $81,218,000
5. GF—Expenditures, $17,600,000
6a. SRF—Expenditures, $690,000
6b. SRF—Revenues, $690,000
7a. GF—Other financing uses—Transfer to DSF, $6,077,000
7b. DSF—Other financing sources—Transfer from GF, $6,077,000
8. DSF—Expenditures, $7,400,000