

**INSTRUCTOR'S MANUAL**

**TO ACCOMPANY**

***ESSENTIALS OF ACCOUNTING FOR GOVERNMENTAL  
AND NOT-FOR-PROFIT ORGANIZATIONS:  
15TH EDITION***

## CHAPTER 1 Introduction to Accounting and Financial Reporting for Governmental and Not-for-Profit Organizations

1-1. THE SOLUTION TO THIS AND THE FIRST EXERCISE OF CHAPTERS 2 THROUGH 9 WILL DIFFER FROM STUDENT TO STUDENT ASSUMING EACH HAS A DIFFERENT ACFR.

1-2.

- 1) **ORGANIZATIONAL PURPOSES:** WHILE THE PURPOSE OF A COMMERCIAL BUSINESS IS TO GENERATE A PROFIT FOR THE BENEFIT OF ITS OWNERS, GOVERNMENTS EXIST FOR THE WELL BEING OF CITIZENS BY PROVIDING PUBLIC SERVICES – WHETHER OR NOT THE SERVICES ARE PROFITABLE UNDERTAKINGS.
- 2) **SOURCES OF REVENUES:** GOVERNMENTS DERIVE MANY OF THEIR RESOURCES FROM TAXES. INDIVIDUALS AND BUSINESSES PAY TAXES TO AVOID PENALTY, NOT VOLUNTARILY BECAUSE THEY PERCEIVE GOVERNMENT SERVICES TO BE OF VALUE AND FAIRLY PRICED. SINCE TAXES DO NOT INVOLVE AN EARNINGS PROCESS, THE TIMING OF THE RECOGNITION OF TAX REVENUE IS NOT ALWAYS CLEAR.
- 3) **POTENTIAL FOR LONGEVITY:** BECAUSE THE U.S. AND STATE CONSTITUTIONS GRANT STATE AND LOCAL GOVERNMENTS THE ABILITY TO TAX, GOVERNMENTS VERY RARELY GO OUT OF BUSINESS. THIS LONG-TERM VIEW OF OPERATIONS CHANGES THE FOCUS OF ACCOUNTING FROM ONE OF NEAR-TERM RECOVERY OF AMOUNTS INVESTED IN ASSETS TO A LONGER-TERM FOCUS ON THE SUSTAINABILITY OF SERVICES AND THE ABILITY TO MEET FUTURE DEMAND.
- 4) **RELATIONSHIP WITH STAKEHOLDERS:** TAXES ARE CREATED THROUGH THE LEGISLATIVE PROCESS BY OFFICIALS ELECTED BY THE CITIZENS. BECAUSE CITIZENS AND BUSINESSES ARE THEN REQUIRED TO PAY THESE TAXES, GOVERNMENTS HAVE AN OBLIGATION TO DEMONSTRATE ACCOUNTABILITY FOR THESE PUBLIC FUNDS.
- 5) **ROLE OF THE BUDGET:** GOVERNMENT BUDGETS ARE EXPRESSIONS OF PUBLIC POLICY AND OFTEN CARRY THE AUTHORITY OF LAW, PREVENTING PUBLIC OFFICIALS FROM SPENDING OUTSIDE THEIR BUDGETARY AUTHORITY. THE INCREASED IMPORTANCE OF BUDGETS IS REFLECTED IN GOVERNMENT FINANCIAL REPORTS BY A REQUIRED REPORT COMPARING BUDGETED AND ACTUAL AMOUNTS.

1-3. THE THREE STANDARDS SETTING BODIES IN QUESTION ARE THE FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD (FASAB), THE GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB), AND THE FINANCIAL ACCOUNTING STANDARDS BOARD (FASB). THE FASAB ESTABLISHES ACCOUNTING AND REPORTING STANDARDS FOR THE FEDERAL GOVERNMENT AND ITS AGENCIES UNLESS OBJECTED TO BY ONE OF THE "PRINCIPALS" (THE DIRECTOR OF THE OFFICE OF MANAGEMENT AND BUDGET, THE COMPTROLLER GENERAL OF THE UNITED STATES (GOVERNMENT ACCOUNTABILITY OFFICE), AND THE SECRETARY OF THE DEPARTMENT OF THE TREASURY). WHEN THE "PRINCIPALS" APPROVE, THE FASAB STANDARDS BECOME GAAP. THE GASB SETS ACCOUNTING AND FINANCIAL REPORTING STANDARDS FOR STATE AND LOCAL GOVERNMENTAL ORGANIZATIONS, INCLUDING THOSE NOT-FOR-PROFIT ORGANIZATIONS THAT ARE DETERMINED TO BE STATE AND LOCAL GOVERNMENTS. THE FASB SETS ACCOUNTING AND FINANCIAL

REPORTING STANDARDS FOR PROFIT SEEKING BUSINESSES AND FOR  
NONGOVERNMENTAL, NOT-FOR-PROFIT ENTITIES.

1-4. THE DEFINITION OF A GOVERNMENT, AS AGREED TO BY THE FASB AND THE GASB IS AS FOLLOWS:

“PUBLIC CORPORATIONS AND BODIES CORPORATE AND POLITIC ARE GOVERNMENTAL ORGANIZATIONS. OTHER ORGANIZATIONS ARE GOVERNMENTAL ORGANIZATIONS IF THEY HAVE ONE OR MORE OF THE FOLLOWING CHARACTERISTICS:

1. POPULAR ELECTION OF OFFICERS OR APPOINTMENT (OR APPROVAL) OF A CONTROLLING MAJORITY OF THE MEMBERS OF THE ORGANIZATION’S GOVERNING BODY BY OFFICIALS OF ONE OR MORE STATE OR LOCAL GOVERNMENTS;
2. THE POTENTIAL FOR UNILATERAL DISSOLUTION BY A GOVERNMENT WITH THE NET ASSETS REVERTING TO A GOVERNMENT, OR
3. THE POWER TO ENACT AND ENFORCE A TAX LEVY.

FURTHERMORE, ORGANIZATIONS ARE PRESUMED TO BE GOVERNMENTAL IF THEY HAVE THE ABILITY TO ISSUE DIRECTLY (RATHER THAN THROUGH A STATE OR MUNICIPAL AUTHORITY) DEBT THAT PAYS INTEREST EXEMPT FROM FEDERAL TAXATION.

1-5. THE SOURCES OF AUTHORITATIVE GAAP FOR STATE AND LOCAL GOVERNMENTS ARE:

- CATEGORY A: GASB STATEMENTS (AND INTERPRETATIONS)
- CATEGORY B: GASB IMPLEMENTATION GUIDES, GASB TECHNICAL BULLETINS AND LITERATURE OF THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS (AICPA) SPECIFICALLY CLEARED BY THE GASB

IF THE ACCOUNTING TREATMENT FOR A GIVEN TRANSACTION IS NOT SPECIFIED BY A STATEMENT IN CATEGORY A, A STATE AND LOCAL GOVERNMENT SHOULD CONSIDER WHETHER IT IS COVERED BY ONE OF THE SOURCES IDENTIFIED IN CATEGORY B. IF THE ACCOUNTING TREATMENT IS NOT SPECIFIED WITHIN ONE OF THESE AUTHORITATIVE SOURCES, THE GOVERNMENT SHOULD CONSIDER WHETHER THE TRANSACTION IS SUFFICIENTLY SIMILAR TO ONES COVERED BY ONE OF THE AUTHORITATIVE SOURCES THAT A SIMILAR ACCOUNTING TREATMENT CAN BE APPLIED. IF NOT, THE GOVERNMENT MAY USE NONAUTHORITATIVE SOURCES FOR GUIDANCE, INCLUDING:

- GASB CONCEPT STATEMENTS,
- FASB, FASAB, OR INTERNATIONAL STANDARDS BOARD PRONOUNCEMENTS,
- AICPA LITERATURE NOT SPECIFICALLY CLEARED BY THE GASB,
- OTHER SOURCES PROVIDED BY PROFESSIONAL ORGANIZATIONS, REGULATORY AGENCIES, TEXTBOOKS, AND PUBLISHED ARTICLES, OR

- PREVALENT PRACTICES THAT EVOLVED AMONG GOVERNMENTS WITHOUT SPECIFIC AUTHORITATIVE ACTION.

1-6.

- A. CONCEPTUALLY, THE MEASUREMENT FOCUS DETERMINES *WHAT* IS MEASURED; THE BASIS OF ACCOUNTING DETERMINES *WHEN* SOMETHING IS MEASURED. THE ECONOMIC RESOURCES MEASUREMENT FOCUS MEASURES ALL ECONOMIC RESOURCES, INCLUDING CAPITAL ASSETS AND LONG-TERM DEBT. THE CURRENT FINANCIAL RESOURCES MEASUREMENT FOCUS MEASURES PRIMARILY FINANCIAL RESOURCES (CASH, ASSETS THAT ARE AVAILABLE TO BE CONVERTED TO CASH (INVESTMENTS AND CURRENT RECEIVABLES) AND ASSETS THAT ARE CONSUMABLE IN LIEU OF CASH (PREPAID ITEMS AND INVENTORIES) AND DOES NOT RECOGNIZE LONG-TERM ASSETS AND LIABILITIES.

THE ACCRUAL BASIS OF ACCOUNTING AS APPLIED TO THE ECONOMIC RESOURCES MEASUREMENT BASIS RECOGNIZES REVENUES WHEN EARNED AND EXPENSES WHEN INCURRED. THE MODIFIED ACCRUAL BASIS FOR CURRENT FINANCIAL RESOURCES OF ACCOUNTING RECOGNIZES REVENUES WHEN MEASURABLE AND AVAILABLE TO FINANCE THE EXPENDITURES OF THE CURRENT PERIOD. EXPENDITURES (NOT EXPENSES) ARE RECOGNIZED IN THE PERIOD IN WHICH THE FUND LIABILITY IS INCURRED.

- B. THE GOVERNMENTAL FUNDS USE THE CURRENT FINANCIAL RESOURCES MEASUREMENT FOCUS AND MODIFIED ACCRUAL BASIS OF ACCOUNTING IN THE FUND-BASIS STATEMENTS. THE PROPRIETARY AND FIDUCIARY FUNDS USE THE ECONOMIC RESOURCES MEASUREMENT FOCUS AND ACCRUAL BASIS OF ACCOUNTING IN THE FUND-BASIS STATEMENTS. THE GOVERNMENT-WIDE STATEMENTS ARE PREPARED USING THE ECONOMIC RESOURCES MEASUREMENT FOCUS AND ACCRUAL BASIS OF ACCOUNTING.

1-7. PRIVATE SECTOR ORGANIZATIONS ARE ORGANIZATIONS THAT ARE NOT OWNED OR CONTROLLED BY GOVERNMENTS AND INCLUDE BUSINESSES AS WELL AS PRIVATE NOT-FOR-PROFIT ORGANIZATIONS. PUBLIC SECTOR ORGANIZATIONS ARE GOVERNMENTS OR ORGANIZATIONS OWNED OR CONTROLLED BY GOVERNMENTS.

1-8. ACCORDING TO THE WEB SITE, “THE MISSION OF THE GASB AND FASB IS TO ESTABLISH AND IMPROVE FINANCIAL ACCOUNTING AND REPORTING STANDARDS TO PROVIDE USEFUL INFORMATION TO INVESTORS AND OTHER USERS OF FINANCIAL REPORTS AND EDUCATE STAKEHOLDERS ON HOW TO MOST EFFECTIVELY UNDERSTAND AND IMPLEMENT THOSE STANDARDS.

1-9. THE APPROPRIATE FUNDS ARE:

- a) CAPITAL PROJECTS FUND: THESE FINANCIAL RESOURCES ARE TO BE USED TO FINANCE CONSTRUCTION OF A CAPITAL ASSET. SINCE THE JAIL IS UNLIKELY

TO CHARGE FOR ITS SERVICES, IT WOULD NOT BE PART OF A PROPRIETARY FUND.

- b) SPECIAL REVENUE FUND: SINCE THE TAX REVENUE IS RESTRICTED BY STATE LAW FOR A PURPOSE OTHER THAN CAPITAL PROJECT OR DEBT SERVICE, THESE AMOUNTS WOULD BE REPORTED IN A SPECIAL REVENUE FUND.
- c) ENTERPRISE FUND: ALTHOUGH THIS REPRESENTS A CAPITAL PROJECT, WATER DEPARTMENTS ARE TYPICALLY REPORTED AS ENTERPRISE FUNDS.
- d) PRIVATE-PURPOSE TRUST FUND: THIS IS A TRUST FUND IN WHICH THE INCOME BENEFITS INDIVIDUALS. IF THE PURPOSE OF THE FUND WAS TO BENEFIT THE GOVERNMENT OR ITS CITIZENRY (BROADLY), THEN IT WOULD BE APPROPRIATE TO REPORT THESE RESOURCES IN A PERMANENT FUND.
- e) SPECIAL REVENUE FUND: ALTHOUGH THE LIBRARY BENEFITS THE CITIZENRY IN GENERAL, THE ABSENCE OF A REQUIREMENT THAT PRINCIPAL BE MAINTAINED PRECLUDES THE RESOURCES BEING REPORTED IN A PERMANENT FUND. SINCE THE RESOURCES ARE RESTRICTED BY THE DONOR, THEY WOULD BE REPORTED IN A SPECIAL REVENUE FUND.
- f) GENERAL FUND: THE RESOURCES ARE NEITHER FIDUCIARY NOR PROPRIETARY. SINCE THE RESOURCES ARE NOT RESTRICTED OR COMMITTED TO A PARTICULAR PURPOSE, THE GENERAL FUND WOULD BE THE APPROPRIATE FUND FOR REPORTING THE PROCEEDS OF THE SALE OF THE EQUIPMENT.
- g) SEVERAL FUNDS WILL BE AFFECTED:
  - GENERAL FUND – CONTRIBUTIONS ON BEHALF OF THE TEACHERS AND PUBLIC SAFETY EMPLOYEES WILL BE PAID BY THE GENERAL FUND WHICH INCLUDES DEPARTMENTS WHERE THESE EMPLOYEES WORK.
  - ENTERPRISE FUND - WATER DEPARTMENTS ARE TYPICALLY REPORTED IN ENTERPRISE FUNDS AND CONTRIBUTIONS ON BEHALF OF WATER DEPARTMENT EMPLOYEES WILL BE PAID BY THIS FUND.
  - PENSION TRUST FUND – THE AMOUNTS CONTRIBUTED BY THE GENERAL AND ENTERPRISE FUNDS WILL BE RECEIVED BY THE PENSION TRUST FUND FOR INVESTMENT.