Introduction to Accounting and Financial Reporting for Governmental and Not-for-Profit Entities
Learning Objectives

After studying Chapter 1, you should be able to:

☒ Identify and explain the characteristics that distinguish governmental and not-for-profit entities from for-profit entities

☒ Identify the authoritative bodies responsible for setting GAAP and financial reporting standards for all governmental and not-for-profit organizations

☒ Contrast and compare the objectives of financial reporting for state and local governments, the federal government, and not-for-profit organizations
Learning Objectives (Cont’d)

≈ Explain the minimum requirements for general purpose external financial reporting of state and local governments and how they relate to comprehensive annual financial reports

≈ Explain the different objectives, measurement focus, and basis of accounting of the government-wide financial statements and fund financial statements of state and local governments
What are Governmental Organizations?

- **General purpose governments**
  - Provide a wide variety of services
  - Examples: Federal government, state governments, cities, towns, townships, villages, counties, boroughs, and parishes

- **Special purpose governments**
  - Usually provide only a single or just a few services
  - Examples: Independent school systems, public colleges and universities, public hospitals, fire protection districts, sewer districts, transportation authorities, and many others
What are Not-for-Profit Organizations?

- Legally separate organizations
- Usually exempt from federal, state, and local taxation
- Religious, community service, private educational and health care, museums, and fraternal and social organizations, among many other kinds of organizations
How Do Governmental and Not-For-Profit Organizations Differ from Business Organizations?

- Resource providers do not expect to receive proportional benefits
- Lack of a profit motive
- Absence of transferable ownership rights
How Do Governmental Entities Differ From Not-For-Profit Organizations?

- Power ultimately rests in the hands of the people
- People delegate power to public officials through the election process
- Empowered by and accountable to a higher level government
- Taxation powers
Criteria for Determining Whether an NPO is Governmental

- Public corporations and bodies corporate and politic
- Other organizations with one or more of the following characteristics:
  - Popular election of officers, or appointment of a controlling majority of the governing body by officials of another government
  - Potential dissolution by a government with net assets reverting to a government
  - Power to enact and enforce a tax levy
Sources of GAAP and Financial Reporting Standards

**FASB**
- Business organizations
- Nongovernmental not-for-profits

**GASB**
- Governmental organizations
- Governmental not-for-profits

**FASAB**
- Federal government and its agencies
Why Must Governmental Financial Reporting Differ from Business Financial Reporting?

- Different financial report users with different needs
- Governmental financial reporting focuses on stewardship and accountability for how public resources are raised and used to provide services
Objectives of Financial Reporting—State and Local Governments (SLG)

Governmental financial reports are used primarily to:

- Compare actual financial results with legally adopted budget
- Assess financial condition and results of operations
- Assist in determining compliance with finance-related laws, rules, and regulations
- Assist in evaluating efficiency and effectiveness
“ACCOUNTABILITY is the cornerstone of all financial reporting in government “ (GASB Concepts Statement No. 1, par. 56)
Q: What do we mean by accountability?

A: Accountability arises from citizens’ “right to know” It imposes a duty on public officials to be accountable to citizens for raising public monies and how they are spent.
Q: How does “interperiod equity” relate to accountability?

A: Interperiod equity is a government’s obligation to disclose whether current-year revenues were sufficient to pay for current-year benefits—or did current citizens defer payments to future taxpayers?
Accountability is also the foundation of federal government financial reporting.

- Federal Accounting Standards Advisory Board (FASAB) standards are targeted at both internal users (management) and external users.
Federal government financial reporting should assist report users in evaluating:

- Budgetary integrity
- Operating performance
- Stewardship
- Adequacy of systems and controls
Objectives of Financial Reporting—Not-for-Profit (NFP) Organizations

NFP financial reporting should provide information useful in:

- Making resource allocation decisions
- Assessing services and ability to provide services
- Assessing management stewardship and performance
- Assessing economic resources, obligations, net resources, and changes in them
Minimum Requirement for General Purpose External Financial Reporting

Management’s discussion and analysis

Government-wide financial statements <-> Fund financial statements

Notes to the financial statements

Required supplementary information (other than MD&A)
Funds have separate self-balancing sets of accounts used to account for resources segregated for specific purposes or restricted as to use by donors or grantors.

Funds are separate accounting and fiscal entities (Chapters 2-9 provide detail).
Fund Accounting

Fund categories:
- Governmental
- Proprietary
- Fiduciary
Governmental Funds

Characteristics:

- Focus on short-term flow of financial resources
- Only account for current assets and current liabilities
- Use *modified accrual* basis of accounting (revenues recognized when measurable and available for spending and expenditures when incurred)
- Closely tied to budgetary accounting
Proprietary and Fiduciary Funds

Characteristics:

- Focus on flow of economic resources
- Accrual basis of accounting (revenues recognized when earned and expenses when incurred)
- Account for both current and noncurrent assets and current and noncurrent liabilities—similar to business accounting
Comprehensive Annual Financial Report (CAFR)

Introductory section

Financial section

Statistical section
CAFR - Introductory Section

- Title page
- Contents page
- Letter of transmittal
- Other (as desired by management)
CAFR - Financial Section

- Auditor’s report
- Basic financial statements
- Required supplementary information (RSI)(other than MD&A)
- Combining and individual fund statements and schedules
Management’s Discussion and Analysis (MD&A)

Brief objective narrative providing management’s analysis of the government’s financial performance
Basic Financial Statements

Government-wide financial statements

- Statement of net assets (Illustration A1-1)
- Statement of activities (Illustration A1-2)
Basic Financial Statements—Government-wide Financial Statements (Cont’d)

Points of interest (Ill. A1-1 and A1-2)

- Information is reported separately for the primary government and discretely presented component units
- Within the primary government, information is reported separately for governmental and business-type activities
Points of interest (Cont’d)

- All financial information in the government-wide financial statements is reported on the accrual basis with an economic resources focus—similar to business financial reporting.
- Assists in assessing operational accountability—how efficiently resources are being used.
Governmental funds

- Statement of revenues, expenditures, and changes in fund balances—governmental funds (Ill. A1-5) with reconciliation (Ill. A1-6)
- These statements report information separately for the General Fund and other major funds (Chapter 2 defines major funds)
Governmental funds—points of interest

- Focus on flow of current (i.e., short-term) financial resources recognized on the modified accrual basis of accounting
- Assist in assessing *fiscal accountability*—whether financial resources were raised and expended in compliance with budgetary and other legal provisions
Governmental funds—points of interest (Cont’d)

- Reporting the same information about governmental activities in two different ways creates a need to reconcile the information reported in the governmental fund financial statements to that in the Governmental Activities Column of the government-wide statements (see Illustrations A1-4 and A1-6)
Proprietary funds

- Statement of net assets—proprietary funds (Ill. A1-7)
- Statement of revenues, expenses, and changes in fund net assets—proprietary funds (Ill. A1-8)
- Statement of cash flows—proprietary funds (Ill. A1-9)
Basic Financial Statements—Fund Financial Statements

Proprietary funds—points of interest

- Reports information for enterprise funds and internal service funds using an economic resources focus and accrual basis of accounting
- Information is reported in separate columns for major enterprise funds. All internal service fund information reported is combined in a single column
Fiduciary funds

- Statement of fiduciary net assets (Ill. A1-10)
- Statement of changes in fiduciary net assets (Ill. A1-11)
Fiduciary funds—points of interest

- Fiduciary activities relate to the government’s responsibility as an agent or trustee to hold and/or manage resources for the benefit of private parties
- Since fiduciary resources cannot be used by the government, they are reported only in the fiduciary fund financial statements—not in the government-wide statements
Tables and charts showing multiple-year trends in financial and socio-economic information (discussed in detail in Chapter 9)
Concluding Comments

- In this course you will become familiar with current GASB, FASB, and FASAB standards relative to governmental and not-for-profit organizations.

- Accounting and reporting for governmental and not-for-profit entities differ from those of for-profit entities because each type of entity has different purposes and reporting objectives.
“...Even when developed to the ultimate stage of perfection, governmental accounting cannot become a guaranty of good government. At best, it can never be more than a valuable tool for promotion of sound financial management...”

Professor R. M. Mikesell, 1951