FINANCIAL MANAGEMENT FOR GEORGIA LOCAL UNITS OF ADMINISTRATION

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INTRODUCTION

The 2015-2016 Governmental Accounting Standards Board (GASB) *Codification of Governmental Accounting and Financial Reporting Standards* (2015-2016 *Codification*) Section 1700 calls for the adoption of an annual budget by every government. The local unit of administration's (LUA's) accounting system should provide the basis for appropriate budgetary control. Unless the accounting system is well organized and maintained, it is difficult to prepare an accurate budget. The accounting system is the basis for evidence of past experience needed for the preparation of the budget. Budget execution is dependent upon the accounting system to provide controls over expenditures and for the monitoring of revenues. LUAs are required to adopt annual budgets.

This chapter includes a discussion of budgets and the budgetary bases of accounting, introduces the budgetary control accounts, illustrates how the budgetary control accounts are integrated formally into the accounting system, and presents in detail the journal entries necessary to report encumbrances.

REVENUE BUDGETS

The revenue budget should include all revenues anticipated within the fund in a given fiscal year, and generally they are segregated by source (e.g., property taxes, Quality Basic Education Act revenues). In addition to revenues, the category "other financing sources" also may be used. Generally, this category describes financial resources that are non-revenue receipts, but are treated as revenue to an individual fund within the LUA. Included in this classification are proceeds from the sale of bonds, sale (or compensation for the loss) of fixed assets, and interfund operating transfers in. The available fund balance at the beginning of the fiscal year which may be spent in the subsequent year's budget is also considered a financial resource for budget purposes.

EXPENDITURE BUDGETS

Generally, expenditure budgets are considerably more detailed than revenue budgets. Governmental expenditures are classified in several ways, using the dimensions illustrated in Appendix C. An important aspect of expenditure budgets is the legal level of budgetary control. This is the level which may not be over expended without the school board's approval. As set forth in Chapter IV - 2, local boards should adopt a policy setting forth the level of budgetary control. A copy of that policy should be available for review as necessary by the Financial Review Unit of the GaDOE and the audit firm responsible for the annual audit of the LUA.

In addition to expenditures, the category "other financing uses" also may be used. This category is reported similarly to "other financing sources" and includes transactions that reduce equity in an individual fund but do not reduce the total equity of the LUA. The primary classification included here is interfund operating transfers out.

BUDGETARY BASIS OF ACCOUNTING

Neither GAAP nor the State Board of Education have any rules about which budgetary basis must be used by LUAs. However, the financial analysis report must be reported on the Modified Accrual Basis, therefore, the GAAP basis for budgetary reporting is recommended for budget to actual comparisons. The most common budgetary bases are these:

1. GAAP Basis. The budget is prepared on the modified accrual basis of accounting for governmental fund types and should be the easiest to understand since this basis is consistent with GAAP basis. This means that the actual financial data (i.e., revenues and expenditures) will be the same on the budgetary comparison operating statements as it is on the GAAP operating statements.

2. GAAP Basis and Encumbrances. Using this basis means that the modified accrual basis of accounting is used; however, actual expenditures on the GAAP basis are adjusted for outstanding encumbrances. Encumbrances are explained later in this chapter. On GAAP basis, encumbrances are not considered expenditures because a fund liability has not yet occurred.

3. Other Bases. Cash basis accounting, modified cash or any modification of the above are acceptable as a budgetary basis. However, the cash and modified cash basis are unacceptable for GAAP accounting as addressed earlier.

Regardless of the budgetary basis used, any "budget and actual" operating statements must be prepared using the budgetary basis. For LUAs, the budgetary basis reported as Required Supplementary Information is using the Modified Accrual Basis. Chapter IV -2 discusses this topic in detail.

BUDGETARY SUBSIDIARY AND CONTROL ACCOUNTS

GAAP suggests that budgets be integrated formally into the subsidiary ledgers and the general ledger control accounts. The PC GENESIS system includes a budget module with the accounts needed to integrate the budget.

Subsidiary Ledger Accounts

Each of the items of estimated revenue and budgeted (i.e., appropriated) expenditures should be accounted for in a separate account so that variances may be identified readily by source as the fiscal year progresses. This accounting is accomplished by the use of subsidiary ledgers: the revenue ledger and the expenditure ledger. These ledgers are illustrated in Chapters I-9 and I-10.

Budgetary Control Accounts. All subsidiary ledgers should be summarized in control accounts in the general ledger. The budgetary general ledger control accounts and numbers are:

- ESTIMATED REVENUES AND OTHER FINANCING SOURCES CONTROL (0301)

- APPROPRIATIONS AND OTHER FINANCING USES CONTROL (0601)

Each of these budgetary general ledger control accounts is supported by a budgetary subsidiary ledger.

The other budgetary account that may be used is the FUND BALANCE - UNASSIGNED account (0799). This account is used to record the difference between the ESTIMATED REVENUE AND OTHER FINANCING SOURCES CONTROL account and the APPROPRIATIONS AND OTHER FINANCING USES CONTROL account. That is, when beginning fund balance is used to balance the budget the difference between the above accounts is reported in the FUND BALANCE - UNASSIGNED account.

The initial step in accounting for any budgeted fund is to record the legally adopted budget. The entry may be recorded in two parts. To record the estimated revenues and other financing sources:

Description	Account No.	DR	CR
Estimated Revenue and Other Financing Sources Control	0301	$1,235,000	
Fund Balance - Unassigned	0799		$1,235,000

In the example, the effect of revenues and other financing sources on the fund balance account is an increase (i.e., credit) of $1,235,000. The second entry is to record the appropriations and other financing uses:

Description	Account No.	DR	CR
Fund Balance - Unassigned	0799	$1,375,000	
Appropriations and Other Financing Uses Control	0601		$1,375,000

The total effect of appropriations and other financing uses on the fund balance account is a decrease (i.e., a debit) of $1,375,000. The total effect on the fund balance account is a decrease of $140,000 (i.e., $1,375,000 minus $1,235,000). This means that if the actual amounts equaled the budgeted amounts at year end, the actual fund balance would decrease $140,000. However, in many states the law requires that revenues and other financing sources must equal the expenditures and other financing uses without the use of the fund balance. The type of budget illustrated here (i.e., a budget which could result in a decrease in fund balance) would be illegal in those states. However, Georgia LUAs may use the fund balance to balance their budgets. Of course, the two budgetary entries illustrated above could be made in a single journal entry. Obviously, if the appropriations and other financing uses exceed the estimated revenues and other financing sources, the budget is considered a "deficit budget" and the deficit would have to be made up from the beginning fund balance.

Anytime an entry is made to a control account, an entry must be made to a subsidiary account. Therefore, when the ESTIMATED REVENUE AND OTHER FINANCING SOURCES CONTROL account is posted for $1,235,000 in the above example, detailed revenue accounts within the revenue subsidiary ledger are posted, such as:

Ad valorem taxes	$ 585,000
Earnings on investments	50,000
QBE formula earnings	650,000
QBE contra account	(50,000)
Total estimated revenue control	$1,235,000

The entries required to close the budgetary accounts at year end are a reversal of the entries formally integrating the budget.

ENCUMBRANCES

Encumbrance accounting is a logical extension of the management control technique of formal budgetary integration. Often, LUAs obligate budget appropriations long before those funds actually are expended. These obligations or commitments are classified as encumbrances.

For example, a purchase order is issued in October for a new truck to be delivered in April at a cost of $25,000. The purchase order represents a commitment to buy a truck at a certain price if it is delivered on schedule and in good condition--provided the purchase order is not later changed or canceled. Since the truck will not be delivered, nor the invoice paid, for several months, it is desirable to reflect this commitment against the capital outlay budget appropriation. In this instance, the purchase order is the source document that results in an encumbrance.

Encumbering Appropriations

By recording an encumbrance in the capital outlay account, the available appropriation balance may be reduced without actually reporting an expenditure. Later, when the truck arrives and the invoice is approved for payment, the encumbrance is liquidated (i.e., canceled), and the actual expenditure is recorded (i.e., since an expenditure and a liability have occurred).

Assume that there is an appropriation of $550 for office supplies in the principal's office. On July 5 a purchase order (i.e., P.O. #17) is issued to the ABC Supply Company in the amount of $50.00 for office supplies to be used in the principal's office. The general journal entry is:

Description	Account No.	DR	CR
Encumbrances Control*	0603	$50	
Fund Balance - Reserved for Encumbrances	0753		$50

* Subsidiary account - 100-0000-2400-610.XX

This entry establishes a debit to the ENCUMBRANCES CONTROL account (0603) and a credit to FUND BALANCE--ASSIGNED FOR ENCUMBRANCES (0753) to set aside a portion of the fund balance to pay this commitment in the future.

Notice that the purchase order has been posted as an encumbrance (i.e., a positive number) and the amount of the encumbrance is subtracted from the available balance. This indicates that there now is only $500 available to spend from the original $550 appropriation.

If a separate journal entry were required each time a purchase order is issued (i.e., an encumbrance is created), the accounting would become quite complex. However, with a computer system, usually all purchase orders are entered into the computer in a single batch and one entry is made in the encumbrance control account for the total of the purchase orders issued. Normally in a computer system, this entry is recorded automatically and posted (i.e., without an additional entry within the computer). However, the individual purchase orders are recorded in the computer's memory and are retrievable.

Liquidating Encumbrances

Assume now that the supplies ordered above are delivered in good order on July 28 and that they are accompanied by an invoice for $53--$50 for supplies and $3 for shipping charges. When the invoice is received, four general ledger accounts are affected: Expenditures/Expenses Control (0602), Accounts Payable (0421), ENCUMBRANCES CONTROL (0603) and FUND BALANCE--ASSIGNED FOR ENCUMBRANCES (0753). This transaction is reported in a single journal entry below, however, the recording of two entries (i.e., canceling the encumbrance and recording the expenditure and liability) is acceptable:

Description	Account No.	DR	CR
Fund Balance - Assigned for Encumbrances	0753	$50	
Encumbrances Control*	0603		$50
Expenditure/Expenses Control*	0602	$53	
Accounts Payable	0421		$53

* Subsidiary account - 100-0000-2400-610.XX

This entry increases Expenditures/Expenses Control and Accounts Payable accounts by the amount of the invoice ($53), and "liquidates" the encumbrance by reversing the original entry made on July 5. The original amount encumbered always is the same amount liquidated regardless of actual amount of the expenditure.

The entry is posted in the expenditure subsidiary ledger to liquidate the encumbrance and record the expenditure.

The effect of this transaction on the supply subsidiary account available balance is $3 (i.e., the expenditure of $53 less the encumbrance of $50) since the encumbrance originally reduced the account balance by $50.

Encumbrances Outstanding at Year-End

LUAs need a system to determine the amount of outstanding encumbrances at any point in time. In a computer accounting system, the amount of outstanding encumbrances is available in a computer-generated report for any single account or in purchase order number.

The 2015-2016 *Codification* Section 1700.127 provides specific guidance regarding the reporting of outstanding encumbrances at year end. Encumbrances outstanding at year end represent the estimated amount of the expenditures ultimately to result if unperformed contracts in process at year end are completed. Encumbrances outstanding at year end do not constitute expenditures or liabilities on a GAAP basis. At year end the outstanding encumbrance budgetary accounts should be closed with a reversal of the original journal entry in the amount of the outstanding encumbrances.

Description	Account No.	DR	CR
Fund Balance - Assigned for Encumbrances	0753	$876,493	
Encumbrances Control	0603		$876,493

Where appropriations lapse at year end, even if encumbered, the LUA may intend either to honor the contracts in progress at year end or to cancel them. If the LUA intends to honor them, encumbrances at year end should be disclosed in the notes to the financial statements. 2015-2016 Codification Section 1800.184 states encumbered amounts for specific purposes for which resources have already been restricted, committed, or assigned should not result in separate display of the encumbered amounts within the classifications. The LUA may choose to increase the next year's appropriation (i.e., the amount of the outstanding encumbrances should be reappropriated), in order to provide authority to complete these transactions without affecting the next year's budget.

Where appropriations do not lapse at year end, or only unencumbered appropriations lapse, encumbrances outstanding at year end should be reported as an assignment of fund balance if designated as such by board policy.

Most often, an amount of fund balance equal to the outstanding encumbrances is assigned.

Description	Account No.	DR	CR
Fund Balance - Unassigned	0799	$876,493	
Fund Balance - Assigned for Encumbrances	0753		$876,493

This entry reclassifies the Fund Balance - Unassigned account by the amount of outstanding encumbrances into the Reserve for Encumbrances account. After recording this entry, the fund balance section of the balance sheet would be reported as follows:

Fund balances:	
Assigned for encumbrances	$876,493
Unassigned	72,090
Total fund balance	$948,583

This means that of the total fund balance of $948,583, $876,493 is encumbered and $72,090 is available for future appropriations. At the beginning of the next fiscal year (e.g., July 1, 20X1), usually the year-end journal entry would be reversed:

Description	Account No.	DR	CR
Fund Balance -			
Assigned For Encumbrances	0753	$876,493	
Fund Balance - Unassigned	0799		$876,493

In addition, an entry to report the amount of outstanding encumbrances (i.e., $876,493) should be made to the encumbrance budgetary accounts in the new fiscal year as follows:

Description	Account No.	DR	CR
Encumbrances Control*	0603	$876,943	
Fund Balance - Assigned for Encumbrances	0753		$876,493

* Various subsidiary accounts

PC GENESIS users do not make entries to the encumbrance control accounts (0603 and 0753). An encumbrance (a purchase order) is entered in the purchase order file in the computer at the fund, function, object, and program level as if the transaction were an expenditure. The software is programmed to recognize and treat the transaction as an encumbrance.

At year-end the PC GENESIS purchase order file is closed to fund balance and assigned for the purpose of encumbrances. The next year, the encumbrances are added to the budget to record the expenditure when the purchase order is liquidated.

SUMMARY

1. A budget is a dollar amount established as an estimate of expenditures and how they will be financed.

2. An appropriation is the authority to spend and the expenditure limit.

3. Revenue budgets include revenues and other financing sources.

4. Expenditure budgets include expenditures and other financing uses.

5. Three of the more common budgetary bases are GAAP basis, GAAP basis including outstanding encumbrances and cash basis.

6. The budgetary general ledger control accounts include ESTIMATED REVENUES AND OTHER FINANCING SOURCES, APPROPRIATIONS AND OTHER FINANCING USES.

7. An encumbrance is an obligation of a budgetary appropriation.

8. The journal entry to record an encumbrance is a debit to ENCUMBRANCES CONTROL (0603) and a credit to FUND BALANCE - ASSIGNED FOR ENCUMBRANCES (0753).

9. The journal entry to liquidate an encumbrance is a debit to FUND BALANCE ASSIGNED FOR ENCUMBRANCES (0753) and a credit to ENCUMBRANCES CONTROL (0603).

10. At year end, all budgetary control accounts should be closed and if the LUA intends on honoring the outstanding encumbrances, an amount of the unassigned fund balance equal to these outstanding purchase orders should be assigned for the purpose of encumbrances.