

FINANCIAL MANAGEMENT FOR GEORGIA LOCAL UNITS OF ADMINISTRATION

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INTRODUCTION

Local Units of Administration (LUA's) report data on two reporting levels, the fund financial reporting level and the government-wide financial reporting level. One of the major challenges of meeting GASB Statement No. 34's Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments (GASBS 34) financial reporting requirements relates to converting data from the fund financial reporting level to the government-wide financial reporting level.

The explanations presented after each illustrative conversion journal entry provide some guidance regarding the source of the required information that is needed to make the journal entry. This chapter explains the reconciliation process and each of the most common reconciling items.

THE ACCOUNTING RECORDS

During the year, most LUA's maintain their accounting records on either a cash or modified accrual basis. Then at year-end, the LUA, makes the necessary journal entries to report the governmental funds on the modified accrual basis, and to report the proprietary and fiduciary fund types on the accrual basis. Once the LUA posts these adjusting journal entries, the LUA's general ledger will reflect the data included in the LUA's fund level financial statements.

Then, in order for LUA's to prepare the government-wide financial statements, it must convert the fund level financial information to a format that will provide information to prepare the government-wide financial statements. This conversion is made through a variety of conversion journal entries. However, LUAs "do not post" all conversion journal entries to their accounting records. Normally, this conversion is prepared either by using pre-designed software or using Excel spreadsheets. LUAs

report activity related to Capital Assets and General Long-Term Debt in the accounting software, but the merging elimination entries are generally completed outside of the accounting system.

After this conversion, the governmental funds (e.g., the general fund) will be reported twice, but differently within the same annual financial report. The LUA will report governmental funds on the modified accrual basis at the fund reporting level and on the accrual basis at the government-wide reporting level. At the fund reporting level, individual governmental funds are reported separately, and at the government-wide fund reporting level, all government funds are aggregated into a single column or row. Obviously, the LUA's accounting records can only report data one way at the same time, therefore the conversion journal entries and the related balances after the conversion, are not posted to the LUA's general ledger.

The software, spreadsheets, and conversion journal entries that support the conversion to the government-wide financial statements must be maintained as they are subject to independent audit.

THE CONVERSION PROCESS

When converting the current reporting year, the revenue and expenditure accounts, as well as the asset and liability accounts, will need to be converted to the government-wide reporting format.

THE CONVERSION JOURNAL ENTRIES

When converting the fund level data to the government-wide level, we may classify the conversion entries into three types as follows:

- Measurement Focus
- Basis of Accounting
- Reclassifications and Eliminations

The conversion journal entries illustrated below are those that the LUA would make annually to convert from the fund financial reporting level to the government-wide financial reporting level. These illustrative journal entries may not be all-inclusive; however, they are the most common conversion entries. Throughout this section, we are assuming a June 30, 20X4 conversion year. Since the LUA will not post these conversion journal entries to their general ledger, account numbers are not included with the illustrative journal entries.

Measurement Focus - The phrase "measurement focus" indicates *what* the LUA is measuring in its financial statements. How a LUA reports capital assets and general long-term debt, including related items, are two types of accounts that need to be converted here.

GASBS 34 requires LUAs to report their capital assets only at the government-wide financial reporting level. The capital assets must be capitalized including recording the accumulated depreciation at the beginning of the reporting year (i.e., July 1) as follows:

	<u>DR</u>	<u>CR</u>
Capital assets (by asset class)	\$XXXX	
Accumulated depreciation		\$XXXX
Net position		XXXX

Explanation - this conversion entry increases the net position (i.e., the equity) by the book value of the capital assets at the beginning of the reporting year. A source for this data will be the note disclosure included in the prior year's audited financial statements which reports "changes in capital assets by asset class." This data is available in the last column of this note. In the current year's notes to the basic financial statements, this data will be reported in the first column of the "changes in capital assets note." Appendix A to this chapter provides a sample "changes in capital assets by asset class" note.

The current year's capital asset purchases need to be reclassified from the current year's expenditures at the fund financial reporting level, to being capitalized as an asset at the government-wide financial reporting level.

	<u>DR</u>	<u>CR</u>
Capital assets (by asset class)	\$XXXX	
Expenditures (by function)		\$XXXX

Explanation - this conversion entry reclassifies the purchases or construction of capital assets from an expenditure at the fund financial reporting level to capital assets at the government-wide financial reporting level. In other words, we are capitalizing the current year's additions to capital assets. Note that each expenditure function will be reduced by the amount of capital assets purchased or capitalized within the function during the current year. The accountant responsible for capital assets should be the source of this information. The amount of assets capitalized normally will agree with the current year's increases column in the capital assets note disclosure that reports "changes in capital assets." The only time when this amount will not agree with the "increases" column of this note is when construction in progress has been reclassified as buildings or when the LUA capitalizes contributed assets. See sample note in Appendix A.

The LUA must report depreciation expense for the current year at the government-wide financial reporting level.

	<u>DR</u>	<u>CR</u>
Expense (by function)	\$XXXX	
Accumulated depreciation (by asset class)		\$XXXX

Explanation - the depreciation expense must be charged to the function that uses the capital asset. Note that the accumulated depreciation must be reported by asset class (e.g., machinery and equipment). Normally the source of this information is the LUA's capital asset system. When a capital asset is initially added to the system, the applicable function should be identified (e.g., a school bus within the transportation function). If a capital asset is used by multiple functions (e.g., a school building), the depreciation should be pro-rated between functions. The amount of the current year depreciation expense will be reported in the LUA's "capital asset changes" note disclosure in the accumulated depreciation section under the "increases" column. See sample note in Appendix A.

Since capital asset donations are not reported at the fund financial reporting level, they need to be valued at fair market value on the date of donation and capitalized on the government-wide financial reporting level with an equal amount reported as program revenue on the statement of activities.

	<u>DR</u>	<u>CR</u>
Capital assets (by asset class)	\$XXXX	
Revenues - contributions		\$XXXX

Explanation - this conversion entry reports contributed assets received during the current year as program revenue. The accountant responsible for capital assets should be the source of this information. Often, this information may be difficult to gather. The amount of contributions also will be included in the current year capital asset note disclosure, which reports changes in capital assets in the "increases" column. See sample note in Appendix A.

When an LUA sells a capital asset at the fund financial reporting level, it reports the sale proceeds as an "other financing source" (if material) (i.e., like revenue). If immaterial, it may be reported as miscellaneous revenue. However, at the government-wide financial reporting level, the book value of capital assets needs to be reported and deducted from the sale proceeds, resulting in an economic gain or loss on the sale.

	<u>DR</u>	<u>CR</u>
Other financing source -		
Sale of capital asset proceeds	\$XXXX	
Accumulated depreciation (by asset class)	XXXX	
Capital assets (by asset class)		\$XXXX
Gain on sale of capital assets		XXXX

Explanation - this conversion entry reduces the sale proceeds by the book value of the capital assets sold. The book value of the capital assets sold should be available from the accountant responsible for capital assets. In addition, the deletion of the capital assets and related accumulated depreciation will be reported in the current year capital asset note disclosure which reports "changes in capital assets" in the "decreases" column. The difference between the cost and the accumulated depreciation should be the total at the bottom of the deletions column on this note. See sample note in Appendix A.

Under GASBS 34, LUAs report their general long-term debt liability (e.g., general obligation bonds) only at the government-wide financial reporting level. The general long-term debt balance at the beginning of the reporting year (i.e., July 1) is recorded as follows:

	<u>DR</u>	<u>CR</u>
Net position	\$XXXX	
General long-term debt payable (by type of debt)		\$XXXX

Explanation - this conversion entry reduces the beginning net position by the amount of general long-term debt outstanding at the beginning of the reporting year. This conversion entry applies to outstanding bonds and capital leases. The source of this information would be the note disclosures included in the prior year's audited financial statements which report "changes in debt by type." Also this data will agree with the amounts reported in the same note in the current year's financial statements, the first column. See Appendix B for sample note.

If the LUA has issued bonds during the year, the face amount of the debt should be reclassified from an "other financing source" at the fund financial reporting level to a liability at the government-wide financial reporting level.

	<u>DR</u>	<u>CR</u>
Other financing source -		
issuance of general obligation bonds	\$XXXX	
General long-term debt payable (bonds)		\$XXXX

Explanation - this conversion entry reclassifies the issuance of debt from an "other financing source" to a general long-term liability on the government-

wide statement of net position. The source of this data would be fund level financial statements, more specifically, the governmental fund “statement of revenues, expenditures, and changes in fund balances.” This amount also will be reported in the changes in “the general long-term debt note,” in the “increases” column. See Appendix B for sample note.

As the LUA retires debt (e.g., bonds) during the year, the retirement should be reclassified from an expenditure at the fund reporting level, to a repayment of the debt principal (i.e., reducing the liability) at the government-wide financial reporting level.

	<u>DR</u>	<u>CR</u>
General long-term debt payable (by type of debt)	\$XXXX	
Debt service expenditure - principal		\$XXXX

Explanation - this conversion entry reclassifies the debt retirement from an expenditure at the fund financial reporting level to a reduction of outstanding debt principal on the government-wide statement of net position. The source of this data would be fund level financial statements, more specifically, the governmental fund “statement of revenues, expenditures, and changes in fund balances.” This amount also will be reported in the “changes in general long-term debt note,” in the “decreases” column. See Appendix B for sample note.

At the fund financial reporting level, prepaid insurance bond issuance costs are reported as debt service expenditures but at the government-wide financial reporting level, they are capitalized and then amortized, if material, over the life of the debt. The capitalization of the prepaid insurance bond issuance costs is recorded as follows:

	<u>DR</u>	<u>CR</u>
Prepaid insurance	\$XXXX	
Debt service expenditures		\$XXXX

Explanation - this conversion entry capitalizes the prepaid insurance associated with bond issuance costs as an asset on the government-wide statement of net position and reduces the expenditures at the fund financial reporting level. The source of this information normally is available from the bond closing statement.

At the end of each subsequent fiscal year end, the prepaid insurance is amortized over the life of the debt. The amortization of the prepaid insurance is recorded as follows:

	<u>DR</u>	<u>CR</u>
Expenses (by function, if appropriate)	\$XXXX	
Prepaid insurance		\$XXXX

Basis of Accounting - The basis of accounting determines when a LUA recognizes revenue or an expenditure/expense. Since LUAs report governmental fund type transactions at the fund financial reporting level on the modified accrual basis and report these same transactions on the accrual basis at government-wide financial reporting level, numerous transactions need to be converted.

If a LUA has a compensated absence liability at the beginning of the fiscal year, this liability must be reported at the government-wide financial reporting level.

	<u>DR</u>	<u>CR</u>
Net position	\$XXXX	
Compensated absences payable		\$XXXX

Explanation - since the compensated absence liability is not reported at the fund financial reporting level, the LUA must report this liability on the government-wide statement of net position. This entry reduces net position by the amount of the liability at the beginning of the reporting period. The source of this information usually is the LUA's human resources personnel. Also this data will agree with the amounts reported in the "changes in general long-term debt" note in the current year's financial statements, the first column. See Appendix B for sample note.

If the LUA has a change in the compensated absence liability (e.g., an increase in liability) at the end of the reporting year from the prior year, this change needs to be reported at the government wide financial reporting level as an adjustment to the expense. If the liability increases, the following entry applies:

	<u>DR</u>	<u>CR</u>
Expenses (by function)	\$XXXX	
Compensated absences payable		\$XXXX

Explanation - since conversion entry #11 above reduces net position by the beginning compensated absences liability, the current years' operations (i.e., expenses) should only reflect the change in the liability. The above illustrative journal entry reports an increase in the liability. A decrease in the liability would reverse the debit and credit. Note that the change must be reported by function. The source of this information is the LUA's human resources personnel. This

amount also is reported in the “changes in long-term debt” note, either in the “increases” or “decreases” column as applicable. See Appendix B for sample note.

If a LUA reports deferred inflows of resources at the fund reporting level, (e.g., for property taxes) because it is considered not available as revenue, normally it would be reclassified as revenue at the government-wide financial reporting level. On the accrual basis, a transaction may be reported as revenue, whether or not it is available. The required entry is to reclassify the deferred inflows of resources balance at the beginning of the reporting year follows:

	<u>DR</u>	<u>CR</u>
Deferred inflows of resources	\$XXXX	
Net position		\$XXXX

Explanation - the conversion entry increases net position by the beginning deferred inflows of resources since this amount was recognized as revenue in prior years on the accrual basis. The source for this entry would be the governmental fund type balance sheet from the prior year’s audited financial statements.

If the LUA has a change in the deferred inflows of resources at the end of the current reporting year from the prior reporting year, this change needs to be reported at the government-wide financial reporting level.

	<u>DR</u>	<u>CR</u>
Deferred inflows of resources	\$XXXX	
Revenue		\$XXXX

Explanation - since conversion entry #13 above increases net position by the beginning deferred inflows of resources amount, the current years’ operations (i.e., revenues) should reflect the change in the deferred inflows of resources (i.e., from the end of the prior reporting year to the end of the current reporting year), which increases or decreases revenue by the increase or decrease in deferred inflows of resources amount. The above illustrative journal entry reports an increase in deferred inflows in resources (i.e., deferred inflows in resources amount was increased so the conversion entry eliminates the increase in deferred inflows in resources and increases current year revenues). A decrease in the deferred inflows of resources would reverse the debit and credit. This amount would be determined by comparing the deferred inflows of revenues for property taxes from the prior year with a comparable amount for the current year.

The LUA must record the accrued interest payable on any outstanding debt (e.g., bonds or capital leases) at the beginning of the fiscal year, if material.

	<u>DR</u>	<u>CR</u>
Net position	\$XXXX	
Accrued interest payable		\$XXXX

Explanation - since the accrued interest liability is not reported at the fund financial reporting level, the LUA must report this liability on the government-wide statement of net position. This entry reduces net position by the beginning amount of the liability. This amount of the accrual is determined by reviewing the last interest payment date. For example, if the interest paid through April 30 and the next interest payment is due October 31, the LUA should accrue two months of interest expense (i.e., for May and June). In our example, the LUA can review the amount of the October interest payment for the source of information. Then, take one-third (two months divided by six months) of this payment, which will be the amount of the accrual.

The LUA needs to adjust for the change in the accrued interest payable from the end of the prior year to the end of the current year. The following conversion journal entry illustrates an increase in the liability.

	<u>DR</u>	<u>CR</u>
Expense (interest)	\$XXXX	
Accrued interest		\$XXXX

Explanation - since conversion entry #14 above reduces net position by the beginning accrued interest liability, the current years' operations (i.e., expenses) should reflect the change in this liability. The above illustrative journal entry reports an increase in the liability. A decrease in the liability would reverse the debit and credit.

Reclassifications and Eliminations - In addition to the above referenced reclassification, there are other reclassifications and eliminations that should be made in the conversion process. Some transactions are reported at the fund level but are eliminated from the government-wide financial reporting level.

Interfund receivables and payable between governmental funds are reported on the balance sheets at the fund financial reporting level, but are eliminated on the government-wide statement of net position. The elimination entry follows:

	<u>DR</u>	<u>CR</u>
Interfund payables	\$XXXX	
Interfund receivables		\$XXXX

Explanation - GASBS 34 requires LUAs to eliminate any interfund receivables and payables between governmental funds so that they are not reported on the government-wide statement of net position. As a result, this entry eliminates both the interfund receivables and interfund payables by an equal amount. Since this entry affects only balance sheet accounts by an equal amount, technically it would not have to be recorded, but by reporting this conversion entry, it illustrates that the interfund receivables and payables are eliminated.

Governmental fund interfund transfers in and out are reported on the operating statement at the fund financial reporting level, but are eliminated on the government-wide statement of activities. The elimination entry follows:

	<u>DR</u>	<u>CR</u>
Other financing source - transfers in	\$XXXX	
Other financing use - Transfers out		\$XXXX

Explanation - GASBS 34 requires LUAs to eliminate any interfund transfers between governmental funds so that they are not reported on the government-wide statement of activities. As a result, this entry eliminates both the transfers in and the transfers out by an equal amount. Since this entry affects operating statement accounts by the same amount, technically it would not have to be recorded, but by reporting this conversion entry, it illustrates the elimination of the interfund transfers in and transfers out.

The internal service fund statement of net position accounts are reported in a separate column on the proprietary fund type statement of net position at the fund financial reporting level, but are combined with the governmental fund types on the government-wide statement of net position. An example of a reclassification follows by adding the internal service fund statement of net position accounts to the governmental fund type statement of net position accounts follows:

	<u>DR</u>	<u>CR</u>
Interfund receivable	\$ XXXX	
Inventories	XXXX	
Capital assets	XXXX	
Accumulated depreciation		\$ XXXX
Accounts payable		XXXX
Net position		XXXX

Explanation - In Georgia, generally only the larger LUAs utilize internal service funds. GASBS 34 requires LUAs to reclassify internal service fund net position by not reporting internal service funds on the government-wide statement of net position separately, but combining them with the governmental fund types on the statement of net position. The source of this information is the current year's proprietary statement of net position at the fund financial reporting level.

The operations of internal service funds that are reported at the fund financial reporting level must be eliminated from the government-wide statement of activities; otherwise, this information would be reported twice, once in the internal service fund and once in the fund that incurred the cost. In other words, if the internal service fund reported operating income, in essence, they over-charged the other funds' functions. If the internal service fund reported an operating loss, the LUA under-charged the other funds' functions. In order to eliminate the internal service fund's operations, we must first adjust the internal service fund's operating income to zero.

If the LUA overcharged the other funds, resulting in operating income to the internal service fund, the journal entry to eliminate the operating income is:

	<u>DR</u>	<u>CR</u>
Net position	\$XXXX	
Expenses (by function)		\$XXXX

Explanation - Since the total net position was increased by the ending balance (which reflects the current year's operating income) (see transaction #18 above), the current year operating income is eliminated and the numerous expenses are reduced by the same amount. By decreasing the governmental fund type functional expenses, this entry ultimately reduces operating revenue in the internal services fund, the operating income then is zero and the operation of this fund may be eliminated.

If the LUA undercharged the other funds, resulting in an operating loss to the internal service fund, the journal entry to eliminate the operating loss is:

	<u>DR</u>	<u>CR</u>
Expenses (by function)	\$XXXX	
Net position		\$XXXX

Explanation - Since the total net position was increased by the ending balance (which reflects the current year's loss) (see transaction #18 above), the current year operating loss is eliminated and the numerous expenses are increased by the related amount.

Appendix A
Example of Note Disclosure
Changes in Capital Assets

	Balance 07/01/20X4	Increases	Decreases	Balance 06/30/20X5
Governmental activities:				
Capital assets not being depreciated:				
Land	\$2,673,955	\$340,600	\$165,100	\$2,849,455
Construction in progress	<u>8,763,588</u>	<u>13,405,112</u>	<u>8,306,158</u>	<u>13,862,542</u>
Total capital assets not being depreciated	<u>11,437,543</u>	<u>13,745,712</u>	<u>8,471,258</u>	<u>16,711,997</u>
Depreciable capital assets:				
Buildings	49,459,209	11,072,811		60,532,017
Equipment	3,910,508	588,137	69,236	4,429,409
Buses	<u>572,045</u>	<u>127,062</u>	<u> </u>	<u>699,107</u>
Total depreciable capital assets	<u>53,941,759</u>	<u>11,788,010</u>	<u>69,236</u>	<u>65,660,533</u>
Total capital assets	<u>65,379,302</u>	<u>25,533,722</u>	<u>8,540,494</u>	<u>82,372,530</u>
Accumulated depreciation:				
Buildings	10,234,271	1,094,247	17,586	11,310,932
Equipment	1,558,009	237,403	34,976	1,760,436
Buses	<u>389,444</u>	<u>57,205</u>	<u> </u>	<u>446,649</u>
Total accumulated depreciation	<u>12,181,724</u>	<u>1,388,855</u>	<u>52,562</u>	<u>13,518,017</u>
Book value - depreciable capital assets	<u>41,760,035</u>	<u>10,399,155</u>	<u>16,674</u>	<u>52,142,516</u>
Governmental activities capital assets, net	<u>\$53,197,578</u>	<u>\$24,144,867</u>	<u>\$8,487,932</u>	<u>\$68,854,513</u>

Appendix B
Example of Note Disclosure
Changes in Capital Assets

Governmental Activities	Outstanding <u>7/1/20X4</u>	<u>Increases</u>	<u>Decreases</u>	Outstanding <u>6/30/20X5</u>	Amounts Due <u>in One Year</u>
General obligation bonds	58,930,000	\$10,475,000	\$11,970,000	\$57,435,000	\$1,875,000
Capital lease obligations	226,209	365,474	226,209	365,474	365,474
Compensated absences	<u>1,092,130</u>	<u>172,956</u>	<u>75,454</u>	<u>1,189,632</u>	<u>506,000</u>
Total Governmental Activities	<u>60,248,339</u>	<u>\$11,013,430</u>	<u>\$12,271,663</u>	<u>\$58,990,106</u>	<u>\$2,746,474</u>