

3. ACCOUNTING

3.1 Accounting Principles and Internal Controls

3.1.1 Fund Types and Accounting Principles

3.1.1.10 The following principles of accounting and financial reporting are based on those set forth in the Governmental Accounting Standards Board's (GASB) [Codification of Governmental Accounting and Financial Reporting Standards](#). The BARS manual permits accounting and financial reporting that conforms to these principles in all respects and requires GAAP municipalities to account and report in conformity with these principles, except that the annual report required is not as extensive as the Comprehensive Annual Financial Report (CAFR).

3.1.1.20 ACCOUNTING AND REPORTING CAPABILITIES

A governmental accounting system must make it possible both: (a) to present fairly and with full disclosure the funds and activities at the government in conformity with generally accepted accounting principles; and (b) to determine and demonstrate compliance with finance-related legal and contractual provisions.

3.1.1.30 FUND ACCOUNTING SYSTEMS

A governmental accounting system should be organized and operated on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. Fund financial statements should be used to report detailed information about primary government, including its blended component units. The focus of governmental and proprietary fund financial statements is on major funds.

3.1.1.40 TYPES OF FUNDS

In fund financial statements, governments should report governmental, proprietary, and fiduciary funds to the extent that they have activities that meet the criteria for using these funds.

Presented below is a system to classify all funds used by local government and the assignment of code numbers to identify each type of fund. A three digit code is used: the first digit identifies the fund type and the next two digits will be assigned by the governmental unit to identify each specific fund.

Governmental Funds

Code

000 General (Current Expense) Fund – should be used to account for and report all financial resources not accounted for and reported in another fund.

Although a local government has to report only one general fund in its external financial reports, the government can have multiple general *subfunds* for its internal managerial purposes. These managerial subfunds have to be combined into one general fund for external financial reporting.

Special Revenue Funds – should be used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specific purposes other than debt service or capital projects. *Restricted* revenues are resources externally restricted by creditors, grantors, contributors or laws or regulations of other governments or restricted by law through constitutional provisions or enabling legislation (similar to restricted component of net position used in government-wide reporting). *Committed* revenues are resources with limitations imposed by the highest level of the government, and where the limitations can be removed only by a similar action of the same governing body. Revenues do not include other financing sources (long-term debt, transfers, etc.).

The term *proceeds of specific revenue sources* establishes that one or more specific restricted or committed revenues should be foundation for a special revenue fund. They should be expected to continue to comprise a substantial portion of the inflows reported in the fund. While [GASB Statement 54](#) has not provided a numeric range for *substantial* portion of inflows, it was recommended that at least 20 percent is a reasonable limit for reporting a special revenue fund. Local governments need to consider factors such as past resource history, future resource expectations and unusual current year inflows such as debt proceeds in their analysis.

They may use the calculation below to determine whether an activity would qualify for reporting as a special revenue fund.

$$\text{Substantial portion of inflows} = \frac{(\text{restricted revenues} + \text{committed revenues})}{\text{total resources}^* \text{ reported in the fund}}$$

*Total resources would include all revenues and other financing sources.

Other resources (investment earnings and transfers from other funds, etc.) also may be reported in the fund if these resources are restricted, committed, or assigned to the specific purpose of the fund.

Governments should discontinue reporting a special revenue fund, and instead report the fund's remaining resources in the general fund, if the government no longer expects that a substantial portion of the inflows will derive from restricted or committed revenue sources.

The Statement requires all revenue to be recognized in the special revenue fund. If the resources are initially received in another fund, such as the general fund, and subsequently remitted to a special revenue fund, they should not be recognized as revenue in the fund initially receiving them. They should be recognized as revenue in the special revenue fund from which they will be expended. So, the local governments can either receive resources directly into the special revenue fund, or account for the resources as agency deposits in the receiving fund and, after remitting them, recognize them as revenue to the special revenue fund.

Special revenue funds should not be used to account for resources held in trust for individuals, private organizations, or other governments.

The general fund of a blended component unit should be reported as a special revenue fund.

The state statutes contain many requirements for special funds to account for different activities. The legally required funds do not always meet GAAP standards for external reporting. So, while the local governments are required to follow their legal requirements, they will have to make some adjustment to their fund structure for external financial reporting.

- 200 Debt Service Funds – should be used to account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest. Debt service funds should be used to report resources if legally mandated. Financial resources that are being accumulated for principal and interest maturing in future years also should be reported in debt service funds. The debt service transactions for a special assessment for which the government is not obligated in any matter should be reported in an agency fund. Also, if the government is authorized, or required to establish and maintain a special assessment bond reserve, guaranty, or sinking fund, [GASB Statement 6](#) requires using a debt service fund for this purpose.
- 300 Capital Projects Funds – should be used to account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays including the acquisition or construction of capital facilities or other capital assets. Capital outlays financed from general obligation bond proceeds should be accounted for through a capital projects fund. Capital project funds exclude those types of capital-related outflows financed by proprietary funds or for assets that will be held in trust for individuals, private organizations, or other governments (private-purpose trust funds).
- 700 Permanent Funds – should be used to account for and report resources that are restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government’s programs – that is for the benefit of the government or its citizens (public-purpose). Permanent funds do not include private-purpose trust funds which account for resources held in trust for individuals, private organizations, or other governments.

Proprietary Funds

Code

- 400 Enterprise Funds – may be used to report any activity for which a fee is charged to external users for goods or services. Enterprise funds are required for any activity whose principal revenue sources meet any of the following criteria:
- Debt backed solely by a pledge of the net revenues from fees and charges.
 - Legal requirement to recover cost. An enterprise fund is required to be used if the cost of providing services for an activity including capital costs (such as depreciation or debt service) must be legally recovered through fees or charges.

- Policy decision to recover cost. It is necessary to use an enterprise fund if the government's policy is to establish activity fees or charges designed to recover the cost, including capital costs (such as depreciation or debt service).

In addition, GAAP mandate the use of enterprise funds for the separately issued financial statement of public-entity risk pools. Public-entity risk pools also are accounted for as enterprise funds when they are included within a sponsoring government's report, provided the sponsor is not the predominant participant in the arrangement. Otherwise, they can use the general fund.

NOTE: Separate funds should not be reported for bond redemption, construction, reserves, or deposits, for any utility that is accounted for on the full accrual basis, using either the BARS accounts or a nationally recognized utility chart of accounts such as FERC or NARUC. Separate funds should not be reported even though bond covenants may stipulate a *bond reserve fund*, *bond construction fund*, etc. The bond covenant use of the term *fund* is not the same as the use in governmental accounting. For bond covenants, *fund* means only a segregation or separate account, not a self-balancing set of accounts. (See account 150 in the general ledger chart of accounts.)

- 500 Internal Service Funds – may be used to report any activity that provides goods or services to other funds, departments or agencies of the government, or to other governments, on a cost-reimbursement basis. Internal service funds should be used only if the reporting government is the predominant participant in the activity. Otherwise, the activity should be reported in an enterprise fund.

Fiduciary Funds

Code

- 600 Fiduciary Funds – should be used to account for assets held by a government in a trustee capacity or as an agent for individuals, private organizations, other governmental units, and/or other funds. These include (a) investment trust funds, (b) pension (and other employee benefit) trust funds, (c) private-purpose trust funds, and (d) agency funds.
- 600-609 Investment Trust Funds – should be used to report the external portion of investment pools reported by the sponsoring government.
- 610-619 Pension (and Other Employee Benefit) Trust Funds – should be used report resources that are required to be held in trust for the members and beneficiaries of defined benefit pension plans, defined contribution plans, other postemployment benefit plans, or other employee benefit plans.
- 620-629 Private-Purpose Trust Funds – should be used to report escheat property and all other trust arrangement under which principal and income benefit individuals, private organizations and other governments.
- 630-699 Agency Funds – should be used to report resources held by the government in a purely custodial capacity (assets and liabilities). Agency funds typically involve only the receipts, temporary investment, and remittance of fiduciary resources to individuals, private organizations, or other governments.

3.1.1.50 NUMBER OF FUNDS

Governments should establish and maintain those funds required by law and sound financial administration. Only the minimum number of funds consistent with legal and operating requirements should be established. Using numerous funds results in inflexibility, undue complexity and inefficient financial administration.

Local governments should periodically undertake a comprehensive evaluation of their fund structure to ensure that individual funds that became superfluous are eliminated from accounting and reporting.

Elected officials should be educated to the fact that accountability may be achieved effectively and efficiently by judicious use of department, program and other available account coding or cautious use of managerial (internal) funds.

3.1.1.60 REPORTING CAPITAL ASSETS

A clear distinction should be made between general capital assets and capital assets of proprietary and fiduciary funds. Capital assets of proprietary funds should be reported in both the government-wide and fund financial statements. Capital assets of fiduciary funds should be reported only in the statement of fiduciary net position. All other capital assets of the government are general capital assets. They should not be reported as assets in governmental funds but should be reported in the governmental activities column in the government-wide statement of net position. The *Capital Assets* (3.3.9 - 3.3.11) sections of the BARS manual provide additional information regarding accounting and reporting of capital assets.

3.1.1.90 REPORTING LONG-TERM LIABILITIES

A clear distinction should be made between fund long-term liabilities and general long-term liabilities. Long-term liabilities directly related to and expected to be paid from proprietary funds should be reported in the proprietary fund statement of net position and in the government-wide statement of net position. Long-term liabilities directly related to and expected to be paid from fiduciary funds should be reported in the statement of fiduciary net position. All other unmatured general long-term liabilities of the governmental unit should not be reported in governmental funds but should be reported in the governmental activities column in the government-wide statement of net position.

MEASUREMENT FOCUS AND BASIS OF ACCOUNTING IN THE BASIC FINANCIAL STATEMENTS

3.1.1.100 **Government-Wide Financial Statements**

The government-wide statement of net position and statement of activities should be prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions should be recognized when the exchange takes place. Revenues, expenses, assets, and liabilities resulting from nonexchange transactions should be recognized in accordance with the [GASB Statements 24 and 33](#).

3.1.1.110 **Fund Financial Statements**

In fund financial statements, the modified accrual or accrual basis of accounting, as appropriate, should be used in measuring financial position and operating results.

- a. Financial statements for governmental funds should be presented using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues should be recognized in the accounting period in which they become available and measurable. Expenditures should be recognized in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest on general long-term liabilities, which should be recognized when due.
- b. Proprietary fund statements of net position and revenues, expenses, and changes in fund net position should be presented using the economic resources measurement focus and the accrual basis of accounting.
- c. Financial statements of fiduciary funds should be reported using the economic resources measurement focus and the accrual basis of accounting, except for the recognition of certain liabilities of defined benefit pension plans and certain postemployment healthcare plans.
- d. Transfers should be reported in the accounting period in which the interfund receivable and payable arise.

NOTE: The various fund types may be grouped in the following manner to more clearly portray their relationship to an accounting basis:

Flow of Current Financial Resources Measurement Focus Funds - use the modified accrual basis:

000	General (Current Expense) Fund
100	Special Revenue Funds
200	Debt Service Funds
300	Capital Projects Funds
700	Permanent Funds

Flow of Economic Resources Measurement Focus Funds - use full-accrual basis:

400	Enterprise Funds
500	Internal Service Funds
600-609	Investment Trust Funds
610-619	Pension (and Other Employee Benefit) Trust Funds
620-629	Private-Purpose Trust Funds
630-699	Agency Funds

3.1.1.120 BUDGETING, BUDGETARY CONTROL, AND BUDGETARY REPORTING

- a. An annual/biennial budget should be adopted by every government.
- b. The accounting system should provide the basis for appropriate budgetary control.
- c. Budgetary comparison schedules should be presented as required supplementary information for the general fund and for each major special revenue fund that has a legally adopted annual/biennial budget. The budgetary comparison schedule should present both (a) the original and (b) the final appropriated budgets for the reporting period as well as (c) actual inflows, outflows, and balances, stated on the government's budgetary basis.

3.1.1.130 TRANSFER, REVENUE, EXPENDITURE, AND EXPENSE ACCOUNT CLASSIFICATIONS

- a. Transfers should be classified separately from revenues and expenditures or expenses in the basic financial statements.
- b. Proceeds of general long-term debt issues should be classified separately from revenues and expenditures in the governmental fund financial statements.
- c. Governmental fund revenues should be classified by fund and source. Expenditures should be classified by fund, function (or program), organization unit, activity, character, and principal classes of objects.
- d. Proprietary fund revenues should be reported by major sources, and expenses should be classified in essentially the same manner as those of similar business organizations, functions, or activities.
- e. At a minimum, the statement of activities should present:
 - (1) Activities accounted for in governmental funds by function, to coincide with the level of detail required in the governmental fund statement of revenues, expenditures, and changes in fund balances.
 - (2) Activities accounted for in enterprise funds by *different identifiable activities*.

3.1.1.140 COMMON TERMINOLOGY AND CLASSIFICATION

A common terminology and classification should be used consistently throughout the budget, the accounts, and the financial reports of each fund.

3.1.1.150 ANNUAL FINANCIAL REPORTS

- a. General purpose external financial reports should be prepared and published. Governments engaged in governmental and business-type activities should include, at a minimum:
 - (1) Management's discussion and analysis (MD&A).
 - (2) Basic financial statements. The basic financial statements should include:
 - (a) Government-wide financial statements.
 - (b) Fund financial statements.
 - (c) Notes to the financial statements.
 - (3) Required supplementary information (RSI) other than MD&A.

Governments engaged only in business-type activities should present only the financial statements required for proprietary funds. They should include:

- (1) Management's discussion and analysis (MD&A)
 - (2) Proprietary fund financial statements consisting of:
 - a. Statement of net position
 - b. Statement of revenues, expenses, and changes in fund net position
 - c. Statement of cash flows
 - (3) Notes to the financial statements
 - (4) Required supplementary information (RSI) other than MD&A, if applicable.
- b. The statements and reports listed above follow national standards of financial reporting. They should not be confused with legal reporting requirements, which are prescribed by the State Auditor's Office for all local governments in Washington State. The legal requirements are consistent with these national standards, but they are not identical. Specific legal reporting requirements are contained in reporting part of this Manual.
- c. A comprehensive annual financial report may be prepared and published, covering all activities of the primary government (including its blended component units) and providing an overview of all discretely presented component units of the reporting entity including introductory section, management's discussion and analysis (MD&A), basic financial statements, required supplementary information other than MD&A, combining and individual fund statements, schedules, narrative explanations, and statistical section. The reporting entity is the primary government (including its blended component units) and all discretely presented component units.
- d. The financial reporting entity consists of (1) the primary government, (2) organizations for which the primary government is financially accountable, and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's basic financial statements to be misleading or incomplete. The reporting entity's government-wide financial statements should display information about the reporting government as a whole distinguishing between the total primary government and its discretely presented component units as well as between the primary government's governmental and business-type activities. The reporting entity's fund financial statements should present the primary government's (including its blended component units, which are, in substance, part of the primary government) major funds individually and nonmajor funds in the aggregate. Funds and component units that are fiduciary in nature should be reported only in the statements of fiduciary net position and changes in fiduciary net position.

- e. The nucleus of a financial reporting entity usually is a primary government. However, a governmental organization other than a primary government (such as a component unit, joint venture, jointly governed organization, or other stand-alone government) serves as the nucleus for its own reporting entity when it issues separate financial statements. For all of these entities, the provisions the [GASB Statement 14](#) should be applied in layers *from the bottom up*. At each layer, the definition and display provisions should be applied before the layer is included in the financial statements of the next level of the reporting government.