**CHAPTER THREE**

**ACCOUNTING FOR GENERAL AND SPECIAL REVENUE FUNDS**

**UNIT objectives**

After reading this unit you will be able to;

* Discuss nature and operation of general and special revenue funds
* Distinguish, at the fund level, between Revenues and Other Financing Sources and between Expenditures and Other Financing Uses.
* Explain how budgetary accounting contributes to achieving budgetary control over revenues and expenditures, including such aspects as: Recording the annual budget, Accounting for revenues, Accounting for encumbrances and expenditures.
* Explain how revenues and expenditures are classified in the General Fund.

**Introduction**

Every state and local government must have a general fund that is used to account for all financial resources, except for those resources that must be accounted for in a different fund. A government may only maintain one general fund. This unit will discuss: The nature and purpose of the general and special revenue funds; Revenues and expenditures recognitions; and Examples of common journal entries.

* 1. **The General Fund**
		1. **Nature and Purpose**

Every governmental unit must establish a General Fund. The General Fund is used to account for most of the current operating revenues and expenditures of the unit including certain capital outlays and certain debt service expenditures. All tax revenues and other receipts and expenditures not specified by law or contractual agreement to another fund type are accounted for in the General Fund. This includes revenues and expenditures for federal programs. The General Fund is usually the largest and most important of the funds maintained by governmental units.

The General Fund typically has a greater number and variety of revenue sources than other funds and its resources finance a wide range of governmental activities. The General Fund is established at the inception of the governmental units and continues to exist throughout the life of the governmental system.

* + 1. **Number of Funds**

The governmental units will report only one General Fund; however, for practical purposes they may find it convenient to maintain separate and distinct components of the General Fund.

* + 1. **Basis of Accounting and Measurement Focus**

The focus of General Fund accounting is sources and uses of “available spendable resources” rather than upon net income determination. The General Fund uses the modified accrual basis of accounting. Therefore, revenues are recognized when they are both measurable and available. This fund also uses the flow of current financial resources measurement focus.

The General Fund contains only “current” assets and “current” liabilities. “Current,” meaning the asset is expected to be received or the liability paid within one year from the Balance Sheet date. General Fund assets and liabilities having a life greater than one year are reported on the entity wide statements.

Claims against the governmental unit should be recognized as General Fund liabilities when the claims are scheduled or applicable for liquidation with existing resources.

The General Fund has many sources of revenue and many types of expenditures, and hence, a need for numerous general ledger accounts. Excessive general ledger accounts are very inconvenient to work with. The local and state governmental unit may, therefore, use general ledger control accounts and subsidiary ledgers.

* + 1. **Accounts and Transactions**
	1. **Revenues and Other Sources of Financing**

Revenues represent increases in current financial resources. Proceeds from issuance of long-term debt and receipt of interfund transfers are not classified as revenue. Instead, these items are classified as “other sources of financing.” General Fund revenues are susceptible to accrual when they are both measurable and available. Revenues are measurable when they can be reasonably estimated. In order to be available, revenues are estimated to be collected during the current budgetary period or after the end of the period, but in time to pay liabilities outstanding at the close of the budgetary period. When amounts are both determined to be measurable and available, we classify them as “revenue accruals.” Do not record the item as revenue in the General Fund if the “measurable” and “available” conditions are not met. Many general fund revenues are measurable, such as taxes, grants and fees.

* 1. **Classification of Revenues**

The primary classification of government revenues is by fund. Within specific revenues may be classified by sources. Generally, there are seven sources. These are explained under:

* + 1. **Tax revenues**

Tax revenues constitute the large portion of governmental revenues and are compulsory or obligatory. In general, tax revenues may be classified in to three categories. These are direct taxes (personal income tax, business income tax, tax on dividend, rental income tax and miscellaneous income taxes), indirect taxes (turn over tax, value added tax, excise tax) and taxes on foreign trade (custom duty on imported goods and services, etc).

* + 1. **Special assessments**

Special assessments are levied against certain properties to defray part or all of the cost of specific improvements or services, which are presumed to be of particular benefit to the properties against which special assessments are levied. Special assessments are levied when routine services are extended to property owners outside the normal service of the government.

* + 1. **Licenses and permits**

They include those revenues collected by the governmental unit from individuals or business concerns for various rights or privileges granted to them, such as business license, driving license, building permit, etc.

* + 1. **Intergovernmental Revenues**

They include grants, entitlements, and shared revenues. A grant is a contribution or gift of cash or other assets from other governmental unit to be used or expended for specific purpose, activity or facility. There are two types of grants, namely capital grants and operating grants. Capital grants are restricted by the grantor for the acquisition or construction of fixed assets. All other grants are considered operating grants.

* + 1. **Charges for services**

They include revenues collected by the government from the public for the services rendered to them. These include revenue from courts, receipts from parking lots, library use fees, tuition fees etc. Library use fees do not include fines.

* + 1. **Fines and forfeits**

Forfeiture is the automatic loss of cash or other properties as a punishment for not complying with legal provisions and as compensation forms the resulting damages, or losses. Fines and forfeits include; Fines and penalties for commissions of statutory offences; Fines and penalties for neglect of office duties; Library fines; Forfeitures of amounts held as a security against loss or damages and Penalty of any sort. Penalties levied on delinquent taxes (past due taxes) are not considered as fines, rather are considered as tax revenues.

* + 1. **Miscellaneous revenues**

They include all revenues other than the above six categories of revenues, such as: Interest earnings on temporary investments; Rent and royalties; Compensation for loss of fixed assets; Contributions from public enterprises; Contributions from private sources; Contributions from donors, and others.

* 1. **Budgetary Accounts**

Budgetary accounts are those accounts that affect budgetary operations and conditions. Budgetary accounts include:

* **Estimated Revenue-** It is used to record total amount of revenue expected to be recognized (from revenue budget).
* **Appropriations-** which are used to record budgeted expenditures.
* **Encumbrances -** which are used to record estimated amount of purchase orders or contracts.
* **Estimated other financing sources-** are used to record estimated other financing sources.
* **Estimated other financing uses-** which are used to record estimated other financing uses.

In order to facilitate the preparation of financial statement that show budget and actual amounts, the accounting systems of funds which budgets are required by law should incorporate budgetary account.

* 1. **Journal Entries**
		+ - 1. **Recording the Budget: Budgetary entry:**

Estimated Revenues xxx

Estimated Other Financing Sources xxx

 Appropriation xxx

 Estimated Other Financing Uses xxx

 Fund Balance xxx

**Example 1**: Assume that a given governmental unit has made the following budget estimate for its general fund:

Estimated Revenues (Br.):

Taxes 780,000

Licenses and permits 256,000

Charges for services 184,000

Appropriations (Br):

Estimated Other Financing Sources (Br):

 Transfer from other funds 115,000

 Bond issue proceed 115,000

Health and Welfare 270,000

General Government 590,000

Public safety 440,000

**Required: Prepare a budgetary entry.**

Estimated Revenue 1,220,000

Estimated Other Financing Sources 230,000

 Appropriations 1,300,000

 Fund Balance 150,000

**Note that** budgetary surplus is said to exist when budgeted sources exceed budgeted uses. On the other hand, budgetary deficit is said to exist if budgeted uses exceed budgeted sources.

1. **Property Taxes and Uncollectible**

Property Taxes should be recorded in the fiscal year, in which they are levied, assuming they are also classified as available. Property taxes are considered available if they are expected to be collected within the current budgetary period, or within 60 days after the end of the period. In unusual circumstances, NCGA Interpretation-3 allows property taxes to be collected during a period longer than 60 days, but the financial statements must disclose both the length of the period used and the reason for using the longer period.

If taxes levied to finance the next fiscal year were collected in advance during the current period, the revenue should not be recognized. Instead, the amount collected should be recorded as deferred revenue. In the following fiscal year, a journal entry will be recorded to recognize the deferred revenue amount collected.

When property taxes are delinquent but expected to be collected, they should be reported as deferred revenue if it is estimated that the taxes will not be available to pay current obligations (collected within 60 days of the end of the fiscal year).

The governmental unit should disclose the assessment date, levy date, due dates and collection dates of taxes. Additionally, they must disclose their policy for recognizing property taxes.

State and local governmental units usually do not collect the entire tax levy. Accordingly, the amount recorded as revenue receivable from taxes often needs to be offset by an allowance for doubtful accounts. Governmental accounting does not recognize a “bad debt expense,” for these uncollectible, as does private business accounting. Instead, an allowance for doubtful accounts is established in the General Fund by reducing the amount of revenue recognized from taxes.

**Example 2:** Property taxes of Br. 20,000,000 are levied. Five percent of the levy is estimated to be uncollectible. The following entry would be made to record the levy:

Property Taxes Receivable-Current 20,000,000

 Revenue—Current Real Estate Taxes 19,000,000

 Estimated Uncollectible Taxes-Current 1,000,000

**Example 3:** Assume that Br.16, 000,000 of the tax receivables are collected and Br.750, 000 of the receivables is now deemed uncollectible: the following entry is made to record the collection:

1. Cash 16,000,000

 Property Taxes Receivable-Current 16,000,000

1. Estimated Uncollectible Taxes 750,000

 Property Taxes Receivable-Current 750,000

**Example 4:** Assume that the remaining receivable balance is considered delinquent; the journal entry used to record is as follow:

* + - 1. Property Taxes Receivable-Delinquent 3,250,000

 Property Taxes Receivable -Current 3,250,000

* + - 1. Estimated Uncollectible Taxes-Current 250,000

 Estimated Uncollectible-Delinquent 250,000

**Example 5:** Br. 400,000 is levied in property taxes during the current year. There is a history of 7.5 percent being uncollectible. Br. 4,000 receivable will not be collected until 90 days after the fiscal year end.

1. ***Revenue Recognized at the Beginning of the Fiscal Year (Time of Levy)***
	1. Taxes Receivable 400,000

 Revenue – Current R/E Taxes 370,000

 Estimated Uncollectible Taxes 30,000

(To record property tax levy)

* 1. Revenues – Current Real Estate Taxes 4,000

 Deferred Revenue 4,000

*(To record property taxes that does not meet the revenue recognition definition of available)*

1. ***Revenue Recognition upon Receipt***
	1. Taxes Receivable 400,000

 Estimated Uncollectible 30,000

 Deferred Revenues 370,000

 *(To record property tax levy)*

* 1. Cash 350,000

 Taxes Receivable 350,000

 *(To recognize revenue for current collections.)*

***Please note Common Errors to Avoid:***

* + Remember to record accrued taxes as of the end of the fiscal year properly. DO NOT report them as fund balance reservation. This error would incorrectly inflate your fund balance.
	+ Recognize Taxes Receivable to be collected within 60 days after year end as revenue and defer the remaining balance.

**Change in Estimate**

A change in estimate does not require that you restate prior financial statements. Only adjusting entries to the current year are required. Include an appropriate disclosure concerning the change in estimate in the financial statements if the effects of the change in estimate are material.

* A particular governmental unit may discover at the end of the accounting period that the allowance for uncollectible accounts for the current period was overstated or understated. To record the revised estimate, adjust the allowance and revenue accounts.
* An estimated uncollectible rate could be incorrect for several years, resulting in consistently overstating or understating uncollectible amounts.

**Example 6:** The uncollectible account should have been six percent, instead of five percent in ***Example 2***. The entry to record the revision at the end of the year would be:

Revenue – Current Real Estate Taxes 200,000

Estimated Uncollectible Taxes 200,000

(Br. 20,000,000 x 6% = Br. 1,200,000; Br. 1,200,000 – Br. 1,000,000 = Br. 200,000)

**Example 7:** The uncollectible accounts were understated by Br. 120,000 in prior years and by Br. 200,000 for the current year. The change in estimate is recorded as follows in the current period.

Revenue – Current Real Estate Taxes 320,000\*

 Estimated Uncollectible Taxes 320,000

(Br. 120,000 + Br. 200,000)

1. **Delinquent Property Taxes**

Taxes not paid by the due date on the bill are **delinquent.** The amount of taxes remaining in “taxes receivable – current year” should be transferred to “taxes receivable – delinquent.” If you maintain separate “allowance for uncollectible taxes” by year, then this account should also be transferred from a current account, to a delinquent account.

Delinquent taxes are usually subject to penalties and interest charges. The cash collection of interest and penalties is similar to the collection of the property taxes.

**Example 8:** To record the receipt of interest and penalties:

Cash XXX

 Interest and Penalties Receivable – Delinquent Taxes XXX

1. **Tax Anticipation Notes Payable**

Notes (or warrants) issued in anticipation of the collection of taxes, usually retriable only from tax collections, and frequently only from the proceeds of the tax levy whose collection they anticipate.

Taxes anticipation notes payable is issued by the governmental unit when expenditures are expected to be made before major items of revenues are received. The unit borrows in the anticipation of the collection of taxes in later months and use for the payment of notes. The transaction is recorded as follows:

Cash xxx

 Tax Anticipation Notes Payable xxx

The repayment of the note, with interest, is recorded as follows:

Tax Anticipation Notes Payable xxx

 Expéditeurs (interest) xxx

 Cash xxx

1. **Taxpayer-Assessed Revenues & Income Taxes**

In the past, accounting standards required that these revenues be recognized on a cash basis, although many governmental units chose to record these revenues when they were measurable and available. The Governmental Accounting Standards Board (GASB) Statement No. 22 put an end to this discrepancy between theory and practice by stating that these taxes must be accounted for using *modified accrual accounting*. Therefore, these amounts must meet the definitions of measurable and available in order to be recognized as revenue. Taxes should be reported net of anticipated refunds to taxpayers.

1. **Grants and Entitlements**
	* Grant means a contribution received from another government, which is to be used or expended for a specific purpose or activity.
	* Entitlement is the amount of payment a local government receives from another government as determined by a formula established by law. For example, Basic Education, Special Education, Transportation.

Before revenue can be recognized, you must evaluate the circumstances surrounding the grant or entitlement to determine if the measurable and available criteria have been met.

1. ***State Subsidies***

Recognize current fiscal year state subsidies as current revenue, even though the funds will be received in the subsequent fiscal year.

**Example 9:** Assume that Br. 50,000 of the current year transportation subsidy was not received as of the end of the budget period.

State Subsidies Receivable – Transportation 50,000

 Revenue – Transportation 50,000

1. **Donations**

Financial donations are usually recorded on the cash basis because they are not considered measurable until they are received.

The proper treatment of donated fixed assets depends on the governmental unit’s plans for those assets. If the unit intends to retain the fixed assets, they are recorded directly in the government wide statement of net assets, with no effect on the governmental funds. If, however, the unit intends to sell the donated fixed assets, that unit should record the transaction in one of three ways:

* + 1. If the assets are sold by the end of the fiscal year, report revenue in the operating statement.
		2. If the assets are sold after the end of the budget year, but before the financial statements are issued, report the fixed assets on the fund’s balance sheet as “assets held for resale” and report revenue on the operating statement.
		3. If the assets were not sold before the issuance of the financial statements, the assets should be reported only in the statement of net assets. When they are sold, the unit would report the sale.

Donations are valued at the Fair Market Value of the item at the time of the donation.

**Example 10:** Assume that a particular governmental unit receives a cash gift of Br. 1,000 from a private benefactor to be used at the discretion of the higher officials for general operations.

Cash 1,000

 Contributions and Donations 1,000

(To record receipt of revenue from a donation)

**Example 11:** Assume that a particular governmental unit receives a gift of land from a donor. An independent appraiser values the land at Br. 50,000 on the current market.

Using the above information, no entries should be completed, to record the general capital asset, on the General Fund; but the Statement of net Assets used to pass the following entry:

Land Br. 50,000

 Investment in Capital Assets Br. 50,000

(To record donated land as a general capital asset)

1. **Miscellaneous Revenues**

The state and local governmental units may collect a variety of other revenues such as fines, fees and charges. Since it is not practical to measure a number of these revenues, GASB’s Codification, Section 1600.113 recommends that some miscellaneous revenues should be accounted for on a cash basis unless the measurable and available criteria can be satisfied. Miscellaneous revenues should be accounted for in the General Fund. Use an Enterprise Fund, however, when a fee is charged to users in exchange for a service.

Other accrued revenues such as tuition, interest, etc are recorded as the current fiscal year if it meets the measurable and available criteria.

**Example 12:** The journal entries may look like:

Accounts Receivable – Type XXX

 Revenue – Type XXX

1. **Proceeds from Issuance of Long-Term Debt**

When long-term debt is issued and the proceeds are available to the General Fund, you should record the proceeds as part of “other financing sources.” These proceeds are reported in the General Fund on the Statement of Revenues and Expenditures, under the “Other Financing Sources” section of the statement. These proceeds should not be reported under the General Fund’s operating revenues. Although bond proceeds are reported in the General Fund, the long-term debt is reported in the non- current liabilities section on the statement of net assets, not in the General Fund.

If short-term debt is issued by the General Fund, i.e. debt to be paid off in one year or less, the debt liability is recorded in the General Fund because, the payment of the debt will require current resources.

**Example 13:** Assume that $10,000,000 of long-term notes are sold and the proceeds are available to the General Fund: the following entry should be recorded in the general fund;

**GENERAL FUND:**

Cash 10,000,000

Proceeds from Issuance of Long-Term Debt 10,000,000

**B. Expenditures and Other Financing Uses**

Expenditures are decreases in fund financial resources. Inter-fund transfers are not classified as expenditures, but instead are reported as “other financing uses.” Some examples of General Fund expenditures are current operations and repayment of principal and interest on long-term debt. Depreciation and amortization are not expenditures within the General Fund. Expenditures are generally accrued when incurred if the transaction results in a reduction of the General Fund’s current financial resources. However, expenditures for long-term debt principal and related interest are recognized when they are due. Do not record expenditure if there is not a reduction in the fund’s current financial resources. For example, a governmental unit may estimate a liability for compensated absences, but if the actual payments to employees are expected to be made after the current fiscal year, the expenditure would not be reported in the General Fund at year end. Expenditures are generally classified by function and object.

The Basic Entry Format for Expenditure should be:

Expenditure Account XXX

 Cash or Accounts Payable XXX

**Examples of Expenditure Items That Can Be Accrued:**

1. **Salaries and Benefits**

**Example 1:** Assume that there are total salaries and benefits of Br.425,000 that were earned but not paid as of Sene 30 of the budget year.

Expenditures – Salaries and Benefits 425,000

 Accrued Salaries and Benefits 425,000

**NOTE:** Payroll expenditures under GAAP reporting include those payroll costs incurred within the fiscal year. The actual disbursement of cash or payroll costs does not always occur in the fiscal year the costs were incurred. Payroll costs must include all payroll charges incurred whether or not they are paid during the same fiscal period.

1. **Interest Expenditure Accrual**

Record accrued interest expenditure/expense as a liability as the debt is due.

**Example 2:** Expenditures – Debt Service Interest 30,000

 Interest Payable 30,000

1. **Inventory**

Governmental accounting requires that amounts spent for the purchase of goods be recorded as expenditures at the time of the purchase. An exception is made for inventory. If the amount of inventory on hand at the end of budget year is significant, the value of such inventory should be recorded on the balance sheet as an asset. This inventory should be disclosed on the balance sheet and the method of accounting for inventory should be disclosed in the footnotes to the financial statements.

Examples of inventory include: Consumable goods, such as office supplies, paper, computer supplies, building and maintenance supplies, science lab supplies, etc.

Generally Accepted Accounting Principles (GAAP) permits two methods of expenditure recognition for inventories: purchase method and consumption method.

The **purchase method** recognizes expenditures for inventory when supplies are purchased. An inventory account and a fund balance reserve must be established at the end of the year.

The **consumption method** first records purchase transactions as supplies, then recognizes expenditures for inventory as supplies are used. The remaining balance in the inventory account at year end is reported as an asset. Since inventories do not finance current or future general fund expenditures, a portion of the fund balance equal to the value of the inventory must be reserved.

**Example 4:** Purchase Method Vs Consumption Method

|  |  |  |
| --- | --- | --- |
| **Transaction** | **Consumption Method (Periodic Inventory System)** | **Purchase Method** |
| Supplies of $75,000 are purchased. | Supplies 75,000  Cash 75,000 | Expenditures–Supplies75,000 Cash 75,000 |
| Based on a year end count, it is determined that $60,000 of the supplies was used during the year. | Expenditures – Supplies 60,000 Supplies 60,000  | No entry |
| Fund balance reserve is established at the end of the year. | Fund Balance 15,000  Fund Balance-Reserved for Supplies 15,000 | Supplies 15,000 Fund Balance- Reserved  for Supplies 15,000 |

1. **Capital Outlays**

The General Fund may purchase capital assets, such as land, buildings, and equipment. The general entries for these transactions are:

***GENERAL FUND:*** Expenditures – Capital Outlay XXX

 Cash XXX

The asset obtained is accounted for in the government wide statement of net assets.

1. **Debt Service Payments**

Debt service payments made from the debt service fund should be recorded in the debt service fund. Debt service transactions are described in detail in the duties addressing debt and debt service funds of this module.

A state and local governmental unit can appropriate and make certain debt payments from their general fund. Debt service payments made from the general fund are recorded in the general fund, not the debt service fund.

Principal and interest payments are recorded when principal and interest payments become due and payable.

**Example 5:** Assume that Br.1,000,000 of 6% bonds are issued on January 1, 2XX1 and pay interest semiannually beginning on July 1, 2XX1. Conditions of this specific bond requires it to be maintained within the general fund. The entry on July 1, 2XX1 in the general fund would be:

Expenditures – Interest 30,000\*

 Cash 30,000

 (To record semi-annual interest payment \*1,000,000\*6%/2)

**Example 6:** Assume there is no requirement to maintain the bond within the general fund. Funds for the interest payment are transferred from the general fund to the debt service fund on June 30, 2xx8.

GENERAL FUND

Transfer to Debt Service Fund 30,000

 Cash 30,000

DEBT SERVICE FUND

* 1. Cash 30,000

 Transfer from General Fund 30,000

* 1. Expenditures – Interest 30,000

 Interest Payable 30,000

When the payment includes a principal portion, you should make an appropriate reduction of the liability in the statement of net assets – non current liabilities section.

**C. Other Transactions Affecting the General Fund**

1. **Appropriations**

An appropriation is an authorization for administrators to incur liabilities in the amounts specified in the appropriation during the budget period. An appropriation is considered expended when the authorized liabilities have been incurred. When determining the uncommitted balance of appropriations, simply determining unrealized budgetary revenue is not sufficient. It is not enough to compare budgeted expenditures or appropriations against actual expenditures, encumbrances must be considered also.

1. **Encumbrances**

Encumbrance accounts allow for the recording of legal commitments issued against the appropriation of a fund. Legal commitments include items such as purchase orders for goods and/or supplies and contracts with suppliers. Recording encumbrances is essential to keeping expenditures within the approved budget. An encumbrance reserves a part of the appropriation at the time of commitment to ensure that resources will be available to cover the expenditure when the goods are delivered or the services rendered to the governmental unit. It is essential for good management and budgetary control to record expenditure commitments that will be paid later from fund resources. The accounting entry to record a commitment is debit Encumbrances and credit Reserve for Encumbrances.

The encumbrance account does not represent expenditure for the period, only a commitment to expend resources. Likewise, the account *reserve for encumbrances* is not synonymous with a liability account since the liability is recognized only when goods are received or the services are actually performed.

**Encumbrance Liquidation**

An encumbrance may be liquidated in whole or in part or canceled when any of the following situations occur:

* + Satisfactory receipt or legal acceptance of a partial or complete shipment of goods or services;
	+ Notice from or failure of the vendor to fulfill terms of the order or contract;
	+ Cancellation of the order; and
	+ If funds are not available due to lack of funds.

Notice that the issuance of purchase orders and/or contracts has two effects: (1) the encumbrance of the appropriation that gave the governmental unit the authority to order goods and services, and (2) the starting of a chain of events that will result in the governmental unit incurring a liability when the purchase orders are filled and the contracts executed. Both effects should be recorded in order to assist administrators in avoiding over expended appropriations and to plan for the payment of liabilities on a timely basis.

**Example 1:** Assume that a purchase order is written for Br.20, 000 on TIKIMIT 20, 2002. Later, on HIDAR 10, 2002, the actual invoice is received with the delivery in the amount of Br.18, 250. The entry to record this transaction is:

**TIKIMIT 20, 2002:**  Encumbrance 20,000

 Reserve for Encumbrances 20,000

 *(To record issuance of the purchase order)*

**HIDAR 10, 2002:** Reserve for Encumbrances Br.20, 000

 Expenditure Control / Subsidiary Accounts Br.18, 250

 Encumbrances Br.20, 000

 Vouchers Payable Br.18, 250

*(to record acquisition of the goods order and to offset the encumbrance accounts using combined entries)*

If this should happen, the available balance at the end of the initial accounting period would be overstated.

Expenditures and the liability account must both be recorded in the actual amount due the supplier. The fact that estimated and actual amounts differ causes no accounting difficulties as long as goods or services are received in the same fiscal period.

**Year-End Treatment of Encumbrances**

At the end of the fiscal year, all remaining encumbrances are considered reservation of fund balance not liabilities. They will become a liability when the goods and / or services are received in the following fiscal year. The budgetary estimate should include an estimated Reservation of Fund Balance as part of the funds available in the following fiscal year.

1. **Fund Balance**

The difference between governmental fund assets and liabilities is referred to as the fund balance. Therefore, the fund balance, for a particular governmental unit, is the difference between total assets and total liabilities as shown on the Balance Sheet or the Statement of Revenues, Expenditures, and Changes in Fund Balance in the Annual Financial Report.

1. **Inter-fund Activity**

Transactions may occur between funds. These interfund transactions are classified as revenue, expenditure or expense within the individual funds, but not to the governmental units overall. Interfund transactions are divided into four categories. These categories are (a) quasi-external transactions, (b) reimbursements, (c) inter fund loans, and (d) inter fund transfers. .

* + 1. **Quasi-External Transactions**

Those transactions that would have been recorded as revenues, expenditures or expenses had involved external organizations. The quasi-external transaction suggests the existence of a buyer-seller relationship. For example, charges for utilities or data processing provided by one fund to another fund.

These transactions should be accounted for as revenues and expenditures (or expenses) in the funds involved. Since each fund is an accounting entity, the amounts due to one fund from other funds, as well as the amounts owed to other funds, should be reflected in the fund accounts as **‘*due to’*** and **‘*due from’*** other funds transactions.

***Due to Other Funds*** is a liability account that reflects amounts owed to another fund for goods sold or services rendered. These amounts include only short-term obligations on open accounts, not interfund loans.

***Due from Other Funds*** is an asset account used to indicate amounts owed to a particular fund by another fund for goods sold or services rendered. This account also includes only short-term obligations on open accounts, not interfund loans.

**Example 2:** Internal Service Fund Billings: Assume that in a particular governmental unit the printing center gives a printing service costing Br.5,000 to the general-type activities; the journal entry is:

**General Fund:** Expenditure – Printing Service 5,000

 Due to Internal Service Fund 5,000

**Internal Service Fund:**

Due from General Fund 5,000

 Revenues - Printing Service 5,000

**Example 3:**  The Enterprise Fund bills the General Fund Br. 6,000 for services rendered, the quasi-external transactions would be recorded as follows:

**General Fund:** Expenditures 6,000

 Due To Other Funds – Enterprise Fund 6,000

**Enterprise Fund:** Due From Other Funds – General Fund 6,000

 Revenues 6,000

* + 1. **Reimbursements**

A reimbursement is a repayment of expenditure or expense initially made in one fund, but properly accounted for in another fund. One fund (the reimbursed fund) pays the expenditures or expenses of another fund (the reimbursing fund) with the understanding that the reimbursing fund will pay the reimbursed fund at a later date. Do not confuse these transactions with loans, advances or interfund transfers. The proper accounting for reimbursements is to record an expenditure or expense in the reimbursing fund, and a reduction of expenditure or expense in the reimbursed fund.

1. **When the General Fund is the Reimbursed Fund**

Record the initial payment of the expenditure or expense as expenditure in the General Fund. No entry is made in the reimbursing fund. When the reimbursing fund reimburses the General Fund, the General Fund reduces its expenditures by the amount received. The reimbursing fund then recognizes the expenditure or expense.

**Example 4:** The general fund pays a utility bill of Br.20,000 for the cafeteria fund. The initial payment is recorded in the general fund as:

1. Expenditures – Utilities 20,000

 Cash 20,000

When the cafeteria fund reimburses the general fund, the general fund reverses its original entry:

1. Cash 20,000

 Expenditures – Utilities 20,000

1. **When the General Fund is the Reimbursing Fund**

When the general fund is the reimbursing fund, this initial payment made by the other fund (reimbursed fund) is not recorded in the general fund. When the general fund reimburses the other fund, the expenditure is recorded in the general fund.

**Example 5:** The cafeteria fund made a Br.20,000 utility bill payment on behalf of the general fund. When the General Fund reimburses the cafeteria fund, the following entry would be made in the General Fund:

Expenditures – Utilities 20,000

 Cash 20,000

1. **Interfund Loans**

Interfund loans are made from one fund to another. The fund that made the loan expects to be repaid. Loans may be short-term or long- term. Interfund loan amounts are reported as gross. You should not net interfund loan amounts. Loans between funds are treated as balance sheet transactions. The borrowing fund reports a liability and an increase in cash. The lending fund reports a receivable and a decrease in cash.

1. ***Short Term Loans and the Short Term Portion of Long Term Loans***

Short-term loans and the short-term portions of long-term loans are expected to be repaid within twelve months. “Due To” and “Due From” accounts are used for short-term loans. The total of governmental unit’s “Due to Other Funds” account should equal the total of the “Due From Other Funds” account.

**Example:** Assume that general fund provides short term inter-fund loan to fund B for Br 1,000, the necessary journal entry to record the loan would be:

**General Fund:** Due From Fund B 1,000

 Cash 1,000

**Fund B:** Cash 1,000

 Due To General Fund 1,000

 (To record an interfund loan to Fund B)

1. **Inter fund transfers**

It is Nonreciprocal activity in which financial resources are transferred between funds with no intention of repayment. The receiving fund records Other Financing Sources—Interfund Transfers In; the giving fund records Other Financing Uses—Interfund Transfers Out.

 Some transactions are labeled as “other financing sources (uses)—transfers” in order to avoid reporting revenues and expenditures more than once in the governmental unit.

**Example:** Assuming that the General Fund made the budgeted transfer of Br. 204,000 to a Debt Service Fund for the payment of debt service, the General Fund entry would be as follows:’

Other Financing Uses—Transfers out Control . . . 204,000

 Due to Debt Service Fund . . . . . . . . . . . . ... 204,000

When the cash is transferred, the entry would be as follows:

 Due to Debt Service Fund . . . . . . . . . . . . . . . . . 204,000

 Cash .. . . . . . . . . . . . . . . . . . . . . . . …………………. 204,000

Example 2: Assume that the General Fund made a permanent transfer of Birr 596,000 to establish an internal service fund. The General Fund entry would be as follows:

 Other Financing Uses—Transfers Out Control. . . 596,000

 Cash . . . . . . . . . . . . . . . . . . . . . . . . . . .…………..596,000

**Preparing Closing Entries**

The essence of the closing process for the General Fund or special revenue funds of a state or local government is the transfer of the balances of the operating statement accounts and the balances of the budgetary accounts for the year to the Fund Balance account. Note that the first closing entry has the effect of reversing the entry to record the budget and the entry to amend the budget. After the closing entries are posted, the Fund Balance account represents the net amount of resources available for appropriation.

**Example 6: Given the following Closing entries information:**

Estimated Revenues Br. 1,625,000 , Appropriations Br.1,620,000 Revenues Br.1,620,000 Expenditures Br.1,610,000 Encumbrances Br.2,000

The closing entries may be made with a budgetary fund balance account as in “A” below or without a budgetary fund balance account as in “B” below:

1. **Closing entries with a budgetary fund balance:**
	1. Appropriations Control Account 1,620,000

 Budgetary Balance 5,000

 Estimated Revenues Control Account 1,625,000

 (To close budgetary accounts)

* 1. Revenues Control Account 1,620,000

 Expenditures Control Account 1,610,000

 Encumbrances Control Account 2,000

 Budgetary Fund Balance 8,000

*(To close the operating accounts and Encumbrances Control Account to the Budgetary Fund Balance.)*

* 1. Budgetary Fund Balance 8,000

 Unreserved Fund Balance 8,000

*(To close the balance of the Budgetary Fund Balance to the Unreserved Fund Balance.)*

1. **Closing entries without a budgetary fund balance account:**
	1. Appropriations Control Account 1,620,000

 Unreserved Fund Balance 5,000

 Estimated Revenues Control Account 1,625,000

 (To close budgetary accounts)

* 1. Revenues Control Account 1,620,000

 Expenditures Control Account 1,610,000

 Encumbrances Control Account 2,000

 Unreserved Fund Balance 8,000

*(To close the operating accounts and Encumbrances Control Account to the Unreserved Fund Balance)*

* 1. **Special Revenue Funds**

The purpose of a special revenue fund is to account for the proceeds of revenue sources that are **legally** restricted for specific purposes. Special Revenue Funds differ from enterprise funds in that the services delivered by a Special Revenue Fund are not financed by user charges. NCGA Statement 1 states that special revenue funds should be used only when legally mandated. Additionally, if resources are used to support expenditures made from the General Fund, these resources should be accounted for in the General fund. This task will discuss: the nature and purpose of Special Revenue Funds; and how Special Revenue Funds are established.

* + 1. **Nature and Purpose**

Special Revenue Funds are used to account for financial resources, which are restricted to expenditures for specified purposes.

* + 1. **Basis of Accounting and Measurement Focus**

As a governmental fund type, the focus of Special Revenue Fund accounting is on sources and uses of “available expendable resources” rather than upon net income determination. Special Revenue Funds are accounted for on a modified accrual basis of accounting as defined in this unit.

The Special Revenue Fund contains only current assets and current liabilities. Current meaning the asset is expected to be received or the liability paid within one year from the Balance Sheet date. Liabilities should be recognized as fund liabilities when the claims are scheduled or applicable for liquidation with existing resources.

**Note** that accounting for Special Revenue Funds are similar to that of the General fund we have illustrated in previous section of this unit.