GASB GOVERNMENTAL ACCOUNTING STANDARDS BOARD®

An Analyst's Guide to Government Financial Statements

3rd Edition

Dean Michael Mead

401 Merritt 7 • PO Box 5116 • Norwalk, CT • 06856-5116

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FOREWORD

Meeting the needs of financial statement users is a primary objective of the GASB. However, when users have difficulty understanding the financial statements issued by state and local governments, the importance of the information conveyed sometimes is lost.

This guide, a third edition of the highly successful user guide series, is written from the user's perspective. From an accountant's standpoint, this posed some challenges. For example, although every attempt was made to make the document technically pure, understandability is the goal of this guide. Because it is not an accounting pronouncement, this document has no standing in the formal hierarchy of generally accepted accounting principles and does not modify or interpret any authoritative pronouncements. The GASB members did not approve or clear this guide, so the accuracy of the content is the sole responsibility of the author and the director of research and technical activities.

Dean Mead, GASB senior research manager and author of this document, brings a unique but highly appropriate background to this project. Before joining the GASB in 1998, Dean spent over 10 years analyzing state and local government financial statements, primarily as assistant director of research for the Citizens Budget Commission of New York. He has spent countless hours working with financial statement users, preparers, and auditors in writing this guide. Without Dean's tireless efforts, the user guide series would not have become a reality.

The ultimate success of the GASB's efforts to improve governmental financial reporting depends on the users. We believe that the third edition of this guide will assist those users to better understand the state and local government financial reports they encounter.

February 2018
Norwalk, Connecticut

David R. Bean
Director of Research and Technical Activities

PREFACE

The GASB's original series of user guides was part of an effort to engage the users of governmental financial information in the process of establishing the standards for reporting that information. The GASB committed itself to communicating with users more plainly and with less accounting jargon and to focusing on how the work of the GASB would affect the kinds of information users would receive. The user guides were a centerpiece of that effort.

The first edition of *An Analyst's Guide to Government Financial Statements* was published in January 2001. The second edition, published in 2012, incorporated a separate user guide to notes and supporting information to produce a volume that comprehensively described financial reporting under generally accepted accounting principles. But neither the governmental environment nor governmental accounting standards are set in stone. Much has happened in the 6 years since the publication of second edition: the reporting of deferrals has been fully implemented; the standards for reporting pensions and retiree health insurance were revamped; and another 23 Statements of Governmental Accounting Standards have been issued, 8 of which relate to retirement benefits. This third edition encompasses the most important of those changes through December 2016. It also makes note of the most significant pronouncements of 2017—on fiduciary activities and leases—although their effective dates still are several years from now.

The guide benefited greatly from the advice of the GASB members and staff, for which I am grateful. I also would like to thank them for their support of the GASB's user outreach efforts. I am grateful as well to the Rutgers Business School students who used a draft of this guide in the Governmental Financial Analysis course and provided valuable input and corrected errors. This edition of the guide would not have reached the finish line were it not for the diligent attention of Ragan Bolesta, editor and supervisor of administration; Patti Waterbury, word processing specialist; and the production staff of the Financial Accounting Foundation.

Dean Michael Mead

SUMMARY CONTENTS

Page Number

Contents xi

Figures xxi

Part One. Introduction to This User Guide 1

Part Two. Overview of the Annual Financial Report 7

- The Contents of the Annual Financial Report 7
- Financial Statements 8
- Notes to Financial Statements 20
- Supporting Information 24

Part Three. Introductory and Background Information 27

- Introductory Section 27
- Auditor's Report 30
- Management's Discussion and Analysis 31
- Summary of Significant Accounting Policies 35

Part Four. Government-Wide Statement of Net Position 37

- Assets 39
- Liabilities 41
- Deferred Inflows of Resources and Deferred Outflows of Resources—Resources Related to Future Years 42
- Net Position 44
- What Can You Do with Statement of Net Position Information? 46

Part Five. Notes Related to the Statement of Net Position 51

- Assets 51
- Liabilities 77
- Deferred Inflows and Outflows of Resources 122
- Net Position 122

Part Six. Supporting Information Related to the Statement of Net Position 125

Page Number

Required Supplementary Information 125
Supplementary Information 139

Part Seven. Government-Wide Statement of Activities 157
Expenses 157
Program Revenues 160
Net Cost of Services 161
General Revenues and Other Changes in Net Position 162
Change in Net Position 163
What Can You Do with Statement of Activities Information? 164

Part Eight. Notes and Supporting Information Related to the Statement of Activities 169
Notes to Financial Statements 169
Supporting Information 179

Part Nine. Governmental Funds 193
Balance Sheet 195
Statement of Revenues, Expenditures, and Changes in Fund Balances 201
Note Disclosures Related to the Governmental Funds 209
Supporting Information Related to the Governmental Funds 220

Part Ten. Proprietary and Fiduciary Funds 235
Proprietary Funds Financial Statements 235
Note Disclosures on Proprietary Funds Segments 245
Supporting Information Related to Proprietary Funds 246
Fiduciary Funds Financial Statements 256
Supporting Information Related to Fiduciary Funds 264

Part Eleven. Special-Purpose Governments 267
Governments Engaged Only in Business-Type or Fiduciary Activities 268
Governments Engaged in a Single Governmental Program 269
Public College and University Financial Statements 275

Part Twelve. Entities Related to a Government 281
Component Units 281

Page
Number

Related Organizations, Joint Ventures, and Jointly Governed Organizations 288

Part Thirteen. Other Information 291

Prior-Period Adjustments: Corrections of Errors and Accounting Changes 291

Changes in Accounting Estimate 293

Going Concern 293

Subsequent Events 294

Finance-Related Legal and Contractual Provisions 295

Demographic and Economic Information 296

Operating Information 301

Other Schedules 303

Part Fourteen. Governmental Financial Analysis 307

Caveats of Financial Analysis 307

Common-Size Ratios 309

Economic Condition Analysis 315

Other Relevant Ratios and Information 338

Appendix A. Management's Discussion and Analysis A-1

Appendix B. Financial Statements for a State Government B-1

Appendix C. Financial Statements for a School District C-1

Appendix D. Financial Statements for a Public College or University Engaged in Both Governmental and Business-Type Activities D-1

Appendix E. Summary of Significant Accounting Policies and Other Illustrations E-1

Appendix F. Glossary of Terms F-1

Appendix G. Information about the GASB G-1

Appendix H. Alphabetical Index H-1

CONTENTS

Page Number

Figures xxi

Part One. Introduction to This User Guide 1

Part Two. Overview of the Annual Financial Report 7

The Contents of the Annual Financial Report 7

Financial Statements 8

Types of Activities Covered 8

Types of Information Presented 10

The Nature of the Information 11

Revenue availability 13

Nonexchange transactions 13

Two levels of statements, one complete picture 17

Distinguishing between the Parts of a Government 19

Notes to Financial Statements 20

Supporting Information 24

Part Three. Introductory and Background Information 27

Introductory Section 27

Letter of Transmittal 28

Financial Report Awards 29

Principal Officials and Organizational Chart 29

Audit Committee Letter 29

Auditor's Report 30

Management's Discussion and Analysis 31

Starting with the Basics 32

Revealing What the Financial Information Means 32

Capital Assets and Long-Term Debt 33

The Condition of Capital Assets 34

Currently Known Facts Bearing on the Future 34

Page Number

Summary of Significant Accounting Policies 35

Part Four. Government-Wide Statement of Net Position 37

Assets 39

Liabilities 41

Deferred Inflows of Resources and Deferred Outflows of Resources—Resources Related to Future Years 42

Net Position 44

What Can You Do with Statement of Net Position Information? 46

Ability to Meet Financial Obligations 47

Ability to Meet Service Commitments 49

Part Five. Notes Related to the Statement of Net Position 51

Assets 51

Deposits 51

What can you do with information about deposits? 52

Investments 53

Where fair value comes from 56

Exposure to risk 57

Repurchase agreements and reverse repurchase agreements 61

Securities lending 63

What can you do with investment information? 64

Receivables 66

Receivables that will not be collected within a year 66

What can you do with information about receivables? 67

Donor-Restricted Endowments 69

Capital Assets 70

Changes in capital assets 70

Asset impairment 74

Service concession arrangements 75

Liabilities 77

Payables 79

Page
Number

What can you do with payables information? ... 79
Short-Term Debt ... 80
What can you do with short-term debt information? ... 81
Long-Term Liabilities ... 81
What can you do with information about changes in long-term liabilities? ... 82
Debt refundings ... 84
Special assessment debt ... 86
Demand bonds ... 87
Derivatives ... 89
Risks associated with derivatives ... 96
What can you do with derivatives information? ... 97
Leases ... 98
Lease disclosures ... 99
Conduit Debt ... 99
Pensions and Other Postemployment Benefits ... 100
Costs and obligations related to pensions and OPEB ... 101
Descriptive information ... 103
Information about the measurement of the liability ... 105
Information about changes in the net liability ... 108
Governments in defined contribution plans ... 109
What can you do with pension and OPEB information? ... 109
Termination Benefits ... 112
Landfill Closure and Postclosure Care ... 113
Claims and Judgments ... 113
Nonexchange Financial Guarantees ... 118
Note disclosures for guarantors ... 119
Note disclosures for obligors ... 120
What can you do with information about nonexchange financial guarantees? ... 120
Contingent Liabilities ... 121
What can you do with information about contingent liabilities? ... 121

Page Number

Deferred Inflows and Outflows of Resources 122
Net Position 122

Part Six. Supporting Information Related to the Statement of Net Position 125
Required Supplementary Information 125
Pensions and OPEB 125
Changes in the liability and related ratios 125
Employer contributions 129
Notes to the schedules 131
Modified Approach Information about Infrastructure 132
What can you do with modified approach information? 135
Public Entity Risk Pools 135
Reconciliation of claims liabilities by contract 135
Ten-year claims development information 137
Supplementary Information 139
Capital Asset Indicators 139
What can you do with capital asset indicators? 141
Debt Service Ratios 142
What can you do with debt service ratios? 142
Debt Capacity 143
Trends in ratios of outstanding debt 143
Direct and overlapping debt 146
Debt limitations 149
Pledged-revenue coverage 151
Trends in Net Position 154
What can you do with trends in net position? 154

Part Seven. Government-Wide Statement of Activities 157
Expenses 157
Program Revenues 160
Net Cost of Services 161
General Revenues and Other Changes in Net Position 162

Page Number

Change in Net Position 163
What Can You Do with Statement of Activities Information? 164
What Do Services Cost, and How Much of That Cost Must Taxpayers Finance? 164
Where Does a Government Get Its Money, and How Does the Government Use It? 165
Is a Government Better or Worse Off Financially, and Why? 166
What Unusual Transactions Occurred During the Year? Was There Financial Activity between the Governmental and Business-Type Activities? 166
Will a Government Be Able to Finance Services in the Future? 167

Part Eight. Notes and Supporting Information Related to the Statement of Activities 169
Notes to Financial Statements 169
Depreciation Expenses 169
Debt Service 170
What can you do with debt service information? 170
Lease Payments 171
What can you do with information about leases? 171
Landfill Closure and Postclosure Care Costs 172
What can you do with information about landfill costs? 174
On-Behalf Payments 174
Special and Extraordinary Items 175
Tax Abatements 175
What can you do with tax abatement information? 176
Supporting Information 179
Trends in Revenues and Expenses 179
What can you do with trends in revenues and expenses? 180
Revenue Capacity 181
Revenue base 181
Revenue rates 187
Principal revenue payers 189
Property tax levies and collections 191
What can you do with revenue capacity information? 191

Page
Number

Part Nine. Governmental Funds 193
Balance Sheet 195
Fund Balance 196
Reconciliation 199
What Can You Do with Balance Sheet Information? 200
You can analyze the nature of current financial resources 200
You can assess short-term financing needs and a government's capacity to meet them 200
You can understand the relationships between government-wide and governmental funds statements and their respective accounting methods 201
Statement of Revenues, Expenditures, and Changes in Fund Balances 201
Surpluses and Deficits 204
Other Changes in Fund Balances 205
Reconciliation 205
What Can You Do with Information from the Statement of Revenues, Expenditures, and Changes in Fund Balances? 206
Will a government be able to finance services in the future? 208
Particular advantages of governmental funds information 208
Note Disclosures Related to the Governmental Funds 209
Interfund Balances and Transfers 209
What can you do with information about interfund balances and transfers? 210
Fund Balance 213
Category details 213
Stabilization arrangements 213
Spending order 214
What can you do with fund balance disclosures? 215
Detailed Reconciliations 215
What can you do with reconciliation disclosures? 216
Special Revenue Funds 218
Property Taxes 218
Supporting Information Related to the Governmental Funds 220
Budgets 220

Page
Number

What can you do with budgetary comparison information? 225
Funds 225
Nonmajor funds 226
Individual Funds 226
What can you do with this information? 226
Trends in Fund Balances 229
Trends in Revenues and Expenditures 229
What can you do with this trend information? 230

Part Ten. Proprietary and Fiduciary Funds 235
Proprietary Funds Financial Statements 235
Statement of Cash Flows 238
Types of cash flows 240
Reconciliation of cash and accrual 244
What can you do with statement of cash flows information? 244
Note Disclosures on Proprietary Funds Segments 245
What Can You Do with Segment Disclosures? 245
Supporting Information Related to Proprietary Funds 246
Nonmajor Enterprise Funds 246
Internal Service Funds 252
Individual Funds 252
What Can You Do with Supporting Information about Proprietary Funds? 252
Fiduciary Funds Financial Statements 256
What Can You Do with Fiduciary Funds Information? 256
Supporting Information Related to Fiduciary Funds 264
Fund Classifications 264
Individual Funds 264
What Can You Do with Supporting Information about Fiduciary Funds? 265

Part Eleven. Special-Purpose Governments 267
Governments Engaged Only in Business-Type or Fiduciary Activities 268
Governments Engaged in a Single Governmental Program 269

Page Number

Public College and University Financial Statements 275

Part Twelve. Entities Related to a Government 281

Component Units 281

What Can You Do with Component Unit Information? 283

Related Organizations, Joint Ventures, and Jointly Governed Organizations 288

What Can You Do with This Information? 289

Part Thirteen. Other Information 291

Prior-Period Adjustments: Corrections of Errors and Accounting Changes 291

Changes in Accounting Estimate 293

Going Concern 293

Subsequent Events 294

Finance-Related Legal and Contractual Provisions 295

Demographic and Economic Information 296

Principal Employers 300

What Can You Do with Demographic and Economic Information? 300

Operating Information 301

Government Employees 301

Operating Indicators 301

What Can You Do with Operating Information? 303

Other Schedules 303

Part Fourteen. Governmental Financial Analysis 307

Caveats of Financial Analysis 307

Definitions 307

Context 308

Persistence 308

Thoroughness 309

Common-Size Ratios 309

Percentage Change 309

Percentage Distribution 310

Adjusting for Inflation 312

Page
Number

Inflation-adjusted change in expenditures 312
Inflation-adjusted change in revenues 313
Potential Applications 313
Economic Condition Analysis 315
Financial Position 316
Fiscal Capacity 318
Liquidity 318
Solvency 320
Ability to Pay 323
Ability to pay off liabilities 323
Ability to raise revenues and pay for services 326
Revenue-Backed Debt 328
Pension and OPEB Information 330
Risk 331
Financial Efficiency 332
Receivables 332
Payables 333
Risk pools 334
Inventory 334
Capital assets 335
Service Capacity 336
Other Relevant Ratios and Information 338

Appendix A. Management's Discussion and Analysis A-1

Appendix B. Financial Statements for a State Government B-1

Appendix C. Financial Statements for a School District C-1

Appendix D. Financial Statements for a Public College or University Engaged in Both Governmental and Business-Type Activities D-1

Appendix E. Summary of Significant Accounting Policies and Other Illustrations E-1

Appendix F. Glossary of Terms F-1

Page
Number

Appendix G. Information about the GASB G-1
What Is the GASB? G-1
Who Is the GASB? G-1
What Is the GASB Trying to Accomplish? G-2
Who Are "Users"? G-2
How Does the GASB Establish Standards? G-3
Appendix H. Alphabetical Index H-1

FIGURES

Page Number

Figure 1. Government-Wide Statement of Net Position 38
Figure 2. Cash Deposits Note Disclosure 52
Figure 3. Investments Note Disclosure 55
Figure 4. Note Disclosure for Net Asset Value per Share 58
Figure 5. Interest Rate Risk Note Disclosure Using Weighted Average Maturity 60
Figure 6. Interest Rate Risk Note Disclosure Using Duration 61
Figure 7. Interest Rate Risk Note Disclosure Using a Simulation Model 62
Figure 8. Reverse Repurchase Agreement Note Disclosure 63
Figure 9. Securities Lending Note Disclosure 65
Figure 10. Receivables Note Disclosure (Narrative Format) 66
Figure 11. Receivables Note Disclosure (Tabular Format) 68
Figure 12. Capital Assets Note Disclosure 73
Figure 13. Service Concession Arrangement Note Disclosure 76
Figure 14. Payables Note Disclosure 78
Figure 15. Short-Term Debt Note Disclosure 81
Figure 16. Long-Term Liabilities Note Disclosure 83
Figure 17. Advance Refunding Note Disclosure 85
Figure 18. Demand Bond Note Disclosure 88
Figure 19. Note Disclosure of Summary Derivatives Information 93
Figure 20. Note Disclosure of Hedging Derivatives Net Cash Flows 94
Figure 21. Note Disclosure of Hedging Derivatives Risks 95
Figure 22. Descriptive Note Disclosures about Pensions 104
Figure 23. Pension Liability Measurement Note Disclosure 106

Page
Number

Figure 24. Note Disclosure of the Effect of the Healthcare Cost Trend Rate on the Net OPEB Liability 108

Figure 25. Changes in Net Pension Liability Note Disclosure 110

Figure 26. Risk Pool Note Disclosure 116

Figure 27. Nonexchange Financial Guarantees Note Disclosure 119

Figure 28. Schedule of Changes in the Net Pension Liability and Related Ratios 126

Figure 29. Schedule of Net Pension Liability Information for a Government in a Cost-Sharing Plan 128

Figure 30. Schedule of Actuarially Determined Employer Pension Contributions 130

Figure 31. Notes to Pension Schedules 132

Figure 32. Modified Approach Information 134

Figure 33. Reconciliation of Claims Liabilities by Contract 136

Figure 34. Schedule of 10-Year Claims Development Information 138

Figure 35. Statistical Section Schedule of Capital Asset Indicators 140

Figure 36. Statistical Section Schedule of Debt Ratios 144

Figure 37. Statistical Section Schedule of General Bonded Debt Ratios 145

Figure 38. Statistical Section Schedule of Direct and Overlapping Debt 148

Figure 39. Statistical Section Schedule of Debt Limitation Information 150

Figure 40. Statistical Section Schedule of Pledged-Revenue Coverage 153

Figure 41. Statistical Section Schedule of Net Assets/Position 155

Figure 42. Government-Wide Statement of Activities 158

Figure 43. Debt Service Requirements Note Disclosure 170

Figure 44. Future Minimum Lease Payments Note Disclosure 172

Figure 45. Landfill Closure and Postclosure Care Cost Note Disclosure 173

Figure 46. Tax Abatement Note Disclosure 177

Page
Number

Figure 47. Statistical Section Schedule of Changes in Net Assets/Position 182

Figure 48. Statistical Section Schedule of Revenue Base Information 184

Figure 49. Statistical Section Schedule of Direct and Overlapping Rates 185

Figure 50. Statistical Section Schedule of Principal Revenue Payers 186

Figure 51. Statistical Section Schedule of Principal Revenue Payers for a Government Reporting a Personal Income Tax 188

Figure 52. Statistical Section Schedule of Property Tax Levies and Collections 190

Figure 53. Governmental Funds Balance Sheet 197

Figure 54. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances .. 202

Figure 55. Reconciliation of Net Changes in Fund Balances to Change in Net Position (Separate-Page Format) 207

Figure 56. Interfund Balances Note Disclosure 211

Figure 57. Interfund Transfers Note Disclosure 212

Figure 58. Note Disclosure Reconciling the Governmental Funds Balance Sheet to the Government-Wide Statement of Net Position 217

Figure 59. Note Disclosure Reconciling the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances to the Government-Wide Statement of Activities 219

Figure 60. Budgetary Comparison Schedule 221

Figure 61. Budgetary Comparison Schedule for a Major Special Revenue Fund 222

Figure 62. Budgetary Comparison Reconciliation 224

Figure 63. Combining Balance Sheet, Nonmajor Governmental Funds 227

Figure 64. Combining Statement of Revenues, Expenditures, and Changes in Fund Balances, Nonmajor Governmental Funds 228

Figure 65. Statistical Section Schedule of Fund Balances 231

Figure 66. Statistical Section Schedule of Changes in Fund Balances 232

Figure 67. Statistical Section Schedule of Detailed Tax Revenues 233

Figure 68. Proprietary Funds Statement of Net Position 237

Page
Number

Figure 69. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position 239

Figure 70. Proprietary Funds Statement of Cash Flows 243

Figure 71. Condensed Statements, Segments 247

Figure 72. Combining Statement of Net Position, Nonmajor Enterprise Funds 249

Figure 73. Combining Statement of Revenues, Expenses, and Changes in Fund Net Position, Nonmajor Enterprise Funds 250

Figure 74. Combining Statement of Cash Flows, Nonmajor Enterprise Funds 251

Figure 75. Combining Statement of Net Position, Internal Service Funds 253

Figure 76. Combining Statement of Revenues, Expenses, and Changes in Fund Net Position, Internal Service Funds 254

Figure 77. Combining Statement of Cash Flows, Internal Service Funds 255

Figure 78. Statement of Fiduciary Net Position 258

Figure 79. Statement of Changes in Fiduciary Net Position 259

Figure 80. Combining Statement of Fiduciary Net Position 261

Figure 81. Combining Statement of Changes in Fiduciary Net Position 262

Figure 82. Combining Statement of Changes in Assets and Liabilities, Agency Funds 263

Figure 83. Statement of Net Position for a Single-Program Government (Single-Column Presentation) 270

Figure 84. Statement of Activities for a Single-Program Government (Single-Column Presentation) 271

Figure 85. Balance Sheet and Statement of Net Position for a Single-Program Government (Combined Presentation) 272

Figure 86. Statement of Revenues, Expenditures, and Changes in Fund Balances and Statement of Activities for a Single-Program Government (Combined Presentation and Statement of Activities Format) 273

Figure 87. Statement of Revenues, Expenditures, and Changes in Fund Balances and Statement of Activities for a Single-Program Government (Combined Presentation and Fund Statement Format) 274

Figure 88. Statement of Net Position for a College or University Engaged Only in Business-Type Activities 276

Page
Number

Figure 89. Statement of Revenues, Expenses, and Changes in Net Position for a College or University Engaged Only in Business-Type Activities 277

Figure 90. Statement of Cash Flows for a College or University Engaged Only in Business-Type Activities 278

Figure 91. Combining Statement of Net Position, Major Component Units 284

Figure 92. Combining Statement of Activities, Major Component Units 286

Figure 93. Condensed Statements of Net Position and Activities, Major Component Units 287

Figure 94. Note Disclosure of Violation of Bond Covenant and Actions to Resolve 295

Figure 95. Note Disclosure of Violation of Fund Balance Requirements and Actions to Resolve 296

Figure 96. Statistical Section Schedule of Demographic and Economic Statistics 297

Figure 97. Statistical Section Schedule of Principal Employers 299

Figure 98. Statistical Section Schedule of Government Employees 302

Figure 99. Statistical Section Schedule of Operating Indicators 304

Figure 100. Percentage Change Calculations for Assets in Figure 1 311

Figure 101. Percentage Distribution Calculations for Expenses in Figure 42 311

Figure 102. Comparison of Ratios with Peer Governments 328

Figure A. Management's Discussion and Analysis A-1

Figure B-1. Government-Wide Statement of Net Position, State Government B-3

Figure B-2. Government-Wide Statement of Activities, State Government (Two-Page Presentation) B-4

Figure B-3. Governmental Funds Balance Sheet, State Government B-6

Figure B-4. Reconciliation of Total Governmental Fund Balances to Total Net Position of the Governmental Activities, State Government B-7

Figure B-5. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, State Government B-8

Figure B-6. Reconciliation of Net Change in Governmental Fund Balances to Governmental Activities Change in Net Position, State Government B-9

Page
Number

Figure B-7. Proprietary Funds Statement of Net Position, State Government....B-10

Figure B-8. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, State Government....B-11

Figure B-9. Proprietary Funds Statement of Cash Flows, State Government....B-12

Figure B-10. Statement of Fiduciary Net Position, State Government....B-13

Figure B-11. Statement of Changes in Fiduciary Net Position, State Government....B-14

Figure C-1. District-Wide Statement of Net Position, School District....C-3

Figure C-2. District-Wide Statement of Activities, School District....C-4

Figure C-3. Governmental Funds Balance Sheet, School District....C-5

Figure C-4. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, School District....C-6

Figure C-5. Reconciliation of Net Changes in Governmental Fund Balances to Governmental Activities Change in Net Position, School District....C-7

Figure C-6. Proprietary Funds Statement of Net Position, School District....C-8

Figure C-7. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, School District....C-9

Figure C-8. Proprietary Funds Statement of Cash Flows, School District....C-10

Figure C-9. Statement of Fiduciary Net Position, School District....C-11

Figure C-10. Statement of Changes in Fiduciary Net Position, School District....C-12

Figure D-1. Institution-Wide Statement of Net Position, Public College or University....D-3

Figure D-2. Institution-Wide Statement of Activities, Public College or University....D-4

Figure D-3. Governmental Funds Balance Sheet, Public College or University....D-5

Figure D-4. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, Public College or University....D-6

Figure D-5. Proprietary Funds Statement of Net Position, Public College or University....D-7

Figure D-6. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, Public College or University....D-8

Page
Number

Figure D-7. Proprietary Funds Statement of Cash Flows, Public College or University D-9

Figure E-1. Auditor's Report E-3

Figure E-2. Summary of Significant Accounting Policies E-6

Figure E-3. Schedule of Contractually Required Employer Pension Contributions E-11

Figure E-4. Calculations to Determine Local City's Major Funds E-12

Figure E-5. Schedule of Capital Assets by Function E-13

PART ONE

INTRODUCTION TO THIS USER GUIDE

There are more than 90,000 state and local governments in the United States. In addition to 50 state governments, there are tens of thousands of local governments—counties, cities, towns, villages, and so on. There are school districts, water districts, park districts, fire districts, and special districts for myriad other purposes. Public authorities are created by states and localities to build housing, coordinate economic development incentives, provide low-cost loans, treat wastewater, operate electric utilities, and construct hospitals, as well as for other activities.

There also are countless numbers of people who follow and analyze the financial activities of those governmental entities. Some are intensive users of governmental financial information—analysts from rating agencies, mutual funds, insurance companies, and banks. Other regular and informed users can be found in research organizations and citizen and taxpayer groups. Some users are located *within* governments—legislators and their staffs, oversight boards, and internal managers. The overwhelming majority of users—everyday citizens—do not directly analyze governmental financial information but, rather, consume information after it has been analyzed by intensive users and repackaged in a more meaningful and broadly accessible form.

The many different kinds of users of financial information have one thing in common: they use the information as part of their decision-making process. These decisions include:

- Whether to buy, hold, or sell a government's bonds
- Where to buy a house, or send a child to school, or locate a business
- Whom to elect for school board or county commission
- How to vote on a proposed issue of state bonds or a property tax increase.

Another common reason that people use governmental financial information is to assess whether governments have been accountable. Managers of corporations keep track of their finances to ensure that they bring in more resources than they send out and thereby earn a profit for their shareholders. Most activities of a government, however, are not motivated to make a profit. Nevertheless, a government still needs to demonstrate to its considerably larger and more diverse shareholders—citizens—and creditors that it has been financially accountable. Even if a government is not expected to generate profits, it still needs to raise enough resources to remain financially viable. Further, as we shall see, governments need to demonstrate their ACCOUNTABILITY for more than just staying solvent. The fact that a government's activities may be very unlike private-sector transactions necessitates special care by a government to demonstrate its STEWARDSHIP over public monies through FINANCIAL STATEMENTS and other means.

Governments do engage in some business-like activities (electric and water utilities are examples), providing a good or service in return for a payment from the actual recipient or user of the service. But most government services are quite unlike private goods and services. Rather than charge fees or prices directly to the consumer, governments levy taxes on property, income, and retail sales to finance services such as police and fire protection, elementary and secondary education, and parks. In such instances, there is no obvious connection between the payment made by the customer (taxes) and the provision of the service. Who is to say whether it was the sales taxes or the property taxes that paid for the police officers' salaries? Who can tell whether the taxes on retail sales in August paid for government services at that time or whether they financed activities the following March?

Another important factor that shapes how a government demonstrates its accountability is the involuntary nature of taxes. In the private sector, customers usually can choose what they want from a variety of products and a multitude of sellers and *voluntarily* exchange cash or a promise to pay (a credit card charge, perhaps) in return. By contrast, governments *impose* taxes on citizens and businesses, which are required to pay *involuntarily* without necessarily seeing what services they will get in return. In other words, no business-like exchange of resources for services takes place. Furthermore, it is much more difficult and time-consuming for the recipient of government services to switch providers. The business customer may only have to cross the street to find another store, whereas the citizen-taxpayer would have to move to another town or county or wait until the next election to select new government officials.

The combination of involuntary financing and the indirect relationship between the financing and provision of government services requires special efforts to demonstrate accountability. Governments seek to show not only that they made ends meet in the aggregate, but also how they used taxpayer dollars to provide services. Furthermore, governments need to prove that they have complied with the many laws and regulations stipulating what, how, when, and where they provide and finance services. Governments employ a variety of means to achieve those ends; financial statements are a principal method. Each year, governments prepare for the public a set of financial statements specially designed to support the unique accountability relationship between a government and its citizens.

State and local government annual financial reports prepared in accordance with **GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP)** are an important source of information upon which decisions and assessments of accountability are based. The American Institute of Certified Public Accountants (AICPA) recognizes the standards established by the **GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB)** as constituting U.S. GAAP. This guide describes the information that can be found in GAAP-based financial reports and explains how that information can be used for decision making and accountability assessments. This and the other volumes in the GASB's User Guide Series are founded on the premise that the annual financial reports of governments contain information that is valuable to the people and groups to which governments are accountable. The guides are intended to familiarize you with the basic parts of a government's annual financial report, and to help you understand what

the information they contain means and how it may be relevant to the important decisions you make in your life and work.

GAAP requires that a financial report include the following items:

- The BASIC FINANCIAL STATEMENTS contain the principal information about a government's finances. Part Two of this guide provides an overview of financial statement information, which comes in three forms:
  - The GOVERNMENT-WIDE FINANCIAL STATEMENTS contain comprehensive financial information about all activities of a government (except FIDUCIARY ACTIVITIES) and are discussed in Parts Four through Eight. Depending on the type of government, these statements might alternatively be called district-wide or institution-wide statements.
  - Each of the FUND FINANCIAL STATEMENTS focuses on information related to particular kinds of activities of a government. These statements are covered in Parts Nine and Ten.
  - The NOTES TO FINANCIAL STATEMENTS provide detailed information supporting the data in the statements and are described in this guide along with the financial statements to which they relate.
- The basic financial statements are presented between two sets of REQUIRED SUPPLEMENTARY INFORMATION (RSI) that are important for a complete understanding of the financial statements:
  - MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A) precedes the financial statements; it prepares you to use the statements by providing a narrative overview of the information contained in the basic financial statements and other RSI. MD&A is discussed in Part Three.
  - The remaining RSI follows the notes. One part of the RSI is a BUDGETARY COMPARISON that contrasts information from a government's originally adopted budget, its final modified budget, and its actual results for the year. (Governments have an option to present the budgetary comparison with the basic financial statements.) When applicable, there is other RSI relating to retirement benefits and risk pools, as well as the physical condition of bridges, roads, and other INFRASTRUCTURE assets and the government's efforts to maintain their condition. Those forms of RSI are discussed in the same sections of this guide as the financial statements to which they relate.

Some governments, especially larger ones, include their financial statements in a COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR), which contains additional statements and schedules that contain relevant financial, economic, and demographic information, often for multiple years. The CAFR has three sections—INTRODUCTORY SECTION, FINANCIAL SECTION, and STATISTICAL SECTION. This additional information is described throughout the guide.

The GAAP-required financial reporting described in this guide applies to *all* state and local governments, including not only GENERAL PURPOSE GOVERNMENTS such as states, counties, cities, towns, and villages, but also SPECIAL-PURPOSE GOVERNMENTS like school districts, public colleges and universities, public hospitals and healthcare systems, public museums and cultural institutions, libraries, water districts, public employee retirement systems (PERS), and so on. The financial

statements of some special-purpose governments may provide information in a slightly different format from those of general purpose governments. The methods employed by special-purpose governments are discussed in Part Eleven. Part Twelve discusses information about specific parts of a government, such as COMPONENT UNITS. Part Thirteen captures the remaining miscellaneous information in a government financial report, including economic and demographic information.

The last section of this guide covers the very basics of analyzing government financial statements. Starting with some overarching principles of analysis, the guide goes on to explore a variety of analytical tools—FINANCIAL RATIOS. The purpose of Part Fourteen is to identify some common methods for analyzing financial statement information. This guide does not, however, go further than that. The next step—making a decision based on your analysis and interpretation of the financial statements—is entirely yours to take. This guide offers some insights into the general meaning of financial statement information, but ultimately, *you* have to decide what is "good" versus "bad," "high" versus "low," or "prudent" versus "unwise."

This guide is written for a reader with at least a rudimentary knowledge of simple accounting and financial reporting concepts; it presumes familiarity with basic vocabulary. Even so, the guide contains a variety of aids to assist you:

- The text of the guide is accompanied by sample financial statements for a local government. In many instances, valuable additional information is conveyed in annotations on the illustrative statements. Additional illustrations are included in Appendices A through E:
  - Appendix A is a sample MD&A.
  - Appendix B contains a set of financial statements for a state government.
  - Appendix C contains a set of financial statements for a school district.
  - Appendix D contains a set of financial statements for a community college.
  - Appendix E contains additional financial schedules and disclosures and other pertinent information.
- The text frequently is accompanied by margin notes and boxes with additional information. Conceivably, you could read through the main text of this guide without reading those notes and boxes and you would still learn what the guide is meant to convey. The notes and boxes provide material for looking at the topics in a little more depth:
  - **Keep in mind…** raises important issues you may wish to consider as you read the guide or as you analyze a government's financial statements.
  - **Upon further review…** delves a layer or two deeper into topics covered in the text, raising relevant qualifying facts and offering additional examples.
  - **By the numbers…** expands on the brief definitions of key terminology presented in the text.
  - **Tools of the trade…** offers tips on how to analyze financial statement information.
- The language spoken by accountants can seem foreign, as if they have a different word for everything. This guide includes "accounting-ese" alerts: Words and phrases printed in MAROON

CAPITAL LETTERS are defined in Appendix F, the glossary. Some especially important terms also are defined nearby in the margin of the page.

- Appendix G offers some background information about the GASB and how state and local government accounting and financial reporting standards are established in the United States.

By the numbers…acronym guide

Not only has accounting developed its own language (see Appendix F, the glossary), but its practitioners use a lot of acronyms. Here is a list of selected acronyms used in this guide and in governmental accounting. It may be your Google Translate for governmental accounting.

AICPA: American Institute of Certified Public Accountants
BFS: basic financial statements
BTA: business-type activity
CAFR: comprehensive annual financial report
CPA: certified public accountant
FAF: Financial Accounting Foundation
FASAB: Federal Accounting Standards Advisory Board
FASB: Financial Accounting Standards Board
GAAFR: governmental accounting, auditing, and financial reporting
GAAP: generally accepted accounting principles
GAAS: generally accepted auditing standards
GAGAS: generally accepted government auditing standards
GASAC: Governmental Accounting Standards Advisory Council
GASB: Governmental Accounting Standards Board
GO: general obligation
IPSASB: International Public Sector Accounting Standards Board
MD&A: management's discussion and analysis
MFBA: measurement focus and basis of accounting
NCGA: National Council on Governmental Accounting
NOL: net OPEB liability
NPL: net pension liability
OPEB: other postemployment benefits
PERS: public employee retirement system
RSI: required supplementary information
SI: supplementary information
TOL: total OPEB liability
TPL: total pension liability

Terms in MAROON CAPITAL LETTERS are defined in Appendix F, the glossary. Some especially important terms also are defined in the margins of the page.

A note to the reader…

This guide discusses the financial reports of governments under the assumption that they are prepared according to existing standards of accounting and financial reporting. However, not all governments prepare their financial reports in accordance with GAAP, so you may not see everything discussed here in every government's financial report.

ACCOUNTABILITY is the responsibility of a government to justify its actions

FINANCIAL STATEMENTS are documents that a government prepares for reporting its finances

NOTES TO FINANCIAL STATEMENTS contain information that expands on and explains the information in the financial statements

REQUIRED SUPPLEMENTARY INFORMATION makes financial statement information and notes more understandable by placing them in context

INFRASTRUCTURE consists of particularly long-lived, stationary capital assets, such as highways, bridges, and sewers

GENERAL PURPOSE GOVERNMENTS are states, counties, cities, and other governments that provide a variety of public services

SPECIAL-PURPOSE GOVERNMENTS are school districts, utilities, colleges, and other governments that provide a single service or a few related services

PART TWO

OVERVIEW OF THE ANNUAL FINANCIAL REPORT

WHAT'S AHEAD?

- WHAT FINANCIAL STATEMENTS ARE IN A GOVERNMENT'S ANNUAL FINANCIAL REPORT?
- HOW DO THEY DIFFER?
- WHAT OTHER THINGS WILL YOU FIND IN THE FINANCIAL REPORT?

THE CONTENTS OF THE ANNUAL FINANCIAL REPORT

If a government prepares its annual financial report in accordance with GAAP, these items typically are presented in the following order in the report:

- MD&A (illustrated in Appendix A)
- Basic financial statements
  - Government-wide financial statements
    1. STATEMENT OF NET POSITION (see Figure 1 in Part Four, for example)
    2. STATEMENT OF ACTIVITIES (Figure 42 in Part Seven)
  - Fund financial statements
    - Governmental funds statements
      3. BALANCE SHEET (Figure 53 in Part Nine)
      4. STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES (Figures 54 and 55)
    - Proprietary funds statements
      5. Statement of net position (Figure 68 in Part Ten)
      6. STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION (Figure 69)
      7. STATEMENT OF CASH FLOWS (Figure 70)
    - Fiduciary funds statements
      8. STATEMENT OF FIDUCIARY NET POSITION (Figure 78 in Part Ten)
      9. STATEMENT OF CHANGES IN FIDUCIARY NET POSITION (Figure 79)
  - Notes to the basic financial statements
- Required supplementary information (other than MD&A).

FINANCIAL STATEMENTS

Financial statements are the core of the annual financial report. This is where the most fundamental information about a government's finances is reported. The notes to financial statements and RSI that also are included in a financial report are intended to expand upon the information in the financial statements and to help you better understand it, respectively.

Depending on the kinds of activities a government engages in, its annual financial report may contain all nine of the basic financial statements listed above. Each financial statement presents information about an important aspect of a government's finances. The financial statements differ in three key ways—the types of activities they focus on, the types of information they contain, and the nature of that information.

Types of Activities Covered

The two government-wide financial statements (1 and 2 in the list on the previous page) encompass the entirety of a government's activities (except fiduciary activities). They present information intended to convey a comprehensive picture of a government's finances related to all of its activities. The information for GOVERNMENTAL ACTIVITIES is shown separately from that for BUSINESS-TYPE ACTIVITIES (BTAs), and the two are added together for the total PRIMARY GOVERNMENT. Financial information about a government's DISCRETELY PRESENTED COMPONENT UNITS is shown in a separate column on these financial statements. The only activities not included in the government-wide statements are fiduciary activities—those in which the government acts as a trustee or agent for resources that belong to others. Fiduciary activities are reported separately in the fiduciary fund financial statements (see more below and in Part 10).

The fund financial statements (3 through 9 in the list on the previous page) look at a government's finances in more detail. The information is divided into FUNDS that focus on the finances related to specific revenue sources or particular types of activities. The GOVERNMENTAL FUNDS track the finances of all of the activities not accounted for in the other two categories of funds. Typically, the most common public services are found here. These are roughly synonymous with governmental activities, though governmental activities generally also include the INTERNAL SERVICE FUNDS (which are described below). Governmental activities predominantly will be found in the GENERAL FUND, though some specific revenue sources that are limited to a particular purpose may be reported in a SPECIAL REVENUE FUND. The repayment of outstanding BONDS often takes place in a DEBT SERVICE FUND, and the purchase and construction of buildings, bridges, streets, and other long-lived assets usually is accounted for in a CAPITAL PROJECTS FUND. If a government has resources that are restricted such that only the earnings they generate when invested (and not the resources themselves) can be spent for public purposes, those resources are reported in a PERMANENT FUND.

The PROPRIETARY FUNDS track the finances of the activities for which a government charges customers directly for the services they receive rather than financing them with taxes and other general revenues. Water and sewer services often are reported in an ENTERPRISE FUND, a type of proprietary fund used to track fee-based activities that provide services to the public. The activities accounted for in a government's enterprise funds generally are synonymous with its BTAs. Internal service funds, on the other hand, are used for services provided to other funds of a government, in return for a fee to reimburse costs; they also may provide services to other governments. Such funds might be related to

a central car pool or supply function, for instance. Because internal service funds primarily do business with other parts of a government, the financial statements would double-count their TRANSACTIONS if they were included as a whole in the government-wide financial statements. For example, when that car pool records an inflow or REVENUE, typically another part of the government is recording an outflow or EXPENSE. The car pool also records its own expenses for the costs it incurs. To avoid double-counting revenues and expenses, only the *net* impact of the financial activity of internal service funds is included in the government-wide statements.

FIDUCIARY FUNDS are used to keep tabs on resources that a government is holding for others outside the government; these resources cannot be used to support the governmental activities and BTAs. A government may act as a trustee or agent over these resources for someone else, such as a government's employees, other governments, or private citizens. The principal example of such an arrangement is an employee pension plan, which is accounted for in a PENSION (AND OTHER EMPLOYEE BENEFIT) TRUST FUND. A government may be responsible for providing resources to the plan and investing and maintaining those resources, and it may operate the benefits distribution aspect of the plan, but the resources in the plan are not available to the government to finance services. For this reason, fiduciary activities are not included in the government-wide statements, because including resources that do not belong to a government might be misleading if you are trying to assess the government's financial health.

If a government manages an investment pool, it will use an INVESTMENT TRUST FUND to account for the investments that belong to other governments participating in the pool (the government's own investments are reported in the other financial statements along with its other assets). Any other type of trust arrangement would be reported in a PRIVATE-PURPOSE TRUST FUND. (Trust arrangements minding resources for *public* purposes are reported as permanent funds, if a portion of the resources cannot be spent, or as special revenue funds.) Finally, if a government holds resources temporarily before disbursing them—for instance, it may collect taxes on behalf of other governments and then distribute them—it would utilize an AGENCY FUND to report this activity. (See **Upon further review…categories of fiduciary funds and their financial statements** on pages 264 and 265 regarding changes that will begin to take place in 2019.)

Types of Information Presented

A government generally prepares two types of financial statements—position statements and flows statements. Position statements compare what a government owns (ASSETS) and outflows of resources related to future periods (DEFERRED OUTFLOWS OF RESOURCES) with the amounts it owes (LIABILITIES) and inflows of resources related to future periods (DEFERRED INFLOWS OF RESOURCES) to determine what, if anything, is left over (NET POSITION or FUND BALANCE) at a given point in time, usually the end of the FISCAL YEAR. Governments prepare up to four position statements (financial statements 1, 3, 5, and 8 from page 7).

Flows statements report the outflows of a government's resources for the fiscal year (expenses, EXPENDITURES, or cash DISBURSEMENTS) and the resources obtained (revenues or cash RECEIPTS). Governments prepare up to five flows statements (financial statements 2, 4, 6, 7, and 9).

By the numbers…major characteristics of the government-wide and fund financial statements

	Government Wide	Governmental Funds	Proprietary Funds	Fiduciary Funds
Scope	All activities of a government (except fiduciary), including governmental activities (governmental funds and internal service funds), BTAs (enterprise funds), and component units	Basic services of government, typically financed with taxes and grants; makes up most of governmental activities (with internal service funds)	Services that charge a fee to users; enterprise funds are basically the same as BTAs (internal service funds generally are governmental)	Established relationships in which a government minds (and may even manage) resources that belong to others and are not available to the government itself
Display Features	Information divided among governmental activities, BTAs, and discretely presented component units	"Major" funds shown individually; smaller governmental funds aggregated into a single column	"Major" enterprise funds shown individually; smaller enterprise funds and internal service funds aggregated into two columns	Funds aggregated into columns by category of fund
MFBA	Economic resources and accrual	Current financial resources and modified accrual	Economic resources and accrual	Economic resources and accrual
Financial Statements	Statement of net position	Balance sheet	Statement of net position	Statement of fiduciary net position Statement of changes in fiduciary net position

By the numbers…major characteristics of the government-wide and fund financial statements				
	Statement of activities	Statement of revenues, expenditures, and changes in fund balances	Statement of revenues, expenses, and changes in fund net position Statement of cash flows	

The Nature of the Information

In addition to differences in the breadth of scope of a government they cover, the government-wide statements and certain of the fund statements also measure a government's finances differently. (See **By the numbers…major characteristics of the government-wide and fund financial statements.**) The government-wide statements and the financial statements for the proprietary and fiduciary funds use an ECONOMIC RESOURCES measurement focus and an ACCRUAL basis of accounting (sometimes called FULL ACCRUAL). They present a comprehensive view of finances that contains all relevant assets, liabilities, deferred inflows and outflows of resources, revenues, and expenses. Under this MEASUREMENT FOCUS and BASIS OF ACCOUNTING (MFBA), a government records *all financial and capital resources* that flow in and out and all changes in net position, regardless of their form, as long as a monetary value can be placed on them. Therefore, governments need to track not only cash that changes hands, but also investments, inventory, equipment, buildings and other property, amounts owed to suppliers and employees, outstanding NOTES and bonds, long-term leases, and obligations for retirement benefits.

Furthermore, *all transactions and other events occurring during the year* and having an impact on a government's finances are reported in each year's financial statements, regardless of whether cash has changed hands. For example, goods and services provided are recorded regardless of whether cash was received in exchange from a customer or credit was extended to a customer. Similarly, purchases of office supplies are recorded whether paid for in cash or bought with a promise to pay later (by using a credit card or a business account).

The statements for the governmental funds employ a CURRENT FINANCIAL RESOURCES measurement focus and a MODIFIED ACCRUAL basis of accounting. This measurement focus concentrates on financial resources that are current in nature, meaning they are likely to be turned into cash or consumed in the short term. This typically includes cash, investments, ACCOUNTS RECEIVABLE, and ACCOUNTS PAYABLE. On the other hand, CAPITAL ASSETS, such as buildings and equipment, are *not* included.

The modified accrual basis of accounting focuses on expenditures rather than expenses. Expenses represent the using up of a resource in order to operate an organization and provide services; full

accrual, therefore, records a reduction in net position when a resource has been consumed or used. Expenditures under modified accrual, on the other hand, represent a payment or a requirement to pay for goods and services purchased and received in the course of operating and providing services. Consequently, modified accrual records a reduction in fund balance when a good or service has been delivered and payment normally is due.

The recording of revenues under the two accounting methods can be different as well. Under full accrual, revenues are recorded and net position increases when an inflow is *measurable* and *reasonably certain to be collected*. Under modified accrual, for an inflow to increase fund balance, the inflow has to be both measurable and *available*. "Measurable" relates to both full and modified accrual and means that one must be able to place an objective monetary value on the inflow. Availability is more conservative than the *reasonably-certain-to-be-collected* concept of full accrual. Under modified accrual, revenue is recognized only if payment *actually is received during the year or soon enough thereafter* to pay current-year liabilities. (See Example 6 in **Upon further review…similarities between the governmental funds MFBA and the MFBA for other statements.**)

Revenue availability

It is important at this juncture to give further consideration to revenue availability, which is peculiar to modified accrual accounting. The PERIOD OF AVAILABILITY specifies how long after the end of the year collected revenues are considered available to pay the current year's liabilities. Accounting standards stipulate a period of availability only for property taxes—up to 60 days—but no prescription is made for other revenue sources. Professional standards of government finance encourage that a consistent availability period be applied across all revenue sources. Governments are required to disclose their revenue accounting policies in notes to financial statements. (See the discussion of the SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (SSAP) in Part Three.)

Nonexchange transactions

Another important feature of governmental accounting is the NONEXCHANGE TRANSACTION. When transactions involve an equal exchange of value between two or more parties, the related revenues and expenses are recorded when they are *earned*. An inflow of cash or a promise to pay is recorded as revenue when a government has provided a good or performed a service in return (and has thereby earned the right to receive the resources). Similarly, an outflow of cash or a promise to pay is recorded as an expense if a government has received a good or service (and thereby a person or group has earned the right to the resources and the government is required to give them the resources).

Upon further review…similarities between the governmental funds MFBA and the MFBA for other statements

Example 1: A village hires a temporary secretary for a week. At the end of the week, the secretary departs without being paid yet. Under both MFBAs, an expense/expenditure for salaries is incurred, even though payment has not been made yet, because the secretary had rendered service to the village, which in turn is now obliged to pay. A liability, salaries payable, is increased, and net position/fund balance is reduced by the same amount.

Example 2: Golfers buy season passes to use the municipal golf course, paying cash at the city clerk's office. Under both MFBAs, this is revenue—net position/fund balance increases, and so does cash, an asset.

Example 3: Office Mart is having a sale on paper clips. A fire district purchases 1,000 boxes of them on account for $1 per box. The purchase is delivered on the last day of the year. Under both MFBAs, accounts payable increases by $1,000, as does the organization's inventory of paper clips. Net position is unaffected in the current year. As the paper clips are used up in future years, an expense will be recorded equal to the purchase price of the paper clips used—net position will decline and inventory will fall by that amount.

…differences between the governmental funds MFBA and the MFBA for other statements

Example 4: A township obtains a loan of $1 million.

Nongovernmental funds and government wide: Cash increases by $1 million, as does a liability called loan payable.

Governmental funds: The increase in cash is balanced by an increase in other financing sources (which increases fund balance), because a loan payable is a long-term liability. The precise fund in which this transaction is recorded depends on the intended use of the loan proceeds, but it is likely to be a capital projects fund.

Example 5: The township uses the loan proceeds to purchase a building.

Nongovernmental funds and government wide: Cash decreases and capital assets (fixed assets, property-plant-equipment, and so on) increase by $1 million. At the end of each fiscal period, a depreciation expense is recorded, reducing net position and causing a net reduction in capital assets. (See **Tools of the trade…inventory and capital asset expenses** on page 26.)

Governmental funds: Capital assets are not reported in the governmental funds. Consequently, while cash decreases, the building is not added; rather, fund balance in the capital projects fund is reduced as a $1 million expenditure is incurred. The entire purchase price is reflected as an expenditure immediately.

Example 6: The loan carries an interest rate of 5 percent. The first payment is due and made on the last day of the fiscal period, in the amount of $60,000. Of this amount, $50,000 is **INTEREST** ($1 million multiplied by 5 percent, or 0.05) and the remaining $10,000 repays a portion of the **PRINCIPAL**.

Nongovernmental funds and government wide: The payment of $60,000 reduces cash. Interest is an expense—you can consider it a charge for "renting" someone else's money. Therefore, net position declines by the $50,000 interest expense. Finally, the loan payable decreases by the $10,000 applied to repay principal.

Upon further review…differences between the governmental funds MFBA and the MFBA for other statements *(continued)*

Governmental funds: The payment of $60,000 reduces cash. The entire amount is treated as a **DEBT SERVICE** (principal plus interest) expenditure, reducing fund balance. Recall, there is no loan payable (a long-term liability) to reduce under this MFBA. This transaction likely would be recorded in a debt service fund. In that case, a separate transfer of cash from the general fund to the debt service fund might occur to cover the expenditure, unless the debt service fund had a revenue source of its own.

Example 7: A municipality works out an arrangement with a property owner in financial difficulty whereby her property tax bill for this year ($500) can be split in two—one-half paid now and the other half paid four months after the end of the fiscal year.

Nongovernmental funds and government wide: The $250 received immediately is recorded as revenue—cash and net position increase. In this MFBA, the other $250 also is recorded as revenue and is balanced by an increase in property taxes receivable rather than cash. When the cash is received in the next year, cash increases and the receivable is eliminated.

Governmental funds: The $250 received immediately is recorded as revenue—cash and fund balance increase. But then the issue of revenue *availability* comes into play. This more stringent burden of revenue recording requires that resources be available during or soon after the year. The period after the year during which different types of revenues are considered available may vary—for property taxes, it is required to be 60 days. Because the payment for the remaining $250 will not be received until 120 days into the next year, it cannot be considered available this year and, therefore, no revenue is recorded. Instead, a receivable is established and balanced with a deferred inflow of resources. When the payment is received, cash and fund balance increase (the revenue is recorded), and the receivable and deferred inflow are eliminated.

The requirement that revenues and expenses be earned does not extend to events and transactions in which an equal exchange of value *does not* take place. Such instances—called nonexchange transactions—are common for governments, especially on the revenue side. Taxes levied can be recorded as revenue but, as noted in Part One, it is not clear what goods and services taxpayers receive in return for specific tax payments, or what the value of those goods and services is. Governmental accounting standards identify four classes of nonexchange transactions; the classification affects when assets, liabilities, deferred inflows and outflows, revenues, and expenses/expenditures are recorded. (See **By the numbers…classes of nonexchange transactions.**)

By the numbers...classes of nonexchange transactions

Class of Nonexchange Transaction	Examples	Standards for Recording Transactions*	
		Full Accrual	**Modified Accrual**
DERIVED TAX REVENUES result from assessments imposed on EXCHANGE TRANSACTIONS.	Income taxes, sales taxes, and other assessments on earnings or consumption	Assets—when the underlying exchange transaction occurs (receivable) or resources are received (cash), whichever is first Revenue—when the exchange occurs	Assets—same as full accrual Revenues—when both the exchange occurs AND resources are available
IMPOSED NONEXCHANGE REVENUES result from assessments imposed on nongovernmental organizations and individuals, other than assessments on exchange transactions.	Property taxes, fines, penalties	Assets—when the government has an enforceable legal claim to the resources (receivable) or resources are received (cash), whichever is first Revenue—at the same time as the assets; however, if time requirements exist, in the period when use of the resources is required or first allowed	Assets—same as full accrual Revenue—when there is a legally enforceable claim AND resources are available; however, if time requirements exist, in the period when use of the resources is required or first allowed
A GOVERNMENT-MANDATED NONEXCHANGE TRANSACTION occurs when one government provides resources to another government and requires the recipient to use the resources for a specific purpose.	Federal aid to state and local governments for federally mandated programs	Assets (recipients) and liabilities (providers)—when all applicable eligibility requirements established by the provider are met (receivables/payables) or resources are received (cash), whichever is first Revenue (recipients) and expense (providers)—when all applicable eligibility or time requirements are met	Assets—same as full accrual Revenue—when eligibility and time requirements are met AND resources are available Expenditures—same as expenses
A VOLUNTARY NONEXCHANGE TRANSACTION results from legislative or contractual agreements, other than exchanges, entered into willingly by the parties to the agreement.	Unrestricted grants and donations		

*Resources received or recorded as receivable from derived tax revenues *prior to* the exchange transaction are reported as a liability by the recipient government.

When resources change hands in a government-mandated or voluntary nonexchange transaction *before eligibility requirements are met,* the provider government continues to report the resources as an asset and the recipient government reports a liability until the eligibility requirements have been met.

When resources change hands *in advance of time requirements being met, and no eligibility requirements remain,* the provider government reports a deferred outflow of resources and the recipient government reports a deferred inflow of resources until the time requirements have been met.

Two levels of statements, one complete picture

The government-wide and fund financial statements contain different kinds of information, but neither type of statement is preeminent. Because governments are held accountable for a much more complex set of goals than businesses, both types of statements are necessary for a government to demonstrate its accountability to the public and to its creditors. The government-wide and fund statements, together with notes to financial statements, provide much of the information that analysts and other users of financial statements need to assess whether a government has been accountable. The relative strengths of the fund financial statement information are its ability to provide a short-term view of the governmental fund activities, to inform questions of *budgetary and legal compliance,* to allow the tracking of *dedicated resources,* and to provide *useful details* behind the government-wide statements. The benefits of government-wide financial statement information are its *comprehensiveness* and *comparability*.

Budgetary and legal compliance. Governments often create specific funds for financial reporting purposes based on the structure of their budget or because of a law or special requirement. Those funds are established specifically to provide an accounting that can demonstrate a government's compliance with the budgetary and legal restrictions placed on its finances. For instance, a state law might require that all school districts provide a detailed report to the legislature regarding resources used to construct new school buildings. Each district might, therefore, establish a capital projects fund in which it would account for (1) the sources and amounts of the resources devoted to new school construction and (2) how those resources were used to provide new classroom space.

Dedicated revenue. Funds also are convenient for following the flow of individual sources of dedicated revenue. Assume, for instance, that a county government levies a real estate transaction tax equal to 1 percent of the sales price of houses. The state law enabling the government to levy and collect that tax stipulates that it must be used for hiring more police officers. The government might establish a special revenue fund to record the amount of the tax flowing into the government and the amount and purposes for which the resources subsequently flowed out. In so doing, the government can demonstrate that the resources were properly used. Another example might be a state government that levies a cigarette and liquor tax devoted to financing addiction and substance abuse services. A

special revenue fund could be established to track how much tax revenue is collected and the purposes for which these resources subsequently are used to support the state's expenditures.

Useful details. The fund-based statements provide detailed information that is important for understanding and interpreting the government-wide statements. For example, the flows of resources for paying the principal and interest on various kinds of debt can be examined in individual debt service funds. The government-wide statements do not provide such details; they contain only an aggregated interest expense amount and do not show the resource flows related to the principal repayment (because the principal payment reduces an outstanding liability, rather than affecting net position).

In a similar vein, obtaining resources and using them to purchase or construct capital assets can be accounted for and subsequently followed in capital projects funds because those funds (1) are segregated from the financial data related to other kinds of activities and (2) measure how current financial resources flow. By contrast, capital expenditures are not shown in the government-wide statements in the year the assets are acquired; rather, depreciation expense generally is used to spread the original cost of capital assets over their useful lives.

A comprehensive view. By covering the whole of a government, the government-wide statements are intended to provide an overall picture of the financial health of the government. All the resources a government has at its disposal are shown, including major capital assets such as bridges and buildings, as well as all the amounts a government owes, including municipal bonds and claims and judgments against a government. A thorough accounting of the cost of government services is rendered because the statements present all costs, not just how much cash was collected and disbursed.

Comparability. Fund structures differ from government to government—each government selects the number and kinds of funds that are appropriate to how it is organized, to the services it provides and how it provides and finances them, and to the laws and rules regulating its operations. The inherent flexibility of fund accounting is tremendously valuable in this way. The downside to that individuality is a lack of comparability across governments; unless you have an intimate knowledge of the funds of each government being compared, you run the risk of comparing apples to oranges. An important benefit of the consolidated presentation of the government-wide statements is that it removes the boundaries created by funds, making it possible to compare the finances of similar governments, at least in the aggregate.

Depending on the level of detail provided by a government, functional expense categories may be comparable across governments and perhaps individual services as well. The absence of a standard set of functions, however, means that the functions used by governments in their financial statements and the services included in each function may vary and, therefore, adversely affect comparability. Nonetheless, comparability is greater in the government-wide statements—at worst, it represents an improvement from apples-to-oranges to tangerines-to-oranges comparisons.

Distinguishing between the Parts of a Government

Both government-wide statements—the statement of net position and the statement of activities—divide the information they contain between the primary government and its discretely presented component units. Component units are organizations that are legally distinct from the government that created or acquired them, but for which the elected officials of the government are nonetheless financially accountable. Component units may have their own managers and governing boards, but the leaders of the parent government are accountable for them to some degree. Component units often take the form of a PUBLIC BENEFIT CORPORATION or PUBLIC AUTHORITY; common examples include housing authorities and port and transit authorities. This guide's sample local government, Local City, has two component units—the Local Public School District, which runs the elementary and secondary schools, and the Local City Landfill Authority, which operates municipal landfills. (Component units are discussed further in Part Twelve.)

The government-wide statements further distinguish between the primary government's governmental activities and BTAs. This distinction is made primarily because the governmental activities and BTAs are different—their operating styles and methods of financing often are quite unalike—and it is logical to separate their financial information.

Governmental activities are composed of the traditional services of government. They generally are not self-supporting but, rather, rely for their financing on taxes and other revenues levied generally on the public. In the absence of government provision, many might not occur in the private sector, or at least not in sufficient quantity to meet demand. Examples include police protection and firefighting for localities, mental health and courts for states, and general and special education for school districts.

BTAs charge a fee directly to the people or groups that use their services. These activities often try to set that fee high enough to cover their costs of operation, and sometimes high enough to generate a profit that can be reinvested in the activity or returned to the general government to finance other activities. BTAs tend not to place a burden on the public in the form of a need for financing from general taxes but, rather, may be net contributors to public resources. Common examples of BTAs are utilities and financing authorities.

➢ **WHAT'S AHEAD?**

➢ WHAT ARE NOTES AND WHY ARE THEY IN THE FINANCIAL REPORT?
➢ WHAT IS SUPPORTING INFORMATION? WHAT DOES IT DO?

NOTES TO FINANCIAL STATEMENTS

The information you find in the notes to a government's financial statements is as important to understanding a government's finances as the statements themselves. You might ask, if the

information is so important, why does it not appear in the financial statements? There generally are three reasons why information is reported in the notes rather than on the face of the financial statements.

First, some information appears in the notes because it is in narrative form. The information in the financial statements principally consists of numbers accompanied by text labels. If a government wants to provide a narrative explanation, it is easier to do so in the notes than it would be on the face of the financial statements. That is one of the primary purposes of notes—to provide explanations and background information. It often consists of describing the accounting methods a government utilizes or explaining circumstances surrounding financial statement information that are not apparent from the statements themselves.

Behind the numbers...selected note disclosure requirements

These two lists of note disclosures have been excerpted and adapted from the GASB's *Codification of Governmental Accounting and Financial Reporting Standards.*

Notes that are essential if the information in the financial statements is to be presented fairly, including:

a. Summary of significant accounting policies
b. Cash deposits with financial institutions
c. Investments
d. Significant contingent liabilities
e. Significant effects of events subsequent to the end of the year
f. Pension and OPEB liabilities
g. Significant violations of finance-related legal and contractual provisions
h. Future debt service requirements for currently outstanding debt
i. Leases
j. Construction and other significant commitments
k. Capital assets
l. Long-term liabilities
m. Deficit fund balance or net position of individual funds
n. Receivables and payables and transfers between funds
o. Significant transactions between discretely presented component units and with the primary government
p. Donor-restricted endowments.

Additional note disclosures that should be made if applicable to the government, including:

a. Risk management activities
b. Property taxes
c. Segment information for enterprise funds
d. Condensed financial statements for major discretely presented component units
e. Basis of accounting used in the budget, and budget-to-GAAP reporting differences not otherwise reconciled in the financial statements
f. Short-term debt instruments and liquidity
g. Transactions with related parties
h. The nature of the primary government's accountability for related organizations (organizations like component units, but for which a government is *not* financially accountable)
i. Joint ventures
j. Jointly governed organizations
k. Debt refundings and troubled debt restructurings
l. INTERFUND ELIMINATIONS in fund financial statements not apparent from headings
m. Pension and OPEB plans
n. Bond, tax, or revenue anticipation notes excluded from fund or current liabilities (proprietary funds)
o. Nature and amount of inconsistencies in financial statements caused by transactions between component units having different fiscal year-ends or changes in component unit fiscal year-ends
p. Special assessment debt
q. Reverse repurchase agreements and dollar reverse repurchase agreements
r. Securities lending transactions
s. Demand bonds
t. Landfill closure and postclosure care
u. Pollution remediation obligations
v. On-behalf payments for FRINGE BENEFITS and salaries (from a government to another organization for employees of the legally separate entity)
w. Involvement in conduit debt obligations

x. Sponsoring government disclosures about external investment pools reported as investment trust funds, and disclosures by participants in those pools
y. The amount of interest expense included in direct expenses
z. Nature of individual elements of a particular reconciling item, if obscured in the aggregated information in the summary reconciliation of the fund financial statements to the government-wide statements
aa. Discounts and allowances that reduce gross revenues, when not reported on the face of the financial statements
bb. Disaggregation of receivable and payable balances
cc. Impairment losses, idle impaired capital assets, and insurance recoveries, when not otherwise apparent from the face of the financial statements
dd. The amount of the primary government's net position at the end of the reporting period that is restricted by enabling legislation
ee. Termination benefits
ff. Future revenues that are pledged or sold
gg. Derivative instruments
hh. Conditions and events giving rise to substantial doubt about the government's ability to continue as a going concern
ii. Bankruptcy proceedings
jj. Stabilization arrangements and minimum fund balance policies
kk. Information about major special revenue funds
ll. Changes in the manner of or basis for presenting corresponding items for two or more periods in comparative financial statements
mm. Short-term obligations
nn. Prior-period adjustments, accounting changes, and error corrections
oo. Deferrals and their effects on net position
pp. Lending and mortgage banking activities
qq. Regulated BTAs
rr. Service concession arrangements
ss. Financial guarantees provided or received for little or no payment
tt. Government combinations and disposals of operations
uu. Fair value measurements
vv. Tax abatements
ww. Asset retirement obligations.

Second, some information appears in the notes because it is too detailed to be presented meaningfully in the financial statements. Governments try to strike a balance in the financial statements between providing the information you need and keeping the statements uncluttered and as easy as possible to read. In order to keep the statements from getting too dense and difficult to decipher, governments may present information in a more aggregated form in the financial statements but then provide a note with the detail underlying the financial statement numbers. For example, a government may include a single total amount for **RECEIVABLES** in the statement of net position but disclose in the notes the individual amounts of specific types of receivables, such as **TAXES RECEIVABLE**, **INTEREST RECEIVABLE**, and so on. (See Figures 10 and 11.)

Third, some information may not meet the criteria for being reported in the financial statements. To be communicated effectively in the statements, financial information has to be *understandable, reliable, relevant, timely, consistent,* and *comparable*. A particular piece of information may fall short on one or more of those characteristics and, therefore, not be eligible to be reported in the statements; yet, that information is so important to understanding a government's finances that it is nevertheless disclosed

in the notes. For instance, some amounts included in the statements are based on estimates that can be made with a degree of certainty from available information, even if the precise amounts are not known. However, as the circumstances upon which an estimate is founded become more uncertain, the reliability of the estimates may diminish to the point that they should not be included in the financial statements. A common example is **CONTINGENT LIABILITIES**. (See page 121.)

Some note disclosures are virtually all text, such as the SSAP. Many note disclosures are predominantly tables of numbers with some introductory or explanatory text. Other notes are a combination of narrative and numbers.

Keep in mind…"required/nonrequired" information

The accounting standards include comprehensive lists of the note disclosures that a government is required to present with its financial statements. (Refer to **Behind the numbers…selected note disclosure requirements**.) However, even if a government prepares every single one of those notes, it may not be fully in accordance with GAAP because the standards also caution that those lists are not all-inclusive. If a government's finance officers are aware of something important that, if omitted, would cause the financial statements to be misleading, they have to disclose it. Such information is not specifically identified in GAAP, but it is required to be disclosed nonetheless. Consequently, as you browse through the notes in a government's financial report, you may see some disclosures that are not described in this guide.

Another reason why a government might voluntarily include notes or supporting information is to satisfy continuing disclosure requirements. When governments issue debt, they typically prepare an "official statement" or prospectus for potential buyers containing the most recent audited financial statements and notes, as well as other relevant information. With few exceptions, the U.S. Securities and Exchange Commission (SEC) requires the underwriters of the debt to ensure that the information from that document continues to be updated and available until the debt has been completely repaid. Many of the required parts of a government's financial report satisfy continuing disclosure requirements, but you also may see other information in the notes, statistical section, or elsewhere in the financial report that has been included as a part of continuing disclosure. This guide references some commonly provided information related to continuing disclosures but, for the most part, it is strictly limited to describing only the notes and supporting information that are set forth in the accounting standards.

SUPPORTING INFORMATION

A government's financial report also contains **SUPPORTING INFORMATION**. Governments are *required* by the accounting standards to present certain supporting information (that is, RSI), while other supporting information is not required, but a government may present it *voluntarily* (**SUPPLEMENTARY INFORMATION** or **SI**). Supporting information (both RSI and SI) is important for interpreting and understanding what the financial statements and notes have to say about the condition of a government's finances. Supporting information is important for understanding the information in the financial statements and notes because it places that information in context. RSI is considered *essential* to providing context for the statements and notes; therefore, governments are *required* to present it.

If a government publishes a CAFR, it presents SI that includes prefatory information in the introductory section, detailed COMBINING FINANCIAL STATEMENTS following the RSI in the financial section, and information for the last 10 years in the statistical section. Governments also may provide other SI that is not specified in the governmental accounting standards, but which they believe is important for providing context for the readers of their financial statements, such as schedules of capital asset information.

Keep in mind...differences in auditing notes and supporting information

The auditor performing the financial audit of a government's financial report examines the notes to financial statements as closely as the financial statements themselves. You should be cognizant, however, that a different and less stringent form of audit is applied to RSI. An auditor's association with RSI does not approach the depth of examination applied to the basic financial statements, including the notes. Rather, the major aspects of an auditor's approach to RSI are as follows:

- After first determining that the government has prepared the RSI it is required to include, the auditor inquires of management about the methods used to prepare the information. This inquiry should cover whether the information is measured and presented within prescribed guidelines, if and why methods have changed since the previous year, and any significant assumptions underlying the information.
- The auditor checks that the information is consistent with the government's responses to this inquiry, with the audited financial statements, and with other knowledge obtained during the examination of the statements.
- The auditor applies additional procedures, if any, that are prescribed for specific types of RSI.

The SI generally is not included within the scope of the audit; the AUDITOR'S REPORT (see Figure E-1 in Appendix E) should identify which parts of the financial report are covered. Not even the limited procedures applied to RSI are replicated for SI. Rather, the auditor reviews the SI contained in the financial report for consistency with the audited financial statements, without attempting to verify its accuracy or to ascertain how it was prepared (unless the auditor is specifically engaged to audit and report on SI, but comparatively few governments do so).

The financial statements and notes certainly can be interpreted on their own. However, the information they contain becomes more meaningful when it is viewed with a basic understanding of a government's particular circumstances. For instance, if you want to learn about the cost of the various public services a government provides, your examination of expense information would be greatly aided if you understood how the government is organized, what kinds of services it provides, how those services are paid for, and how much of those services it provides. Those kinds of issues are addressed by some of the SI you can find in the introductory and statistical sections of a CAFR.

If you want to assess aspects of a government's financial health—such as its capacity to raise additional taxes or issue more LONG-TERM DEBT—it is very important to understand the economy and population of the jurisdiction in which the government resides. Consider two governments that present very similar financial information in their statements and notes. One government is in an area with a robust, growing economy—unemployment is low, personal income is rising, and so on. The other government has a weak economy and a population with significant needs for public services—illnesses are more common, families are less affluent, the school-age population is large and growing rapidly. Although these two governments have very similar financial reports, you likely would conclude that,

all other things being equal, the government with the healthier economy and fewer spending pressures is better able to afford more borrowing or raise more revenue. Supporting information about economics and demographics can be found in the statistical section.

No matter what questions you are trying to answer about a government, historical perspective is crucial. If you were trying to determine the affordability of a government's outstanding debt, you might divide total long-term debt by population or real estate values. How would you determine if the resulting number was high, low, or somewhere in between? One way to find out would be to examine how that number has changed over time. How does it compare with last year, 5 years ago, 10 years ago? The information presented in MD&A focuses on how a government's finances have changed since the previous year or over the course of the year. RSI about pensions covers a period of 10 years. Almost all the schedules in the statistical section contain information for the past 10 years.

Tools of the trade…inventory and capital asset expenses

Expenses represent the using up of an asset or incurrence of a liability while operating a government and providing goods and services. For instance, a sanitation department's annual expense for garbage bags equals the total cost of the garbage bags used during the year. The department determines this figure by comparing the inventory of garbage bags at the beginning and end of the year, adjusted for additional purchases of garbage bags during the year. Consider a department that had 100 cases of garbage bags on hand at the start of the year, bought 20 cases more during the year, and had 50 cases left at the end of the year:

Beginning inventory + purchases − amount used during year = ending inventory

or

Beginning inventory + purchases − ending inventory = amount used during year

100 + 20 − 50 = 70

If the cost per case of garbage bags was $100, the garbage bags expense for the year equaled $100 times 70 cases, or $7,000.

Capital assets are not "used up" in the same way inventory is, though. Most people probably would be disconcerted to hear that some portion of the bridge they cross every day had been "consumed." Governments approximate the using-up concept by spreading the purchase or construction price of their long-lived assets over the number of years those assets are expected to be used (their **USEFUL LIFE**), often in equal amounts. This produces an annual depreciation expense that theoretically represents each year's cost for consuming a portion of the asset's usefulness for providing services (its **SERVICE UTILITY**).

For example, a public electric utility buys some transformers for $1 million. The transformers are expected to last 10 years, at which time they will have a residual or **SALVAGE VALUE** of $10,000 (meaning, that is what the government might receive if it sold the transformers at the end of their useful lives).

depreciation expense = (purchase price – salvage value) ÷ useful life

(1,000,000 – 10,000) ÷ 10 = 99,000

In each of those 10 years, the utility's statement of activities would include a $99,000 charge called *depreciation expense.*

GOVERNMENTAL ACTIVITIES are activities that generally are financed with taxes and intergovernmental aid and typically are reported in the governmental funds

BUSINESS-TYPE ACTIVITIES are activities that primarily are financed with charges for goods and services and typically are reported in the enterprise funds

a **PRIMARY GOVERNMENT** comprises governmental activities and BTAs, as well as component units that are so inextricably linked with the governmental activities and BTAs that they are aggregated with them

DISCRETELY PRESENTED COMPONENT UNITS are legally separate entities for which a government is financially accountable and that are reported separately from the governmental activities and BTAs in the government-wide financial statements

GOVERNMENTAL FUNDS account for the basic activities of a government

PROPRIETARY FUNDS account for activities that operate by charging a fee to service recipients

FIDUCIARY FUNDS account for resources that a government is minding on behalf of others and which do not belong to the government

CAPITAL ASSETS are assets that can be used to provide services for more than one year, such as buildings, equipment, and roads

NONEXCHANGE TRANSACTIONS are common governmental transactions in which there is no equal exchange of resources, or one or more parties involved is an unwilling participant

Upon further review…can two different MFBAs share a financial report?

An important benefit of the governmental funds MFBA is that it provides more detailed information than the government-wide MFBA for assessing how well a government manages its short-term resources. One of the objectives of financial reporting is to demonstrate a capacity to manage day-to-day finances. The current-period focus of the governmental funds, and the fact that those funds track most of the day-to-day, basic services of government, combine to offer data that can help you assess the fiscal management skills of the government's finance officials. That aim is further aided by the fact that this MFBA, which is used for external reporting, is very similar to (if not precisely the same as) the measure that many governments use internally to manage their finances and to budget.

The government-wide statements (and those of the proprietary and fiduciary funds) use the economic resources measurement focus and accrual basis of accounting. The use of this MFBA gives the statements features not available in the governmental funds statements. The government-wide statements offer both a short- and long-range view of finances because they contain both current and long-term resources. They report the complete economic impact of a government's operations, not just those transactions in which cash was exchanged during the year or shortly thereafter. The inclusion of all resources and all of a government's transactions leads to data about the full cost of services that cannot be derived from the governmental funds statements.

SUPPORTING INFORMATION makes the information in financial statements and notes more understandable by placing it in context

SUPPLEMENTARY INFORMATION is voluntarily provided supporting information

PART THREE

INTRODUCTORY AND BACKGROUND INFORMATION

Sometimes the best way to learn a new subject or skill is simply to jump feet-first into the deep end of the pool and start treading water. This method is not recommended when it comes to using a government's annual financial report. Instead, a government's financial report contains introductory and background information to familiarize you with the government, to guide you through the various parts of the financial report, to explain what certain information means and how it was developed, and to help you use the information in the report more ably. Such information can be found in the introductory section of a CAFR, in MD&A, and in the SSAP note disclosure.

WHAT'S AHEAD?

- HOW IS A GOVERNMENT ORGANIZED AND WHO IS IN CHARGE?
- DO THE FINANCIAL STATEMENTS CONFORM TO ACCOUNTING STANDARDS?

INTRODUCTORY SECTION

The introductory section of a CAFR is unaudited SI. That is, it is provided voluntarily by a government, and only if the government presents its financial statements in a CAFR. As the name suggests, it is the first part of the CAFR, introducing you to the government itself—how it is structured, how it operates, what services it provides, and so on. This kind of information is valuable for understanding the environment in which a government's financial activity—as reported in the financial statements, notes, and RSI—took place. It also is important for understanding the context of the other SI a government may present, such as combining financial statements and the statistical section.

The standards established by the GASB and its predecessors govern how and what information a government includes in its financial reports but specify very little about the contents of an introductory section, other than a table of contents, LETTER OF TRANSMITTAL, and other items the government considers appropriate. Nonetheless, because of guidelines issued by professional associations such as the Government Finance Officers Association (GFOA) and the Association of School Business Officials International (ASBOI), the contents are fairly consistent from government to government. A government's introductory section is likely to include the following, often in this general order:

- Title page
- Table of contents
- Letter of transmittal
- Financial report award, if applicable
- List of principal officials

- Organizational chart
- Audit committee letter.

Letter of Transmittal

The letter of transmittal is addressed to you, the reader of the CAFR, from the government's chief financial officer and sometimes its chief executive or operating officer, such as the mayor or city manager. Its principal purpose is to formally *transmit* the CAFR to you by explaining why it has been prepared (perhaps the government is legally required to do so) and by describing the controls that the government uses to ensure the accuracy of its financial information. The letter of transmittal acknowledges that *the management of the government is responsible for the contents of the financial report.* In other words, even though the auditor, audit committee, or others may be involved in the preparation of the financial report, it is nevertheless *the government's* financial report.

The GFOA, through its publication *Governmental Accounting, Auditing, and Financial Reporting,* suggests several types of information that a government should consider including in its letter of transmittal. For instance, the letter of transmittal may contain a profile of the government that briefly describes how it is organized, the types of services it provides, its history, and the population it serves. This profile also may explain in broad terms the government's budgetary process and practices. If a government has received an award for its CAFR or other external recognition of its financial and managerial practices, it may identify those as well.

A government's letter of transmittal also may include other information that it believes would be helpful to you in assessing the government's financial health. The letter of transmittal may refer to information elsewhere in the financial report but should not be duplicative. Rather, the letter of transmittal tends to include information that is more subjective in nature and, therefore, not appropriate to be included in the other sections of the CAFR. The GFOA identifies examples of pertinent issues that a government might address, such as the state of the local economy, pensions and other benefits promised to employees and retirees of the government, and its financial management practices, including long-term planning, capital investment strategies, and management of cash and investments.

Financial Report Awards

The GFOA, ASBOI, and some state organizations conduct programs to encourage and recognize excellence in financial reporting. Governments submit their CAFRs to these programs, which review the reports to determine if they meet a lengthy list of requirements for content and presentation. Governments that receive a Certificate of Achievement for Excellence in Financial Reporting (GFOA), a Certificate of Excellence in Financial Reporting (ASBOI), or a state award often include a facsimile of the certificate in their introductory section. They do so to make you aware of their achievement and to acknowledge a certain level of financial management competence on their part.

Governments also frequently mention how many times they have won a certificate or the number of years in a row they have been recognized.

Principal Officials and Organizational Chart

Who is in charge in the government? The introductory section presents a list of the major elected and appointed officials of the government. This list sometimes is combined with an organizational chart, which may show the departments, agencies, or divisions of the government, how responsibilities for services and operations are apportioned among them, and the lines of responsibility and accountability. The principal officials alternatively may be found on the title page.

Audit Committee Letter

A government's audit committee, if it has one, is composed of persons knowledgeable about accounting, financial reporting, and auditing, who serve in an advisory capacity to a government. It oversees the process of auditing the government's financial report, fosters communication between the government and its independent auditor, and helps to resolve any issues that are raised during the audit; audit committees usually select the auditor, as well. If a government presents its audit committee letter in the financial report, it generally will appear in the introductory section of the CAFR.

AUDITOR'S REPORT

- The auditor's report is a letter attached to the front of the financial statements reflecting the results of an audit of the statements in accordance with the applicable auditing standards established by the AICPA and the U.S. Government Accountability Office (GAO). Essentially, the auditor—either a CPA firm or state government auditor—determines whether a government's financial statements are presented fairly in accordance with GAAP. (See Figure E-1 in Appendix E.) The language generally is the same in all auditors' reports, unless (1) the scope of the audit is limited to less than a government's entire REPORTING ENTITY, (2) the auditor has found that the statements are not presented in accordance with GAAP, or (3) the RSI is not consistent with the GASB requirements. If the auditor has identified a significant problem, you should be aware of it before reading the statements. There generally are four kinds of reports:
- "Unqualified" opinion—the auditor finds the financial statements present a government's finances fairly in accordance with GAAP; sometimes called a "clean" opinion.
- "Qualified" opinion—there is a departure from GAAP in the financial statements, such as a component unit or other part of the government that does not follow GAAP, or an omission of capital asset information from the government-wide financial statements. A qualified opinion also might stem from a portion of the government being excluded from the audit (a "scope limitation") or from a government's inability to provide sufficient evidence to support some information in the financial statements or notes.

- "Adverse" opinion—the financial statements *do not* present a govern-ment's finances fairly in accordance with GAAP.
- "Disclaimer" of opinion—the auditor is unable to express an opinion on one or more parts of the financial statements (or the financial statements in their entirety). The auditor's report should explain why the auditor could not express an opinion.

The audit opinion speaks to whether the financial statements (including the notes) present a government's finances fairly, but the opinion does not encompass RSI. Auditors conduct "certain limited procedures" regarding RSI, such as checking that RSI agrees with the information presented in the statements and notes and inquiring about how the RSI was assembled by the government. The auditor's report should note if any RSI is missing, but a government can get a clean opinion even if it presents none of the RSI. (Refer to **Keep in mind…differences in auditing notes and supporting information** on page 24.)

You also should be mindful that the auditor's report is not an opinion on the financial *health* of a government. A government in poor financial shape can receive a clean opinion, just as a government in good condition can get an adverse opinion, because the auditor is reviewing whether the government followed the standards of accounting and reporting, not whether it had favorable financial results.

WHAT'S AHEAD?

- WHAT HELP IS PROVIDED IN USING A GOVERNMENT'S FINANCIAL REPORT KNOWLEDGEABLY?
- HOW CAN YOU GET AN OVERALL SENSE OF A GOVERNMENT'S FINANCIAL HEALTH AND LEARN ABOUT SIGNIFICANT FINANCIAL ISSUES?

MANAGEMENT'S DISCUSSION AND ANALYSIS

MD&A is the only RSI that precedes the financial statements. (All other RSI follows the notes to financial statements.) MD&A is prepared by the finance officials of a government and is intended to be a readable, objective analysis of the government's financial activity during the year. MD&A serves multiple purposes:

- It introduces you to a government's financial statements and provides a framework and context for understanding the information they contain. Upon reading MD&A, you should be better prepared to understand the information in the statements.
- MD&A also gives finance officials the opportunity to highlight issues they believe are important to you and other financial statement users and which you might otherwise miss when examining the statements unaided.

One thing MD&A is *not* intended to do, however, is take the place of your own review and analysis of the financial statements. Rather, it is meant to direct your attention to important occurrences during the period covered by the statements and to offer the benefit of the uniquely informed opinions of the government's finance officers. MD&A not only can answer some of your most basic questions about a government's finances, it can prepare you to ask more knowledgeable questions and to find the answers in the statements.

Be aware, though, that MD&A, the financial statements, and other information presented with the statements are designed and prepared with a knowledgeable user in mind. They require some prior familiarity with financial statements and governmental accounting and a willingness to take the time necessary to understand the statements.

MD&A is distinctly different from the letter of transmittal, even though both are narrative sections, are written by a government's finance officers, cover some similar topics, and precede the financial statements. There are three important distinctions. First, MD&A is required to be *objective,* whereas the letter of transmittal may contain subjective assessments and assertions. Second, the auditor applies certain limited procedures to MD&A, as mentioned earlier, but does not do so to the letter of transmittal. Third, MD&A is required to address a very specific list of topics; governments should not add any information to MD&A that is not relevant to one of those topics. The letter of transmittal is not governed by any such limitation.

MD&A covers five topics:

- Descriptive information about a government's financial statements (identified in Appendix A with a ①)
- An analysis of the financial information in the statements (②)
- Activities during the year regarding capital assets and long-term debts (③)
- Physical condition of infrastructure and efforts to maintain it, if the government employs the modified approach (④), and
- Currently known facts bearing on the future finances of the government (⑤).

Starting with the Basics

MD&A begins with an introduction to the individual financial statements that follow, similar to section ① on pages A-1 to A-4 of Appendix A. This overview covers the functions of the statements and the types of information they contain. MD&A also discusses how the financial statements relate to one another. This entails explaining the differences between the information presented in the government-wide and fund-based statements, as well as the ways in which the information is connected.

Revealing What the Financial Information Means

One of MD&A's clearest benefits to you is its potential for insightful and knowledgeable commentary about a government's finances. No one is more intimately aware of a government's financial status than its own finance officers, and these officials are responsible for preparing MD&A. This part of MD&A (section ②, pages A-4 to A-10) presents summarized information from the financial statements and an overview of what the information says about the government's finances. The information is accompanied by the finance officers' explanations of significant changes from the previous year.

The FINANCIAL ANALYSIS in MD&A covers a government's BFS, beginning with its overall FINANCIAL POSITION and how it changed during the year. (Financial position and financial analysis are explained in Parts Four and Fourteen, respectively.) The section beginning on page A-4 discussing net position as of the end of 2017 addresses financial position and includes a table (Table A-1) summarizing information from the statement of net position. Data are presented for 2017, the primary year of concern in these statements, and for 2016, the immediately prior year. By doing so, MD&A gives you a sense of not only where a government stands right now but also how that status has changed. Overall net position of Local City (the government addressed in the sample MD&A) was virtually unchanged, but the text of the sample MD&A explains that financial position was very different for the governmental activities and BTAs.

MD&A also explains major factors leading to the financial position reported in the statements. The sample MD&A discusses flows of resources under the heading "changes in net position." This section describes a government's revenues and expenses, and other changes that affected net position and, therefore, financial position. (See Table A-2 and Figures A-3 and A-4.) The section approaches this information separately for governmental activities and BTAs because the results of each were noticeably different. Appropriate explanations are included here as well. This part of MD&A also provides statement of activities information about the NET COST of government services. (See page A-8 and Table A-3. Net cost is explained in Part Seven.)

In addition to an analysis of the overall financial health of a government, MD&A analyzes and explains significant changes that occurred during the year in:

- The individual funds of a government; MD&A also identifies any significant restrictions imposed on the balances of a government's funds (see page A-9); and
- The operating budgets for the general fund and major special revenue funds (see page A-10).

Capital Assets and Long-Term Debt

MD&A describes briefly what happened during the year to capital assets and long-term debt (see section ③ on pages A-10 and A-11), including summarized information about:

- The general types of capital assets a government owns, the total dollar amount of each type, and how that amount changed from the previous year (Table A-4 on page A-11)
- Significant commitments a government has made to construct or acquire capital assets in the future. (The sample MD&A cites a major highway reconstruction project and a community housing program.)

MD&A's long-term debt information includes:

- Amounts and general types of debt owed at the end of the year, and how they changed from the prior year (Table A-5 on page A-13)
- Significant amounts borrowed during the year and significant repayments of debt
- Major events or circumstances that affect the amount and cost of debt a government may incur, such as changes in its CREDIT RATING or laws restricting the total amount it is allowed to owe at any given time.

The Condition of Capital Assets

Governments that follow the "modified" approach to reporting some or all of their infrastructure assets present RSI pertaining to the physical condition of infrastructure and their efforts to maintain it. (The MODIFIED APPROACH and the related RSI are described in Part Six.) These governments also discuss the infrastructure information in MD&A. Pages A-11 to A-12 (section ④) contain a discussion of the modified approach, which Local City uses to report its roads. This section briefly explains the concepts of the modified approach and the system the government uses to evaluate road conditions. It then summarizes the data the government is required to disclose in RSI. In this case, two bar charts are used to show how road conditions have changed (Figure A-5 on page A-12) and how much it cost to preserve and maintain the roads (Figure A-6 on page A-12).

Currently Known Facts Bearing on the Future

MD&A concludes with a discussion of any circumstances of which the finance officers are aware, at the time the financial statements are prepared and audited, that are likely to have a significant impact on the government's finances in the future. (See section ⑤ starting on page A-13.) For instance, municipal tax rates may have changed since the previous year, or perhaps a limit was placed on the amount of taxes a school district may levy by a state law or voter referendum. Another example might be a large local employer's announcement of plans to move out of a county, taking with it a substantial amount of tax revenue—both from the company and from the employees who will have to relocate. On the other hand, a government might have reached an economic incentive deal with a major corporation that is expected to bring a large number of new jobs to the economy.

No such dramatic changes are identified in the sample MD&A. (The presumption should be that none occurred, or that the finance officials were unaware of any.) The discussion in this section points out

the major economic factors Local City considered in its projections of future finances (as embodied by its budget for the following year). The sample MD&A also mentions labor agreements Local City signed with several employee groups and rate increases that will go into effect in its BTAs.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The first note disclosure following the financial statements usually is the SSAP, which identifies procedures and assumptions employed by a government when preparing its financial statements. (Figure E-2 in Appendix E is an example.) The information that is or is not included in the financial statements is determined by the methods used to record financial information and to prepare the financial statements.

This note is particularly valuable when the accounting standards give governments a choice between two or more approaches—the note explains which option a government has selected. For example, governments may select between two or more options for inventory accounting and depreciation methods, as well as many others.

Most of the required SSAP disclosures are discussed throughout this guide. **By the numbers…selected disclosures in the SSAP** lists some of the topics that are included in this note.

Keep in mind…the illustrative MD&A

A sample MD&A based on the illustrative local government financial statements in this guide can be found in Appendix A. It is provided for your reference as you proceed through the description of MD&A in this section. You also are encouraged to read through it as a whole, because it offers an example of how one might assess a complete set of government financial statements.

Rather than a representative illustration of a typical MD&A, the sample MD&A is an example of how one might be organized by a local government. The format of MD&A may develop in different ways for different types of governments, in order to meet their particular needs and circumstances. Governments have the flexibility to design their MD&A in the way they believe best meets the needs of their constituents, as long as it meets the information requirements of the prevailing accounting standards. The sample MD&A should be viewed as an example of what *could* be done, rather than what is *required* to be done.

Upon further review…how many years should MD&A cover?

In most cases, a government's MD&A contains information for two years—the year covered by the financial statements and the year immediately prior. However, if a government presents COMPARATIVE FINANCIAL STATEMENTS in its financial report, its MD&A includes *three* years of information—the two years covered by the comparative financial statements and the year immediately prior. If a government's comparative financial statements covered 2016 and 2017, its MD&A would cover *2015*, 2016, and 2017.

By the numbers…selected disclosures in the summary of significant accounting policies

- Description of government-wide statements, noting exclusion of fiduciary activities (indicated with a ① in Figure E-2)
- Policy for eliminating internal activity in the government-wide statement of activities ②
- Description of types of transactions included in program revenues and policy for allocating indirect expenses to functions in the statement of activities (if applicable) ③, and activities associated with operating revenues and expenses in the proprietary funds ④
- Measurement focus and basis of accounting used in the government-wide ⑤ and fund financial statements ⑥

- Government's policy regarding whether first to use restricted or unrestricted resources when an expense is incurred for purposes for which both restricted net position and unrestricted net position are available ⑦
- Definition of cash and cash equivalents used in the statement of cash flows ⑧
- Policy for capitalizing assets and for estimating the useful lives of those assets (used to calculate depreciation expense), and description of modified approach, if used. ⑨

PART FOUR

GOVERNMENT-WIDE STATEMENT OF NET POSITION

The statement of net position reports what a government owns (assets) and owes (liabilities) at a given point in time, usually the last day of the fiscal year. The bottom line of the statement of net position—net position—represents the resources remaining for the government to use after the liabilities have been paid off or otherwise satisfied. Net position is not merely the difference between assets and liabilities, however. It also encompasses items called deferred outflows of resources and deferred inflows of resources, which are neither assets nor liabilities, but which still affect a government's net position.

The statement is designed to display the equation for deriving net position (the **ACCOUNTING EQUATION**): *assets plus deferred outflows minus liabilities minus deferred inflows equals net position*. (Alternatively, a government may arrange the elements in a balance sheet format: *assets plus deferred outflows equals liabilities plus deferred inflows plus net position*.) Therefore, the statement lists assets first, followed by deferred outflows, liabilities, deferred inflows, and finally net position. (See Figures 1, B-1, and C-1 for illustrative statements of net position for a local government, state government, and school district, respectively.)

Figure 1: As of December 31, 2017, Local City had assets totaling $438,577,188, deferred inflows of $24,806,668, liabilities of $334,365,555, deferred outflows of $12,193,093, and total net position of $116,825,208.

The statement of net position shows assets and liabilities in order of their relative **LIQUIDITY** and **MATURITY**, respectively. The statement begins with the assets most easily converted to cash or consumed most quickly and the liabilities that are expected to be satisfied soonest, proceeding to the least liquid assets and the liabilities due latest. This is the approach recommended in the accounting standards, although some governments employ the optional **CLASSIFIED FORMAT**, which divides the assets and liabilities between current and noncurrent and provides separate subtotals for each. (Figures 1 and B-1 are in the classified format; Figure C-1 is not.) The classified format can be helpful for certain kinds of analyses (financial ratios will be discussed later). For example, if you want to assess a government's short-term financial needs, you may focus only on its most immediately available resources.

Figure 1. Government-Wide Statement of Net Position

Local City
Statement of Net Position
As of December 31, 2017

	Primary Government			⑨
	Governmental Activities	Type Activities	Total	Component Units
ASSETS				
Current assets:				
Cash and cash equivalents ①	$ 13,597,899	$ 10,221,420	$ 23,819,319	$ 303,935
Investments	27,365,221	47,596,245	74,961,466	7,428,952
Receivables, net	11,118,035	3,568,121	14,686,156	4,042,290
Due from other governments	1,714,097	41,494	1,755,591	—
Internal balances	175,000	(175,000)	—	—
Inventories	322,149	126,674	448,823	83,697
Total current assets	54,292,401	61,378,954	115,671,355	11,858,874
Noncurrent assets:				
Restricted cash and cash equivalents	—	1,493,322	1,493,322	—
Capital assets (Note 2): ②				
Land and nondepreciable infrastructure	89,333,120	3,836,119	93,169,239	—
Depreciable infrastructure, net	29,787,241	30,952,214	60,739,455	751,239
Buildings, property, and equipment, net ③ ⑤	50,903,399	116,600,418	167,503,817	36,993,547
Total noncurrent assets	170,023,760	152,882,073	322,905,833	37,744,786
Total assets	224,316,161	214,261,027	438,577,188	49,603,660 → +
DEFERRED OUTFLOWS OF RESOURCES				
Pensions	8,365,521	4,999,868	13,365,389	1,488,110
Retiree health insurance ④	6,686,417	2,999,966	9,686,383	892,866
Accumulated decrease in fair value of hedging derivatives	1,754,896	—	1,754,896	2,987,635
Total deferred outflows of resources	16,806,834	7,999,835	24,806,668	5,368,611 → +
LIABILITIES				
Current liabilities:				
Accounts payable	7,102,607	751,430	7,854,037	4,790,967
Advances on grants ⑥	1,435,599	—	1,435,599	—
Portion of long-term obligations due within one year (Note 3)	9,236,000	4,426,286	13,662,286	1,426,639
Total current liabilities	17,774,206	5,177,716	22,951,922	6,217,606
Noncurrent liabilities:				
Portion of long-term obligations due after one year (Note 3)	183,598,630	127,815,003	311,413,633	42,979,322
Total liabilities	201,372,836	132,992,719	334,365,555	49,196,928 → −
DEFERRED INFLOWS OF RESOURCES				
Pensions	3,903,910	2,333,272	6,237,182	694,451
Retiree health insurance ④	3,120,328	1,399,984	4,520,312	416,671
Service concession arrangement proceeds	—	1,435,599	1,435,599	—
Total deferred inflows of resources	7,024,238	5,168,855	12,193,093	1,111,122 → −
NET POSITION				
Net investment in capital assets	103,711,386	73,088,574	176,799,960	15,906,392
Restricted for:				
Capital projects	11,705,864	—	11,705,864	492,445
Debt service	3,020,708	1,451,996	4,472,704	—
Community development projects	4,811,043	—	4,811,043	—
Other purposes ⑦	3,214,302	—	3,214,302	—
Unrestricted (deficit)	(93,737,382)	9,558,717	(84,178,665)	(11,734,616)
Total net position ⑧	$ 32,725,921	$ 84,099,287	$ 116,825,208	$ 4,664,221 ← =

Figure 1 Notes

① Governments are encouraged to list assets and liabilities in order of their relative liquidity or maturity, respectively, although they are allowed to list current and noncurrent assets and liabilities separately (the classified format). Assets are presented in order of how readily they can be converted to cash; cash is the most liquid, capital assets the least. Liabilities are shown in order of when they are expected to be paid off or otherwise satisfied.

② The capital assets note includes the beginning and ending balances of major classes of capital assets and their related accumulated depreciation, and how they changed during the year. (See Figure 12.)

③ Most capital assets are shown at their original purchase/construction cost, less annual depreciation charges accumulated over time, except for land, construction in progress, and infrastructure reported with the modified approach, which are not depreciated. Local City uses the modified approach to report its roads and, therefore, does not depreciate them. (See Figures 12 and 32.)

④ Certain parts of the annual increase or decrease in the pension and other postemployment benefit liabilities are initially reported as deferrals before being reported as expense. The amounts shown here are disaggregated in the notes to its financial statements. (See Figure 25 and **Upon further review…level of detail for reporting deferrals** on page 43.)

⑤ Accumulated depreciation already is subtracted from historical cost (hence the word "net"); if a government does not show the amount of accumulated depreciation here, it will disclose it in the notes.

⑥ This note discloses details about major types of long-term liabilities. (See Figure 16.)

⑦ Governmental activities have no unrestricted net position because those activities owe more than they own. This fact is discernible because governments separate governmental activities from BTAs in this statement.

⑧ Total assets + deferred outflows − total liabilities − deferred inflows = total net position ($224,316,161 + 16,806,834 – 201,372,836 – 7,024,238 = $32,725,921).

⑨ See the discussion of component units beginning on page 281.

WHAT'S AHEAD?

- WHAT DOES A GOVERNMENT OWN?
- WHAT IS THE VALUE OF A GOVERNMENT'S CAPITAL ASSETS?

ASSETS

Among the **CURRENT ASSETS**, cash is the most liquid asset (as it is already cash). Investments such as certificates of deposit, U.S. Treasury notes, and bonds can be readily sold or cashed in. Accounts receivable may take longer to liquidate than investments, but cash payments from a government's debtors typically will be received more quickly than a government will use up its inventory.

Figure 1: Local City had total current assets of $115,671,355 and total noncurrent assets of $322,905,833.

The largest asset amounts for most governments are **NONCURRENT ASSETS**, predominantly their long-lived capital assets, such as land, buildings, and equipment. When a government purchases, constructs, or substantially renovates a capital asset, typically the original or **HISTORICAL COST** of the asset is added to the government's capital asset accounts rather than being reported as expense right away. This is called "capitalization." Governments report the historical cost as expense by spreading it over the estimated useful life of the capital assets; the annual expense is called depreciation. The most common form of depreciation is the "straight-line" method, which spreads depreciable value (original cost minus salvage value) equally among each year of an asset's useful life. For example, if a capital asset costs $10,000, has a salvage value of $1,000, and is expected to last 10 years, the annual depreciation expense in each of those 10 years is $900: ($10,000 – 1,000) ÷ 10. (Refer to **Tools of the trade...inventory and capital asset expenses** on page 26.)

The capital assets are shown in the statement of net position, then, at their historical cost less depreciation that has accumulated over time. The **ACCUMULATED DEPRECIATION** sometimes is shown separately from historical cost, or *net* amounts are shown—historical cost with the accumulated depreciation already subtracted (as in Figure 1).

One exception to this general approach is land used in operations, which always is shown on the statement at its original purchase price and is not depreciated over time because it generally is not considered to have a finite useful life over which the acquisition cost could be divided. Another exception is construction in progress—the historical cost of capital projects not yet completed. Conceptually, the useful life over which depreciation is spread does not commence until the asset is put into use; therefore, depreciation does not take place prior to that time.

A third exception may be infrastructure assets, such as bridges and roads. A government may report some or all of its infrastructure using the modified approach. Under the modified approach, infrastructure assets are capitalized but are not depreciated. Rather, a government annually expenses the cost to maintain the assets and to sustain their usefulness indefinitely. (For more information, see **By the numbers…the modified approach.**)

By the numbers…the modified approach

Some observers consider traditional depreciation ill-suited for most infrastructure assets because they last far longer than other capital assets. In fact, they say that infrastructure assets are maintained and preserved in such a fashion that their useful lives are practically infinite, rendering the process of depreciating historical cost over those lives impossible (theoretically, at least) or meaningless because the amounts would be so small. Some also state that many infrastructure assets, such as roads and bridges, contain many individual components that are repaired and replaced at different times; consequently, the task of depreciation is made extremely complex.

Based in part on those premises, accounting standards allow governments to report annual maintenance and preservation expenses (instead of depreciation) for infrastructure assets that they can prove are, in fact, preserved at a consistent physical condition each government chooses. To be eligible, a government has to meet two requirements for each **ASSET NETWORK** or **NETWORK SUBSYSTEM** it wishes to report with the modified approach:

1. The government manages the assets with an asset management system that:
   - Has an up-to-date inventory of the assets
   - Assesses the physical condition of the assets and summarizes the results using a measurement scale, and
   - Estimates each year the amount needed to maintain and preserve the assets at the condition level the government establishes.
2. The government documents that the assets are being preserved approximately at or above the condition level it chooses and discloses. It does so by disclosing this evidence in RSI schedules. (These schedules are described in Part Six and illustrated in Figure 32.)

Even if a government's infrastructure assets meet the aforementioned requirements to be reported with the modified approach, the government may still choose not to use the modified approach for them—it is an *option,* not a requirement. When the modified approach is used for some assets but not all, a government includes infrastructure in both the depreciated and nondepreciated categories on the statement of net position or in the notes.

WHAT'S AHEAD?

- WHAT DOES A GOVERNMENT OWE?
- HOW MUCH OUTSTANDING DEBT DOES A GOVERNMENT HAVE?

LIABILITIES

Liabilities are listed in order of how quickly they are expected to be repaid, beginning with those that must be repaid earliest. (If a government uses the classified format, it distinguishes between **CURRENT LIABILITIES** and **NONCURRENT LIABILITIES**, just as it does with assets.) Current liabilities generally are a variety of **PAYABLES** such as amounts owed to employees, vendors, and student organizations. One of the most common long-term or noncurrent liabilities of governments are amounts they have borrowed and must repay, usually with interest, over periods ranging from a couple of years to a couple of decades depending on the type of debt. The amounts of noncurrent liabilities are divided into two parts—the portion that is due within one year and the remainder. The classified format lists the portion due within one year with the current liabilities and the remainder with the noncurrent.

Figure 1: Local City's governmental activities had current liabilities of $17,774,206 and noncurrent liabilities of $183,598,630. The portion of noncurrent liabilities due within one year is $9,236,000.

Issues of estimation come into play with long-term liability amounts on the statement of net position. Long-term liabilities such as those associated with pensions (discussed further in Part Five), claims and judgments, and **COMPENSATED ABSENCES** are not precisely known at the time financial statements are prepared. The best governments can do is estimate such obligations because, for instance, they do not know for certain, at present, how many employees will depart and be paid for their unused vacation and sick leave, or when they will depart, or how many unused leave days they will have accumulated. A government typically builds estimates based on past trends and the government's cumulative current knowledge, sometimes using sophisticated actuarial methods. Governments disclose their assumptions and methodologies for valuing long-term liabilities in the notes.

WHAT'S AHEAD?

- WHAT ARE DEFERRALS?
- WHAT INFLOWS AND OUTFLOWS OF RESOURCES ACTUALLY RELATE TO THE FUTURE?

DEFERRED INFLOWS OF RESOURCES AND DEFERRED OUTFLOWS OF RESOURCES—RESOURCES RELATED TO FUTURE YEARS

Assets and liabilities result from resources flowing to and from the government. Consider these transactions:

- A city levies its property taxes—now the city records property taxes receivable (an asset) and revenue.
- A town has an outstanding loan with a bank and interest on the outstanding amount of the loan is due on the 15th of every month—at the end of the reporting period, the town records a liability called interest payable and an expense in the amount of the interest payable.

These inflows and outflows are related to the fiscal year covered by the financial statements (or an earlier year) and, therefore, result in the immediate reporting of assets, liabilities, revenues, and expenses.

Some inflows and outflows during the fiscal year, however, actually are related to *future* fiscal years. They also result in the immediate reporting of assets and liabilities—*but the reporting of revenues and expenses is deferred until a future period.* Consider, for instance, a county that receives a state grant for general operating purposes during fiscal year 2018. The county does not have to meet any eligibility requirements for the grant, so it usually reports the cash received as an asset and as revenue. But what if the state had said that the grant could not be used until *next year,* fiscal year 2019? Should the county still report the grant as revenue in fiscal year 2018? No, because the grant belongs to next year, based

on the limitation imposed by the state. Consequently, the county initially reports a deferred inflow in 2018 instead of revenue. Only when fiscal year 2019 arrives does the county report the grant as revenue and eliminate the deferred inflow.

Here is another example: A state government enters into an agreement with a private company, in which the company gives the state $100 million and, in exchange, the state gives the company the right to operate a toll bridge and collect tolls from drivers for the next 10 years. The state now has an asset in the form of the cash payment from the company, but is the entire cash payment revenue for this year? No, only the portion related to this year should be recorded as revenue this year; the remainder of the cash payment is related to the remaining years on the agreement. In general, the state would record $10 million ($100 million divided by 10 years) as revenue now, and the other $90 million would be recorded as a deferred inflow of resources (as long as it is not associated with a liability stemming from a commitment the government has made to the company as part of the transaction). The impact on net position in the first year, therefore, would be just the $10 million in revenue; the $100 million in cash is balanced partially by the $90 million deferred inflow. With each passing year, the state would record another $10 million in revenue and reduce the deferred inflow by $10 million.

The main reason governments report deferred inflows and deferred outflows is to help the users of their financial statements assess **INTERPERIOD EQUITY.** Interperiod equity refers to the degree to which a government raises sufficient resources in a year to cover its costs, as opposed to living off of resources accumulated in the past or pushing costs off to future years. By waiting to report inflows and outflows as revenue and expenses, respectively, until the years they are related to, financial statements make it easier to assess whether governments are living within their means from year to year.

WHAT'S AHEAD?

- WHAT RESOURCES CAN BE USED, AND FOR WHAT PURPOSES?
- ARE THERE RESOURCES THAT CAN BE USED FOR ANY PURPOSE?

NET POSITION

Theoretically, net position represents the resources a government has left over to use for providing services after its debts are settled. However, those resources are not always in a spendable form. Furthermore, there may be restrictions on how some of those resources can be used. In order to clarify these issues, governments divide net position into three components:

- **NET INVESTMENT IN CAPITAL ASSETS**—This figure is derived by subtracting the outstanding debts incurred by a government to buy or construct its capital assets from the net figure for those capital assets shown on the financial statement. Capital assets cannot readily (or ever, in some cases) be sold and converted into cash.

- RESTRICTED NET POSITION—A government shows how much of its net position is *restricted* for various purposes. If the restricted net position includes permanent endowments or permanent fund principal, the restricted net position is divided into two components—expendable and nonexpendable. Nonexpendable net position represents resources that cannot be spent but must be retained in perpetuity.
- Net position is considered restricted if its use is constrained to a particular purpose. An external organization, such as a higher level of government or the buyers of a government's bonds, might impose restrictions on how a government may use certain resources. Similarly, a government may be legally or constitutionally required to use resources for particular programs. In order to be considered *legally* restricted by the reporting government itself, rather than an external party, there must be ENABLING LEGISLATION that imposes the restriction before the resources are obtained. Enabling legislation not only authorizes a government to mandate payment from groups and individuals, but also includes a legally enforceable requirement that the resources be used only for specific purposes. Legal restrictions imposed on resources retroactively by governments do not fit these criteria; such resources would be reported as unrestricted.
- UNRESTRICTED NET POSITION—Simply put, these are the resources that do not fall into the first two categories. They generally can be used for any purpose, though they are not necessarily in a readily spendable form, like cash.

Figure 1: Local City had total restricted net position of $11,705,864 for buying and building capital assets, $4,472,704 for repaying long-term debts, $4,811,043 for community development programs, and $3,214,302 for other purposes.

You may find that unrestricted net position is a negative number—a net position deficit. (Such is the case for governmental activities in Figure 1.) This happens because most governments finance long-term obligations such as claims and judgements, compensated absences, and termination pay on a year-to-year basis as they come due and are expected to be paid, rather than setting aside resources as the liabilities are incurred. For some other liabilities, such as those related to pension benefits provided to employees, governments set money aside in advance, but the liability exceeds the amount of the assets. In such circumstances, the existence of an unrestricted net position deficit indicates that the government has deferred the funding of these liabilities, but it does not necessarily reflect positively or negatively on the government's ability to fund those liabilities when they come due. The deficit does not necessarily mean the government will not be able to pay the liabilities in the future. Alternatively, it is possible that the deficit is, in fact, evidence of a serious financial problem. In either case, further investigation is necessary to get to the root of the situation.

One contributing factor is that governments are now following accounting standards that require the reporting of obligations to provide pension benefits to employees as a liability in the statement of net position. Governments will soon do the same for OTHER POSTEMPLOYMENT BENEFITS (called OPEB for short and primarily taking the form of retiree health insurance). These liabilities are quite large for many governments. (See Part Five for more information about these accounting standards.)

Another situation that may cause a government to have a negative unrestricted net position is the issuance of long-term debt to finance the purchase or construction of capital assets that are subsequently given to another government. For instance, a state might issue bonds to construct school buildings and then give the buildings to local school districts. As a result, the state has recorded a liability (the bonds) but has no balancing capital asset (the school buildings appear in the statements of net position of the school districts). Only debt that is related to the capital assets belonging to the state would be subtracted from the net investment in capital assets category of net position; debt related to other governments' capital assets is deducted from unrestricted net position.

WHAT CAN YOU DO WITH STATEMENT OF NET POSITION INFORMATION?

You can use the information in the government-wide statement of net position to address at least three issues:

- What a government owns and how much it owes, and how that has changed over time
- A government's current financial status, and
- A government's future financial status.

One thing you can do with statement of net position information is examine the composition of a government's assets and liabilities (see COMMON-SIZE RATIOS in Part Fourteen). You can determine what proportion of total assets (or total liabilities) is represented by each individual kind of asset (liability) a government owns (owes). The PERCENTAGE DISTRIBUTION may be more meaningful if you calculate similar figures for earlier years to get a sense of what direction the government is headed in. You can get some of this data from the prior-year information in MD&A and from prior years' financial statements. Growth in the percentage of assets that are receivables might signal difficulties collecting taxes. On the other hand, it could mean that a significant cost associated with a new state grant was incurred late in the year and payment from the state government is expected to be received in the following year. Other information would be necessary to determine this for certain, but this quick analysis raises a red flag for you to look further for clues to a potential problem.

You also can determine the degree to which assets and liabilities changed from one year to the next. The tables with summary financial information in the sample MD&A in Appendix A include PERCENTAGE CHANGE numbers to help you understand what happened to Local City's finances during the year. One benefit of percentage change is its ability to raise your awareness of potentially important financial issues. Changes of significant magnitude, for example, should catch your eye immediately and lead you to investigate the circumstances behind them. Local City's receivables increased almost 64 percent in a single year. Determining the precise cause requires further investigation, but you would not have known in the first place that a potential problem might exist if not for the percentage changes you calculated.

The simplest and most straightforward way to assess a government's present financial situation is to compare its total assets and liabilities. Does it own more than it owes, or vice versa? Do assets and deferred outflows exceed liabilities and deferred inflows? You do not even need a calculator, because total net position is the difference between those amounts.

To add some additional meaning to the net position figure, you could compare it to the previous year's net position. (This kind of information can be found in Table A-1 of the sample MD&A as well.) Did net position increase? Then financial position improved. Decrease? Then financial position deteriorated. (The financial statement discussed in Part Seven—the statement of activities—can help you determine *why* financial position improved or deteriorated.)

You also could divide net position by total assets and compare the result with other governments. In either case, you can alternatively utilize only the unrestricted component of net position if you wish to assess or compare the most broadly available resources.

A simple definition of **ECONOMIC CONDITION** (sometimes called **FINANCIAL CONDITION**) is *a government's ability and willingness to meet its financial obligations and service commitments on an ongoing basis*. The statement of net position provides information to help you assess the *ability* part of that definition. (See more on economic condition in Part Fourteen.)

Ability to Meet Financial Obligations

A government's ability to finance its obligations in the future can be examined along two dimensions—short term and long term. If you want to know if a government has enough readily available resources to meet the obligations that will come due over the next year, you could compare its current assets to its current liabilities. (See **LIQUIDITY RATIOS** in Part Fourteen.) Are there enough liquid assets to cover the obligations that will come due in the next year? In other words, are current assets greater than current liabilities? You may want to do this for the governmental activities alone, and not for the total primary government, unless the resources of the BTAs are available to fund governmental activities.

If you make this comparison for Local City's governmental activities, you will find that its current assets are 3.1 times greater than its current liabilities. That means current assets are nominally sufficient to cover obligations as they come due over the coming year. Deciding whether this is the *right* level depends upon your personal views—some might be comfortable with this level of liquidity, while others might believe it to be too high or too low.

If you are particularly concerned about a government's liquidity, you might take a more stringent approach. You could compare only the *most* liquid assets of the government—generally cash, near-cash assets like money market funds, and other short-term investments—to its current liabilities. This is a more conservative indicator of a government's ability to meet financial obligations, assuming

implicitly that its current liabilities will come due so soon that current assets like receivables cannot be liquidated quickly enough to pay for them.

The cash and investments of Local City's governmental activities are more than double the current liabilities. Is that good enough? Ultimately, it is up to you to decide what a satisfactory number is for the purposes of the decisions you wish to make. Though there are plenty of "rules of thumb" to which you may choose to compare a government, they should be handled with extreme care. The circumstances of governments vary greatly from jurisdiction to jurisdiction, raising the very real possibility of comparing apples to oranges. A particular rule of thumb may be predicated on a set of assumptions that are not applicable to the government you are interested in—in which case, the comparison may be meaningless or, worse, misleading.

Even though this guide cannot state categorically how large current assets should be relative to current liabilities, it is appropriate, at least, to mention some possible implications. If you divide current assets by current liabilities, you can produce a number that is indicative of a government's liquidity. In the eyes of some observers, as that ratio gets smaller, a government is less able to cover its obligations as they are due or expected to be paid in the next year. On the other hand, some believe that a higher ratio suggests that more of a government's resources are in the form of cash or near-cash assets than is necessary to pay bills as they come due. In their view, the government would be better off investing more of these highly liquid assets on a longer term basis, which would generate more investment income for the government than leaving them in low-interest bank accounts and short-term investments.

If you are interested in a government's long-term viability or **SOLVENCY**, you will want to look at a broader set of assets and liabilities than just the current ones. Two ways to consider solvency are **LEVERAGE** and **COVERAGE**. (See the section on solvency in Part Fourteen.) Leverage is the degree to which a government's assets are financed through borrowing and other long-term obligations. Stated differently, leverage measures the extent to which a government's assets will be needed to satisfy its debts, rather than be available resources for providing public services. Coverage refers to a government's ability to generate sufficient resources to "cover" its future debt repayments when they are due.

You can use the statement of net position information in two ways to assess solvency—you can compare total liabilities to either total assets or net position. If you divide Local City's total liabilities by its total assets, you get 0.76 or 76 percent; in other words, more than three-quarters of the city's assets will be needed over the long run to satisfy its debts. Dividing by net position instead produces a ratio of 2.9, meaning for every dollar of resources Local City has available to use for providing public services, it owes nearly three dollars. Although these two numbers are different, they provide the same answer to the question, "What kind of burden do the government's liabilities place on its available resources?"

Ability to Meet Service Commitments

Some of the information you will need to determine a government's capacity to finance the services needed by its constituents—either by raising additional revenue or borrowing—comes from the statement of activities (Part Seven) and the statistical section of a government's CAFR. However, liability information in the statement of net position, when combined with certain nonfinancial data, can offer insights into a government's financial capacity.

For instance, you might compare outstanding debts with economic indicators that imply a constituency's "ability to pay" for government services. (See **ABILITY-TO-PAY RATIOS** in Part Fourteen.) The pertinent indicators typically are those related to the economic activity that a government taxes. Because debt frequently is financed with property taxes, a standard comparison would be debt-to-property-values (alternatively, you could include all liabilities instead of only debt). A government's CAFR often contains information about the value of property within its geographic boundaries. Local City's figure is $2.02 of debt per $100 dollars of assessed property value. Many governments are limited by law as to how much they can borrow, and these limitations often are stated in terms of a proportion to assessed value. So it would be relevant to compare this debt ratio to a government's debt limit. (See more on debt limits in Part Six.) Personal income and population also are commonly used in measures of ability to pay—Local City has outstanding debt of $9.09 per $1,000 of personal income, or $882 per resident.

Those ratios can be examined over time to determine if debt levels are rising or falling relative to the economic base that supports a government through taxes. Comparisons also can be made with similar governments, though you will need to make sure the governments measure property value the same way. (This issue is discussed further in Part Fourteen.)

CURRENT ASSETS are expected to be converted to cash within a year and face no restrictions that would prevent the government from doing so

NONCURRENT ASSETS will be liquidated beyond the current year, if at all

CURRENT LIABILITIES are due within a year and require the use of cash or other current assets or the incurrence of another liability

NONCURRENT LIABILITIES come due beyond the current year

NET INVESTMENT IN CAPITAL ASSETS is the portion of net position represented by a government's capital assets, minus the debt issued to construct or buy them

RESTRICTED NET POSITION represents resources that are legally limited to being used for a particular purpose

UNRESTRICTED NET POSITION represents resources that can be used for any purpose

By the numbers…works of art and historical treasures

Most works of art and historical treasures are reported just like other capital assets. However, under certain circumstances, governments do not have to include those kinds of assets in their financial statements (though accounting standards encourage them to do so). A government may elect not to report an art collection or historical treasure if it is:

- Exhibited or otherwise used to further public service, rather than for financial gain
- Protected and preserved, and
- Subject to a policy requiring that, if it is sold, the proceeds be used to acquire other items for the same collection.

If a government decides not to report such a collection or treasure, it provides a note disclosure that describes the collection and explains why it is not being reported as a capital asset in the financial statements.

Upon further review…long-term leases

Long-term leases are common among noncurrent liabilities. If a government signs a lease lasting several years, it commits to paying the owner of the equipment specific amounts on a regular basis over time in return for the right to use the equipment. Structurally, a capital lease is no different from a bank loan, in which a government essentially receives the right to use a bank's money and promises in return to pay the bank certain amounts over a specific schedule.

Upon further review…level of detail for reporting deferrals

A government may show its deferred outflows of resources and deferred inflows of resources in the statement of net position by source—for example, Figure 1 shows deferred inflows related to pensions, retiree health insurance, and a transaction called a "service concession arrangement." Alternatively, governments may present only the total amount of deferred outflows and the total amount of deferred inflows in the financial statements if they disclose the breakout of those totals by source in the notes.

Upon further review…net position v. net assets

The residual amounts in financial statements began to be called *net position* in 2011. Previously, the residual was labeled NET ASSETS. Net assets equal assets minus liabilities. Net position is a broader measure that also encompasses deferrals: assets plus deferred outflows minus liabilities minus deferred inflows. Despite the name change, net position and net assets are directly comparable and the definitions of the three components are identical. Only one small change to the components was made for grammatical reasons: *invested in capital assets, net of related debt,* was retitled *net investment in capital assets.*

Upon further review…does unrestricted mean "usable"?

Unrestricted net position is not necessarily unspent cash sitting in a bank account. Consider a government with unrestricted net position of $5 million, but cash on hand of just $2 million. In order to spend the remaining unrestricted net position, $3 million of noncash assets would have to be sold, a choice with repercussions that must be considered before acting. Sell an asset and you no longer have the benefit of its use in the future, such as investments that generate interest income to pay for services. When the proceeds from selling the investments have been spent, the earnings on the investments are no longer available to the government.

PART FIVE

NOTES RELATED TO THE STATEMENT OF NET POSITION

An extensive set of disclosures relates to the information reported in the government-wide statement of net position, including notes on changes in capital assets and long-term liabilities, risks associated with investments, and obligations for pensions, OPEB, and pollution remediation.

ASSETS

WHAT'S AHEAD?

- WHAT RISKS ARE DEPOSITS AND INVESTMENTS EXPOSED TO?
- WHAT KINDS OF INVESTMENTS DO GOVERNMENTS MAKE?
- WHO OWES GOVERNMENTS MONEY?
- WHAT LIMITS ARE PLACED ON HOW GOVERNMENTS CAN USE ENDOWMENTS?

Deposits

The note disclosures a government makes about the cash it has deposited with banks and other financial institutions primarily are concerned with the risk of loss—the possibility that when the government wants to use the cash, it will not be there. Deposits tend to be insured against loss—for example, by the Federal Deposit Insurance Corporation, but only up to a certain amount. Any deposits above the insured amount might not be recovered if a bank fails. Deposits also may be insured by state government depository insurance funds or insurance pools created by multiple individual financial institutions; however, there tend to be limits on that coverage as well.

In some states, governments are required to "collateralize" their cash deposits with institutions that pledge securities or other collateral against uninsured deposits or the portion of deposits in excess of insurance. The level of collateral required varies from state to state—from a share of the uninsured deposit (such as 75 percent) to a percentage above the uninsured amount (such as 110 percent). The level of collateral required may vary even within a state based on the type of financial institution.

A government prepares a note disclosure if it is exposed to **CUSTODIAL CREDIT RISK**, the possibility that deposits might not be recovered if a bank fails. A government's deposits are *not* considered exposed to that risk if they are:

- Insured, or
- Collateralized with securities held:
  - By the government, or

– In the government's name by a third-party agent representing the interests of the government (in other words, not the bank, but potentially the bank's trust department).

If a government's deposits or a portion of them (1) are not insured and not collateralized or (2) are collateralized with securities that are held by (a) the bank or (b) the bank's agent but not in the government's name, the government will disclose that the deposits are exposed to custodial credit risk.

The note begins by describing the government's policies for addressing custodial credit risk. (See Figure 2.) If it does not have a policy, it will say so.

Figure 2. Cash Deposits Note Disclosure

Custodial Credit Risk—Deposits. Custodial credit risk is the risk that in the event of a bank failure, the County's deposits may not be returned to it. The County does not have a deposit policy for custodial credit risk. As of December 31, 2017, $2,183,000 of the County's bank balance of $9,778,000 was exposed to custodial credit risk as follows:

Uninsured and uncollateralized	$1,683,000
Uninsured and collateral held by pledging bank's trust department, but not in the County's name ①	500,000
Total	$2,183,000

Figure 2 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

The county government in Figure 2 discloses that $2,183,000 of its deposits are exposed to custodial credit risk. It also tells you the nature of that exposure: all $2,183,000 is uninsured, and $1,683,000 is uncollateralized as well.

What can you do with information about deposits?

If you are interested in a government's overall financial health, its ability to pay its bills, or whether there are resources for providing new or additional services, you will want to know if some of the assets reported in the financial statements are exposed to a risk of loss. This note disclosure is intended to help you to ascertain whether a government's deposits are exposed to risk, to understand the sources of the risk, and to begin to assess the extent of that risk.

Investments

If a government has liquid resources available that it will not need immediately for paying bills, it may make good financial sense to invest those resources in order to get a better return than can typically be earned on a bank deposit. However, the greater potential rewards of investments usually go hand-in-hand with greater potential risks. Depending on the type of investment, a government may be exposed to a variety of risks that its investments will not pay out the *amounts* expected or *when* expected or, even worse, that some or all of the amount invested by the government could be lost.

For instance, the longer the maturity on an investment, the greater the rate of return the investment typically offers. (In this context, *maturity* means the future date when the investment is expected to pay off.) However, the longer the period until maturity, the greater the opportunity for market conditions to change in a way that adversely affects the value of a government's investments.

Furthermore, the longer the maturity, the greater the impact that a given change in market interest rates has on value. For instance, an increase in the interest rate of 1 percentage point has a much bigger adverse impact on an investment that matures in 2 years than one that matures in 2 months. You need information about the investments reported in a government's statement of net position in order to assess their inherent risks.

Figure 3: The fair value of Gretatown City's investment in corporate bonds is $35,493,000.

The investments note disclosures present a government's investments by type, along with their FAIR VALUE as of the date of the financial statements. (See Figure 3.) Instead of fair value, governments may use AMORTIZED COST to report interest-earning investments that can or will be liquidated (converted to cash) in the short run—those that will come due in less than one year and MONEY MARKET INVESTMENTS. (See **Upon further review…amortized cost.**) Virtually all other investments are reported using fair value. Investments tend to be aggregated in the financial statements, so this detail in the notes can tell you a lot about *what kinds of investments a government owns.*

The notes also should disclose basic descriptive information about a government's investments:

- A government's policy for determining which qualifying investments, if any, are reported at amortized cost instead of fair value
- If a government has investments in an EXTERNAL INVESTMENT POOL, it discloses:
  - The regulatory oversight for the pool, if any, if the pool is not registered with the SEC, and whether there is a difference between the fair value of the investments and the value of the government's shares in the pool
  - Whether involvement in the external investment pool is involuntary (for example, state law might require that, if a government invests, it does so through the state-sponsored pool)
  - The methods and assumptions made to estimate fair value if a government cannot obtain from the pool the information needed to determine fair value, and

  - The existence of any limitations on the ability of a government to withdraw a part or all of its investment in the pool (for instance, a government is required to provide advance notice, or there is a maximum amount that may be withdrawn at any time).
- Income from the investments of one fund that is assigned to another fund
- The types of investments that the government is legally or contractually allowed to purchase, if there were any violations of those legal or contractual provisions, and actions the government took to address the violations.

Figure 3. Investments Note Disclosure

As of December 31, 2017, Gretatown City had the following recurring fair value measurements (amounts are in thousands):

①

		Fair Value Measurements Using:		
Investment Type	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. Treasuries	$ 112,316	$ —	$ 112,316	$ —
GNMA	23,614	—	23,614	—
ABC Corp. commercial paper	50,697	—	50,697	—
Corporate bonds	35,493	—	35,493	—
Residential mortgage-backed securities	22,548	—	—	22,548
Mutual bond fund	75,420	75,420	—	—
Total	$ 320,088	$ 75,420	$ 222,120	$ 22,548

Debt and equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities. Debt securities classified in Level 2 of the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices. Residential mortgage-backed securities classified in Level 3 are valued using discounted cash flow techniques.

The investments had the following maturities:

②

		Investment Maturities (in years)			
Investment Type	Fair Value	Less Than 1	1–5	6–10	More Than 10
U.S. Treasuries	$ 112,316	$ 77,000	$ 20,316	$ 15,000	$ —
GNMA	23,614	—	15,000 *	8,614	—
ABC Corp. commercial paper	50,697	50,697	—	—	—
Corporate bonds	35,493	—	10,000	20,493	5,000
Residential mortgage-backed securities	22,548	—	22,548	—	—
Mutual bond fund	75,420	75,420	—	—	—
Total	$ 320,088	$ 203,117	$ 67,864	$ 44,107	$ 5,000

*These bonds mature July 2020 but are callable July 2018.

Interest Rate Risk. As a means of limiting its exposure to fair value losses resulting from rising interest rates, the City's investment policy limits at least half of the City's investment portfolio to maturities of less than one year. Investment maturities are limited as follows:

Maturity	Maximum Investment
1 to 5 years	30%
6 to 10 years	15%
More than 10 years	5%

③

Because the mutual bond fund had a weighted average maturity of 9.5 months as of December 31, 2017, it was presented as an investment with a maturity of less than 1 year.

Credit Risk. State law limits investments in commercial paper and corporate bonds to the top 2 ratings issued by nationally recognized statistical rating organizations (NRSROs). It is the City's policy to limit its investments in these investment types to the top rating issued by NRSROs. As of December 31, 2017, the City invested in commercial paper that was rated A1 by Standard & Poor's, F-1 by Fitch Ratings, and P-1 by Moody's Investors Service. The City invested in corporate bonds that were rated AAA by Standard & Poor's and Fitch Ratings, and Aaa by Moody's Investors Service. The City invested in mutual bond funds that were rated AAAf by Standard & Poor's and Aaa by Moody's Investors Service.

Custodial Credit Risk. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Of the City's $15 million investment in repurchase agreements, $2 million of underlying securities are held by the investment's counterparty, but not in the name of the City. The City's investment policy limits holding of securities by counterparties to no more than $5 million.

④ ⑤

Concentration of Credit Risk. The City places no limit on the amount it may invest in any one issuer. The City's investment in ABC commercial paper accounted for 15.84% of the City's total investments.

Figure 3 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② This is an example of using segmented time distribution to disclose exposure to interest rate risk. (See page 59.)

③ You can tell this government is within its state-imposed limits: The investments with maturities between 1 and 5 years represent 21.2 percent of its total investments ([$67,864 ÷ $320,088] × 100); those between 6 and 10 years represent 13.8 percent ([$44,107 ÷ $320,088] × 100); and those over 10 years represent 1.6 percent ([$5,000 ÷ $320,088] × 100).

④ This government does not have a policy for managing concentration of credit risk and, therefore, states that fact.

⑤ This government is not exposed to foreign currency risk and, therefore, does not disclose this type of risk.

Where fair value comes from

The fair value of many investments is easily determined because they are investments that are bought and sold regularly in active markets. Recently issued U.S. Treasury notes—referred to as "on-the-run" Treasuries—are an example of an investment whose fair value can be determined by anyone simply by checking their prices online. This type of valuation information is referred to as "Level 1 inputs" and is considered highly reliable because it is *observable*—in other words, you can find the information yourself and verify its accuracy.

However, some investments may not be the type that are traded on public exchanges, or they may not be traded frequently. Each time the federal government sells new U.S. Treasury notes, the previously issued Treasuries become "off-the-run" and are not bought and sold as often as when they were on-the-run. To measure the fair value of investments that are not traded publicly and frequently, a government may need to look at the prices at which *similar* investments have been sold. Or it may need to develop a value by corroborating two or more sources of observable information. These types of fair values are said to be based on Level 2 inputs, which still are observable information but are not as easily verified by you and others outside the government's financial management.

Still other investments are valued using Level 3 inputs. These fair values are based on *unobservable* information, meaning that they are developed internally by a government using the best data available to it but which you cannot independently verify. A government may use a private company that specializes in measuring fair value, sometimes called a "pricing service." Consequently, these types of fair values are considered relatively less reliable than fair values based on Level 1 or Level 2 inputs. Because you have little or no access to information about the investment, you cannot assess on your own the reliability of the values placed on it.

For some investments such as limited partnerships and hedge funds, there may not be any inputs, regardless of level, with which a government can determine fair value. Instead, the government obtains

information from the entity that it has invested in regarding the value of each ownership share in the entity. This often is called *net asset value (NAV) per share*. The government essentially calculates the value of its investment in the fund by multiplying the NAV per share by the number of shares it owns.

Fair value disclosures. To assist you in understanding the nature of the fair values placed on their investments and how they were determined, governments disclose anything measured at fair value (there may be items other than investments) by the level of inputs used. You can see in Figure 3 that all of the sample government's mutual bond fund investments are in the Level 1 column. By contrast, all of its investments in corporate bonds have fair values based on Level 2 inputs.

If a government has investments with a value based on the NAV per share (or an equivalent measure), it discloses additional information to help you understand the nature of the investment, the risks associated with it, and the possibility that it could be sold for an amount that is not the same as the fair value. For example, a government's note would include descriptions of the following:

- The investment strategy of the entity in which it has invested
- The terms and conditions under which it can redeem its investment
- Circumstances under which it would not be allowed to redeem its investment
- When it would be allowed to redeem investments that currently are not allowed to be redeemed, and
- Any other significant restrictions on its ability to sell the investments.

A sample disclosure might look like Figure 4.

Exposure to risk

A government's notes also reveal whether its investments are exposed to any of five types of risk of loss: overall credit risk, custodial credit risk, concentration of credit risk, foreign currency risk, and interest rate risk. For any of these risks that a government is exposed to, it discloses its policy for addressing the risk (or states that it has no policy). Notice in Figure 3 that each of the risk disclosures is accompanied by a policy description. Observe as well that one of the five risks—foreign currency—is not mentioned, which means that the government's investments are not exposed to that risk.

OVERALL CREDIT RISK is the chance that an issuer of an investment will not fulfill its obligations; for instance, the possibility that a government may not receive the payments it is due from a corporate bond. Obligations of or explicitly guaranteed by the U.S. government are not considered in the accounting standards to be exposed to overall credit risk sufficient to warrant additional disclosures. Governments disclose overall credit risk by reporting the credit quality ratings of their investments as determined by the rating agencies. The investments in mutual bond funds of the city in Figure 3 were rated AAAf by one rating agency and Aaa by another. High credit quality ratings such as those suggest the risk that the investments will not pay off is relatively low.

Figure 4. Note Disclosure for Net Asset Value per Share

Multi-strategy hedge funds. The County invests in 15 hedge funds that pursue multiple strategies to diversify risks and reduce volatility. The hedge funds' composite portfolio for this type includes investments in approximately 50 percent U.S. common stocks, 30 percent global real estate projects, and 20 percent arbitrage investments. The fair values of the investments in this type have been determined using the NAV per share of the investments. Investments representing approximately 15 percent of the value of the investments in this type cannot be redeemed because the investments include restrictions that do not allow for redemption in the first year after acquisition. The remaining restriction period for these investments ranged from four to six months at December 31, 2017.

As with cash deposited with a bank or financial institution, a government's investments could be exposed to *custodial credit risk*. When investments are uninsured and held by a counterparty or a counterparty's trust department or agent (but not in the government's name), a government discloses the amounts of those investments. A government's investments in mutual funds and external investment pools are not exposed to this type of risk, however, because they do not involve an actual individual security but, rather, a share of the total investments made by the fund or pool as a whole.

A government's potential losses from credit risk are heightened if a significant portion of its resources are invested with a single issuer. If that issuer did not make good on its obligation to the government, the impact could be potentially damaging. Therefore, governments report their **CONCENTRATION OF CREDIT RISK** by disclosing, by amount and issuer, investments in any single issuer that represent more than 5 percent of the total investments in the column they are reported in. (For these purposes, governments do not have to report investments of or guaranteed by the U.S. government, or investments in mutual funds, external investment pools, or other pooled investments.)

FOREIGN CURRENCY RISK is the chance that changes in exchange rates will adversely affect the fair value of a government's investments and deposits. Governments disclose the amounts, in U.S. dollars, of deposits and investments exposed to foreign currency risk, organized by currency denomination and investment type.

Interest rate risk. The possibility that changes in interest rates will reduce the fair value of a government's investments is called **INTEREST RATE RISK**. As mentioned before, in general, the longer the period until an investment matures, the greater the negative impact that changes in interest rates can have on fair value. Governments may use any of five prescribed methods for reporting interest rate risk (based on how they actually manage interest rate risk), disclosing any assumptions that were required.

1. A government with few investments might use *specific identification* to list each of the investments and their maturity dates individually.

2. A *segmented time distribution* shows the total fair value of investments maturing during a given period. For instance, Figure 3 divides fair value into four periods—less than 1 year, 1 to 5 years, 6 to 10 years, and more than 10 years.
3. *Weighted average maturity* of a type of investment is calculated by multiplying each individual investment's fair value by the amount of time until maturity (in years or months), then adding the individual calculations and dividing them by total fair value for the investment type. For example, using the amounts in Figure 5, weighted average maturity is calculated as follows:

$	215,000	×	0.24	=	$	51,600		
	119,864	×	4.20	=		503,429		
	23,614	×	3.24	=		76,509		
	55,493	×	6.24	=		346,276		
	160,500	×	17.52	=		2,811,960		
	Total				$	3,789,774	÷ $ 574,471	= 6.60

This produces an average maturity that takes into account the size of individual investments relative to the total. Figure 5 presents an example of what this disclosure might look like.

Figure 5. Interest Rate Risk Note Disclosure Using Weighted Average Maturity

As of December 31, 2017, the City of Pattiville had the following investments:

Investment Type	① Fair Value	Weighted Average Maturity (months)
Repurchase agreements	$ 215,000	0.24
U.S. Treasuries	119,864	4.20
U.S. agencies	23,614	3.24
Commercial paper	55,493	6.24
Corporate bonds	160,500	17.52
Total fair value	$ 574,471	
Portfolio weighted average maturity		6.60

Interest Rate Risk. In accordance with its investment policy, the City manages its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio to less than 10 months.

4. *Duration* is another approach to calculating aggregate measures of the time to maturity. Duration essentially calculates weighted average maturities for each of the individual payments made until an investment's maturity, rather than an average of the aggregate fair values of all investments of a similar type. In so doing, duration takes into account the *timing* of payments—if two investments have the same fair value but the first investment makes a larger portion of its payments earlier

than the second investment, the first investment would have a lower duration. Duration is an indicator of volatility—the higher the duration, the greater the loss of fair value as interest rates rise. Figure 6 presents an example of what the interest risk disclosure might look like using duration.

5. Lastly, some governments use a *simulation model* to estimate the impact that potential changes in interest rates would have on fair value. For example, the disclosure might show (as in Figure 7) estimated fair values if interest rates were to rise 1, 2, or 3 percentage points (each percentage point equals 100 basis points).

Figure 6. Interest Rate Risk Note Disclosure Using Duration

As of December 31, 2017, the Milligan Water District had the following investments (dollars are in thousands):

Investment Type	① Fair Value	Duration (months)
Repurchase agreements	$ 250,000	2.52
U.S. Treasuries	119,864	14.88
U.S. agencies	23,614	38.52
Taxable state bonds	10,000	21.96
Corporate bonds	90,500	8.16
Total fair value	$ 493,978	
Portfolio duration		8.64

Interest Rate Risk. Through its investment policy, the District manages its exposure to fair value losses arising from increasing interest rates by limiting the duration of its investment portfolio to less than nine months.

Figures 4–6 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Governments pay particular attention in the disclosures to investments that are highly sensitive to interest rate risk—in other words, small changes in interest rates result in large changes in fair value. Governments disclose in the notes the fair value of highly sensitive investments and the terms that cause them to be sensitive. For instance, an investment might include a multiplier that amplifies the effect of changes in interest rates—say, 1.25 times a commonly used interest rate index. For any change in interest rates, the impact on the fair value of that investment will be 25 percent greater.

Repurchase agreements and reverse repurchase agreements

Some governments engage in an investment called a REPURCHASE AGREEMENT. This involves a government providing cash to an investment firm or other financial institution and receiving U.S. government securities in exchange. The firm promises to repay the cash with interest in exchange for the return of the securities. Governments engage in "repos" because they tend to be short term but offer a relatively high return in relation to the market; furthermore, they generally involve U.S. government securities, which are high-quality investments. Repurchase agreements are distinguished from other types of investments in the required note disclosures, including the notes identifying potential risks.

Figure 7. Interest Rate Risk Note Disclosure Using a Simulation Model

Interest Rate Risk. The following table summarizes the estimated effects of hypothetical increases in interest rates on the fair values of the County's investments. It assumes that the increases occur immediately and uniformly to each type of investment. The hypothetical changes in market interest rates do not reflect what could be deemed best- or worst-case scenarios. Variations in market interest rates could produce significant changes in the timing of repayments due to prepayment options. For these reasons, actual results might differ from those reflected in the table.

① ②

	Fair Value
December 31, 2017	$ 3,000,000
Fair value of portfolio after an increase of:	
100 basis points	2,915,979
200 basis points ③	2,834,756
300 basis points	2,756,226

Figure 7 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② What do these last couple of sentences mean? A particular change in interest rates might lead the counterparty to the investment to exercise a prepayment option, which would result in the government's not receiving the payment it expected had the investment remained intact until the expected maturity date.

③ 100 basis points equal 1 percentage point. An increase of 100 basis points might be a rise in the interest rate from 3 to 4 percent, for example.

In a REVERSE REPURCHASE AGREEMENT, the roles are switched: the government provides the securities in exchange for cash from the financial firm, which the government returns with interest at a later date upon return of the securities. They actually are two sides of the same transaction—a repo agreement from the government's perspective is a reverse repo agreement from the perspective of the firm, and vice versa.

There are risks inherent in a reverse repo. One is a credit risk that the securities transferred to the financial firm will not be returned; the government would lose the difference, if any, between the value of the securities and the cash received from the firm. Another risk is that the value of the securities diminishes before they are repurchased. A third risk relates to how the government uses the cash it receives. Ideally, it invests the cash in securities that (1) provide a greater return than the amount the government is obligated to pay and (2) pay off in time to make the payments. There are risks, however, that the return will not be as great as expected or that the securities purchased with the cash will not be repaid in a timely fashion.

If a government participates in any reverse repurchase agreements, its investments note disclosures provide information you can use to assess the risks the government is exposed to. First, the government's note compares the amount of its obligations related to the agreement with the fair value of the securities underlying the agreements. (See Figure 8.) Second, if the government is committed as of the date of the financial statements to repurchasing securities, it discloses the fair value of the securities and the terms of the agreement. Third, if a financial firm defaults on an agreement, the government discloses the resulting losses, as well as any amounts recovered from losses in prior years. Finally, if the government invests the proceeds of the reverse repurchase agreement, it discloses whether the maturities of those investments are matched to the maturities of the agreement.

Figure 8. Reverse Repurchase Agreement Note Disclosure

Reverse Repurchase Agreements. State statutes permit Ragan County to enter into reverse repurchase agreements. The credit exposure at year-end related to these agreements was $1,539,000. All sales of investments under reverse repurchase agreements are for fixed terms. In investing the proceeds of reverse repurchase agreements, County policy is for the term to maturity of the investment to be the same as the term of the reverse repurchase agreement. Such matching existed at year-end. (1)

Securities lending

A SECURITIES LENDING transaction involves a government transferring securities to a financial firm or other party in exchange for collateral (which may be cash, securities, or letters of credit), while simultaneously agreeing to return the collateral for the same securities in the future. Securities lending differs from reverse repurchase agreements in that the latter involves the actual *sale* and *repurchase* of securities. In the midst of the agreement, a government's financial statements report only the proceeds

of the repo agreement (or the investments made with the proceeds of a reverse repo) as assets, and not the securities, because the securities have been sold to the financial firm. Under securities lending, however, the securities have been *borrowed* from the government. Consequently, its financial statements continue to report the securities as assets, *as well as* the collateral provided by the financial firm (if that collateral is cash or securities the government has the right to pledge or sell in another transaction) and a liability to the financial firm.

The basic descriptive note disclosures made for other investments also are made for securities lending transactions—the authority to engage in these activities, significant violations and actions to address them, exposure to custodial credit risk, classification by type of investment, and so on. Governments also describe their securities lending transactions, including:

- The types of securities involved
- The types of collateral received and whether the collateral can be pledged or sold
- The amount by which the value of the collateral is required to exceed the value of the securities
- The degree to which the borrower of the securities protects the government against loss.

The disclosure should report the fair values of the underlying securities as of the date of the financial statements, as well as the amounts reported for those securities in the financial statements if they differ from the fair value. (See Figure 9.)

Governments also make securities lending note disclosures similar to those for reverse repurchase agreements, including:

- Whether the maturities of investments made with collateral cash generally match the maturities of the loaned securities
- The degree of credit risk exposure resulting from the amounts the borrower of the securities owes the government being greater than the amount the government owes the borrower
- A government's losses, as well as any amounts recovered from losses in prior years, related to a borrower of the government's securities defaulting.

What can you do with investment information?

Because cash deposits tend to earn lower interest, some governments invest much of their idle cash to earn more income until the resources are needed. If there is a risk that a government may not be able to cash in those investments for the expected amount when necessary, you should know about it. These notes to the financial statements help you to assess *whether a government's investments are exposed to the most common risks of loss*. What are the chances the issuer of an investment will not make payment when the government needs its money back? Is the government heavily invested in one or a few types of investments or issuers that are exposed to greater risk than is typical? If interest rates go up, what will happen to the value of the government's investments and, therefore, to the amount of money it will get if it needs to sell them? How long will it be before these investments pay off (come due)?

Figure 9. Securities Lending Note Disclosure

①

Securities Lending Transactions. State statutes and board of trustees investment policies permit the Pelham County Pension System to use investments of the two plans to enter into securities lending transactions—loans of securities to broker-dealers and other entities for collateral with a simultaneous agreement to return the collateral for the same securities in the future. The System's securities custodians are agents in lending the plans' domestic securities for cash collateral of 102 percent and international securities for cash collateral of 105 percent. At year-end, the System has no credit risk exposure to borrowers because the amounts the System owes the borrowers exceed the amounts the borrowers owe the System. Contracts with the lending agents require them to indemnify the System if the borrowers fail to return the securities (and, if the collateral is inadequate, to replace the securities lent) or fail to pay the System for income distributions by the securities' issuers while the securities are on loan.

All securities loans can be terminated on demand by either the System or the borrower, although the average term of the loans is one week. In lending international securities, the term to maturity of the securities loans is matched with the term to maturity of the investment of the cash collateral by investing only in overnight repurchase agreements. Such matching existed at year-end. In lending domestic securities, cash collateral is invested in the lending agent's short-term investment pool, which at year-end had a weighted average maturity of 28 days. The relationship between the maturities of the investment pool and the System's loans is affected by the maturities of the securities loans made by other entities that use the agent's pool, which the System cannot determine.

Custodial Credit Risk. Custodial credit risk is the risk that, in the event of the failure of the counterparty, the System will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Consistent with the System's securities lending policy, $226,050,000 was held by the counterparty that was acting as the System's agent in securities lending transactions.

The disclosure also provides important, basic details you are not likely to see in the financial statements. What kinds of investments does the government have? Is it more heavily invested in one kind of investment or another? What kind of investing is the government allowed to do?

Receivables

Amounts that a government is owed from individuals, businesses, other governments, and others (or that one part of a government is owed by another) are known as receivables. The receivable amounts are reported in a government's financial statements net of what it estimates it (1) will have to refund or (2) will not be able to collect in the first place. In order to keep the financial statements orderly and readable, a government may aggregate certain similar items, such as different types of receivables—taxes receivable, FINES RECEIVABLE, interest receivable, and DUE FROM OTHER GOVERNMENTS, for instance. If it does so, a government will prepare a note disclosure with additional information about the significant components of that receivables amount. (See Figure 11.)

Governments are not required to present a note disclosure that looks like the table in Figure 11. Smaller, less complex governments sometimes present a narrative description of the types of

receivables they have and the percentage those receivables represent of the amount shown in the financial statements. That narrative might look like Figure 10.

Figure 10. Receivables Note Disclosure (Narrative Format)

①

Receivables in the general fund are 48 percent property taxes receivable ($2,513,755), 28 percent intergovernmental receivables ($1,466,356), and 24 percent other receivables ($1,256,877). Receivables in the housing program funds consist principally of notes and liens receivable, 90 percent of which ($2,801,308) are not scheduled to be collected in the subsequent year. The remaining receivables in the nonmajor governmental funds are primarily intergovernmental receivables. Receivables in the water and sewer fund are 63 percent accounts receivable ($3,415,670) and 37 percent due from other governments ($2,006,028).

However, many governments present the information in the tabular form shown in Figure 11. That illustration shows the different types of receivables for this government—accounts receivable, taxes receivable, special assessments receivable, due from other governments, and other accounts receivable—arrayed across the top of the table. The list in the left-hand column includes the government's funds. Thereby, for each fund you can see the different types of receivables it contains.

Receivables that will not be collected within a year

If significant receivable amounts are not expected to be collected during the next year, a government will identify them in this note disclosure. The government in Figure 11 meets this requirement by showing a separate line for "amounts not scheduled for collection during the subsequent year." That line reports that $1,650,000 of special assessments receivable are not scheduled to be collected in the year after the financial statement date. Rather than including such a line, some governments may discuss this issue in narrative form; for example:

> The only receivables not expected to be collected within 1 year are $10 million of notes and liens receivable in the housing program funds.

What can you do with information about receivables?

The first thing you may notice in this note is that governments have different kinds of receivables. Are all accounts receivable created equal? Perhaps not. Some may be collected more quickly than others. This could be important to you if you are interested in a government's liquidity—its ability to come up with the cash it needs to meet its payments in the short run. Such an assessment would involve a comparison of the resources the government will have available over the coming year with the bills that will come due during that time; some people look at even shorter periods: one month, three months, or six months.

Figure 11: Taxes receivable in the general fund totaled $4,457,000.

Figure 11. Receivables Note Disclosure (Tabular Format)

Receivables at June 30, 2017, for the Town of Lakeville Green were as follows:

①

	Accounts	Taxes	Special Assessments	Due from Other Governments	Other	Total Receivables
Governmental activities:						
General	$ 10,935,000	$ 4,457,000	$ —	$ 5,004,000	$ 235,000	$ 20,631,000
Utilities services tax	2,676,000	—	1,990,000	—	—	4,666,000
Gas tax	347,000	—	22,000	1,841,000	—	2,210,000
Other governmental	141,000	—	—	653,000	182,000	976,000
Internal service	215,000	—	—	—	—	215,000
Total—governmental activities	$ 14,314,000	$ 4,457,000	$ 2,012,000	$ 7,498,000	$ 417,000	$ 28,698,000
Amounts not scheduled for collection during the subsequent year	$ —	$ —	$ 1,650,000	$ —	$ —	$ 1,650,000
Business-type activities:						
Wastewater	$ 3,789,000	$ —	$ —	$ 1,825,000	$ 323,000	$ 5,937,000
Solid waste	1,199,000	—	—	—	—	1,199,000
Other proprietary	435,000	—	—	—	89,000	524,000
Total—business-type activities	$ 5,423,000	$ —	$ —	$ 1,825,000	$ 412,000	$ 7,660,000

Figures 8–11 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Information about receivables that will not be collected in the coming year also is important if you are interested in a government's ability to pay its bills in the short run. If a government tells you in this note that a certain receivable will not be collected until more than a year later, you know that you cannot include it as a resource that can be used to pay bills this year. If you did not have this note, you would not have known that a portion of the receivable amount in the financial statements would not be available for at least a year, unless the government presents its statement of net position in a classified format; even so, you likely would not be able to identify the amount separately in the statement.

Examining receivable balances over time may help you to understand whether a government's ability to collect its receivables is improving or declining. This might involve comparing a particular type of receivable with the relevant revenue source—for example, you might divide a town's property tax receivables at the end of the fiscal year by its property tax revenues for the year. (See the FINANCIAL EFFICIENCY RATIOS in Part Fourteen.) For Local City, that ratio would be 5.86 percent.

This ratio enables you to track whether a government is collecting more or less of its property taxes over time. The lower the ratio, the more that is being collected (or, conversely, the less that remains uncollected). If this ratio were to rise over time, for instance, it might indicate that property owners are having greater difficulty making their payments. Alternatively, a government may not be doing as good a job at collecting on delinquent tax payments; perhaps the number of enforcement staff has declined. You would need to pursue the matter further with the government to determine the cause, but the ratio gives you a heads up that the issue may require further exploration.

Another way to look at receivables is to measure how long it takes a government to collect on its receivables. Based on the information in Local City's financial statements, we can show that it collected property taxes it was owed in a little more than 24 days on average in fiscal year 2017. (The calculation is explained in Part Fourteen.)

Changes in a government's ability to collect monies it is owed affect its liquidity—the quicker it collects, the more cash it has available to pay bills. If, on the other hand, a government is having more difficulty collecting on its receivables, it may have to borrow money in the short run (or increase the amount it already borrows short term) in order to pay its bills. That means higher costs for the government. A declining rate of collection on receivables, especially taxes receivable, also may be an omen of coming economic stress, if taxpayers are having greater difficulty paying their tax bills.

Donor-Restricted Endowments

An endowment is a restricted gift of resources that is invested to produce earnings that can be used to finance activities. Donors often require that a government maintain the donation in perpetuity—the donated monies are invested and the earnings can be spent, but the principal or corpus of the endowment is required to remain unspent. Some donors also place restrictions on how the earnings

may be utilized—to fund college scholarships to needy students, perhaps, or to provide for the upkeep of an historic site. If you are trying to assess what resources a government can utilize to provide services, it is important to understand what portion of an endowment can be used and for what purposes.

Consequently, if a government has a donor-restricted endowment, it prepares a note disclosure with the following information:

- What portion, if any, of net increases in the value of the endowment's investments can be spent and where in the government's net position that amount is reported
- The state law authorizing a government to spend such amounts
- The government's policy for authorizing and spending investment income. For instance, it may be the government's policy to spend a particular percentage of increased value.

WHAT'S AHEAD?

- WHAT KINDS OF CAPITAL ASSETS DOES A GOVERNMENT HAVE?
- HOW HAVE THE CAPITAL ASSETS CHANGED OVER TIME?
- HAS THE SERVICE CAPACITY OF CAPITAL ASSETS CHANGED?
- HAS A GOVERNMENT TRANSFERRED OPERATION OF A CAPITAL ASSET TO A COMPANY OR ANOTHER GOVERNMENT?

Capital Assets

These long-lived assets usually are a government's most expensive assets, and include land, buildings, infrastructure (such as bridges and sewer pipes), equipment (computers and networks, for instance), and vehicles (school buses, patrol cars, garbage trucks, and so on). When a capital asset is purchased, constructed, or donated, it is added to the statement of net position. That amount is not reported immediately as an expense, however. To do so would overstate a government's costs in a given year, because that asset can be used by the government for many years. Accounting employs depreciation to allocate that original cost among each of the years in which the asset is expected to be used. (For an explanation of how depreciation works, refer to **Tools of the trade…inventory and capital asset expenses** on page 26.) Depreciation simulates the deterioration of capital assets—absent any effort to improve or extend the life of a building, its physical condition would be expected to diminish with each passing year.

Changes in capital assets

A government presents a note disclosure that details how its capital assets changed during the year covered by the financial report. (See Figure 12.) The first thing you should notice is that there is a lot more information here than in the statement of net position. (Compare with Figure 1.) A government

may include as few as two lines for capital assets in the financial statement (those that are depreciated and those that are not), but in this note, it is required to show major classes of capital assets, such as land, buildings, infrastructure, and equipment. The note also shows capital assets related to governmental activities separately from those related to BTAs. Finally, assets that are not subject to depreciation—land, infrastructure that is reported using the modified approach, and construction in progress—are reported separately from capital assets that are depreciated.

Figure 12: Construction in progress added during the year to BTAs was $980,000. The beginning balance for land associated with governmental activities was $29,484,000.

The capital assets note contains four columns of information. The first column presents the original cost, accumulated depreciation, and net amounts *as of the start of the year*. Unless an adjustment has been made, these likely are the amounts that were reported as ending balances in the previous year's financial report. The right-hand column presents the same information, but *for the end of the year* covered by the financial statements. The totals in the right-hand column are the same as those shown in the statement of net position.

The two middle columns explain how the capital asset amounts changed from the end of the previous year to the end of the current year. One column shows additions to the government's capital assets through purchases, the completion of construction, or donation, as well as the depreciation reported for the year. The other column reports information about assets that have been sold or otherwise disposed of. If a capital asset suffers an IMPAIRMENT—meaning it cannot be used, or its capacity to be used to provide services is greatly diminished, because of physical damage, obsolescence, or some other reason—the "writing down" of the asset is shown in the retirements column, too. (Asset impairment disclosures are discussed below.) Lastly, the column includes "reclassified" amounts—shifting the value of an asset from construction in progress to one of the other lines (such as buildings or infrastructure) when the asset is put into operation.

Because depreciation expense is a direct cost that is aggregated with other direct costs in each function or program reported in the statement of activities (see Part Seven), you cannot tell how much depreciation was for the year from the financial statement alone. The additions column includes the depreciation expense for each kind of capital asset and a total. The bottom part of the note then shows how depreciation expense was allocated among the expense categories in the statement of activities.

What can you do with information about changes in capital assets? Comparing the overall net value of capital assets that is shown in the statement of net position with the previous year does not provide a complete or detailed picture of the extent of a government's investment in its physical plant, nor of the pace of depreciation. This note disclosure includes information that can help you understand what types of capital assets the government has and the portion of the amount shown in the financial statements that each represents. This note provides information not just about how much capital assets increased or decreased *overall* during the year, but also what caused that change: How much did

the government add to its capital assets through construction and other means? Were capital assets removed from the government's stock? Is the government's physical plant increasing or decreasing in value? Are specific types of capital assets increasing or decreasing faster than others?

Figure 12. Capital Assets Note Disclosure

Capital asset balances and activity for the year ended December 31, 2017, was as follows (in thousands): ①

	② Beginning Balance	Additions	③ Retirements/ Reclassifications	Ending Balance
	Primary Government			
Governmental activities:				
Capital assets that are *not* depreciated:				
Land	$ 29,484	$ 2,020	$ (4,358)	$ 27,146
Construction in progress	2,881	768	(2,326)	1,323
Total	32,365	2,788	(6,684)	28,469
Capital assets that *are* depreciated: ④				
Buildings and improvements	39,961	734	—	40,695
Equipment	32,110	1,544	⑤ (1,514)	32,140
Infrastructure	92,594	14,378	—	106,972
Totals	164,665	16,656	(1,514)	179,807
Less accumulated depreciation:				
Buildings and improvements	(10,358)	(691)	—	(11,049)
Equipment	(9,247)	(2,676)	⑤ 1,040	(10,883)
Infrastructure	(15,301)	(1,020)	—	(16,321)
Totals	(34,906)	(4,387) *	1,040	(38,253)
Total depreciable capital assets, net:	129,759	12,269	(474)	141,554
Governmental activities capital assets, net	$ 162,124	$ 15,057	$ (7,158)	$ 170,023 ⑥
Business-type activities:				
Land	$ 3,691	$ 145	$ —	$ 3,836
Distribution and collection systems	35,522	3,838	—	39,360
Buildings and equipment	122,870	3,847	(32)	126,685
Construction in progress	4,955	980	(3,311)	2,624
Totals at historical cost	167,038	8,810	(3,343)	172,505
Less accumulated depreciation for: ⑦				
Distribution and collection systems	(7,654)	(897)	—	(8,551)
Buildings and equipment	(11,789)	(808)	32	(12,565)
Business-type activities capital assets, net	$ 147,595	$ 7,105	$ (3,311)	$ 151,389 ⑧

Depreciation expense was charged to governmental functions as follows: ⑨

General government	$ 275
Public safety	330
Public works, which includes the depreciation of general infrastructure	1,315
Health and sanitation	625
Cemetery	29
Culture and recreation	65
Community development	40
In addition, depreciation on capital assets held by the City's internal service funds is charged to the various functions based on their usage of the assets	1,708
Total depreciation expense	$ 4,387

Figure 12 Notes

① NOTE: These amounts have been rounded to thousands of dollars, whereas they are shown in whole dollars in Figure 1.

② The amounts in the beginning balance column come from the prior year's financial statements.

③ Additions typically are the cost of assets acquired, constructed, or rebuilt during the year (and new construction not yet completed). Additions also include the year's depreciation expenses, which are added to accumulated depreciation. Retirements are the removal of historical cost and accumulated depreciation related to assets sold, destroyed, or that otherwise became unusable to the government during the year (and adjustments to reflect completion of construction in progress).

④ A government may show as much of this detail for governmental activities and BTAs on the face of the statement of net position as it chooses.

⑤ Not only is the historical cost of the retired equipment removed from the beginning balance but also the accumulated depreciation on that equipment.

⑥ This amount appears in Figure 1 (though not rounded).

⑦ Historical cost and accumulated depreciation also may be shown separately on the statement of net position (Figure 1 shows a net amount of historical cost minus accumulated depreciation).

⑧ This amount (when not rounded), plus restricted cash, equals the total noncurrent assets amount shown for BTAs in Figure 1.

⑨ Depreciation is allocated among the functional and programmatic expenses in the statement of activities (see Figure 42).

The presentation of the information allows you to examine governmental activities and BTAs separately. The capital assets of governmental activities and BTAs may be maintained differently, which might be reflected in the degree to which each has been depreciated. Comparing accumulated depreciation with the original or historical cost of capital assets can give you a general sense of how old the assets are as a group. Consider, for instance, a government using straight-line depreciation to allocate historical cost in equal annual amounts: If accumulated depreciation on the government's equipment were greater than half the original cost, you would know that the equipment, on average, has less than half of its useful life left. (See financial efficiency ratios in Part Fourteen.) In this way, you can make broad judgments about the general need to rehabilitate the government's capital assets or to purchase or construct new ones. To know for certain, you would need to obtain additional information, but such a comparison could be a useful signal.

Tracking that ratio of net capital asset value divided by original cost over time may be an indicator of whether a government is investing sufficiently in its capital assets to keep pace with their physical deterioration. Ideally, this would be done separately for the major classes of capital assets. Using information on buildings and improvements from the note disclosure for Local City in Figure 12, that ratio was 74.1 percent at the start of 2017 and 72.8 percent at the end of the year. In other words, the average life remaining on the city's buildings got shorter. The change in this indicator over a period

of 10 years or more would offer significant insight into whether a government is gaining or losing ground in maintaining the useful lives of its capital assets.

Asset impairment

When a capital asset is put into service, a government estimates how long it will have service capacity—in other words, how long it can be used to provide services. Inherent in some of those estimates are assumptions about the volume of usage—number of vehicles crossing a bridge, number of gallons of wastewater treated by a sewage plant, and so on. Such estimates may be based on prior experience with similar assets or on industry benchmarks. Sometimes, however, the actual useful lives or levels of service capacity that have been assumed for a capital asset do not turn out to be accurate. There may be several reasons for this:

- Physical damage, such as the collapse of a bridge
- Changes in laws and regulations, such as more stringent drinking water rules that a treatment facility no longer meets
- Obsolescence, such as computer equipment that is out of date and no longer used
- A change in how an asset is used or how much it is used, such as the closing of a school building because enrollment has declined and the space is no longer needed
- A stoppage in the construction of a capital asset, perhaps because a government has run out of money for that project.

If such events or circumstances arise, a government evaluates whether an asset impairment has occurred. If the government determines that a capital asset is impaired, it follows procedures laid out in the accounting standards for determining the degree to which service capacity has been diminished and, thus, how much the carrying value of the asset (historical cost minus accumulated depreciation) should be reduced.

If an impairment has happened, but its occurrence is not apparent from the information in the financial statements (probably because it is aggregated in a much larger category with many other assets), a government presents a note disclosure that includes a description of the impairment, the amount of the loss in the value of the asset as reported in the financial statements, and the classification of capital assets in the financial statements from which the loss was deducted. The government also discloses the net value of impaired capital assets that are idle (in other words, not being used) at the date of the financial statements. An impairment disclosure for obsolete equipment might look like this:

> Hospital program expenses include an impairment loss of $1,156,754 related to a magnetic resonance imaging (MRI) machine, previously reported with equipment, that has become impaired due to unexpected obsolescence.

Service concession arrangements

Governments sometimes enter into a transaction called a **SERVICE CONCESSION ARRANGEMENT (SCA)**. An SCA involves a government transferring the responsibility to operate a capital asset, such as a toll road, along with the right to collect fees from the users of the capital asset, to a private company or another government (referred to as the *operator*). In return, the operator usually makes a significant up-front cash payment (or sometimes up-front installment payments) to the government. Such a transaction is considered an SCA for accounting and financial reporting purposes if (1) the government retains the power to determine who the operator provides service to, how much it provides, and how much it charges (even if the government does not exercise those powers) *and* (2) there will be significant service capacity left on the capital asset when it is returned to the government at the end of the transaction. Otherwise, the arrangement would be reported using the accounting standards for a lease, asset sale, or other transaction, as appropriate.

If a government has entered into an SCA, it discloses a general description of the SCA, its reasons for entering into it (for example, to reduce operating expenses or to obtain a new or improved capital asset), and the status of construction if the SCA involves the operator building a new capital asset or renovating an existing one. Governments also disclose:

- The amounts of assets, liabilities, and deferred inflows associated with the SCA that are reported in the financial statements
- A description of the rights retained by the government in the agreement and any rights transferred to the operator
- Any guarantees or commitments made by the government in the agreement, such as making up the difference if the operator's revenues do not meet an agreed upon threshold.

An illustrative note disclosure for a state that enters into an SCA to operate a toll bridge might look like Figure 13.

Figure 13. Service Concession Arrangement Note Disclosure

①

At the end of the current year, the State, through its State Department of Transportation (SDOT), entered into an agreement with a private company, under which the company will operate and retain tolls from the Dolan State Bridge for the next 20 years. The company is required to operate the bridge and the SDOT is required to maintain the bridge in accordance with the State Bridge Concession Contract. The present value of the SDOT's maintenance obligation is estimated to be $10 million. SDOT received from the company a lump-sum payment of $100 million. The SDOT plans to use the proceeds from the up-front payment to finance infrastructure investment throughout the state. The State reports the bridge as a capital asset with a carrying amount of $50 million at year-end and also reports a deferred inflow of resources in the amount of $90 million and a performance liability related to maintenance activities in the amount of $10 million at year-end pursuant to the service concession arrangement.

As previously noted, the accounting standards for SCAs do not allow governments to recognize the up-front payment as revenue in one lump sum. Rather, the payment is reported as a deferred inflow of resources in the statement of net position, and the deferral is reduced and revenue is recognized systematically each year over the length of the SCA. In the illustration above, the state received $100 million from the operator; initially, it would have recognized a $100 million deferred inflow and then reduced the deferral and recognized a revenue for the first year's portion. If this were done in equal installments, the deferral would decline by $5 million in each of the 20 years of the SCA, and revenue of $5 million would be reported. Thus far, according to the disclosure, $10 million of the illustrative SCA's up-front payment has been reported as revenue ($100 million minus the $90 million deferred inflow).

If the SCA obligates the government in some manner, the government reports a liability in the statement of net position equal to the cost of the obligation. In the illustration, the government is obligated to provide maintenance services to the operator of the bridge, which the government estimates at $10 million. A liability of $10 million would appear in the financial statements as a result.

What can you do with information about SCAs? SCAs are transactions generally involving valuable infrastructure assets and significant sums of money paid to a government. How much did the government receive up front? How much has been recognized as revenue thus far, and how much remains because it relates to future periods?

Why did the government enter into the SCA in the first place? What did it hope to accomplish? Knowing the objectives up front helps you know how to judge whether the government's intentions were accomplished.

SCAs sometimes obligate a government to guarantee debt or revenues of the operator or to provide services to the operator, such as security or sanitation. What liabilities did the government recognize relative to its obligations under the SCA? How much will it cost the government to fulfill those obligations?

LIABILITIES

Information about most of the liabilities in a government's financial statements—such as accounts payable, short- and long-term debt, and retirement benefit obligations—can be found in the notes.

WHAT'S AHEAD?

- WHO DO GOVERNMENTS OWE MONEY TO?
- DID A GOVERNMENT BORROW IN THE SHORT RUN? WHY?

Payables

As it does with receivables (refer to Figure 11), a government may aggregate its accounts payable on the face of the statement of net position and then disclose the significant components of that payables amount in a note. (See Figure 14.) In fact, some governments present a combined disclosure of both receivables and payables. However, the types of payables a government has may be less varied than its receivables and, therefore, it may present sufficient detail on the statement of net position. If that is the case, it may not need to present a note disclosure.

The table in Figure 14 is arranged like the receivables disclosure in Figure 11. The types of payables—including vendors payable, salaries and benefits payable, and accrued interest payable—are shown at the top, with the government's funds shown on the left-hand side. (Alternatively, a government might put the payables in the rows and the funds in the columns.)

Figure 14: Salaries and benefits payable for the wastewater function were $289,000.

What can you do with payables information?

This note disclosure allows you to identify, in general terms, who a government owes money to. The organization of the payables by fund may help you to identify the particular activities or services these liabilities are related to. As with receivables, information about payables is important for understanding a government's liquidity.

What bills are coming due that the government will need to have resources available to pay? How do these payments compare with amounts it is owed? The additional detail in this note can help you to seek answers to further questions: When is the government expected to pay on these different types of liabilities? Are some more flexible than others?

Payables also can be tracked over time. If compared with relevant expenses (salaries payable divided by salaries expense, for example), you can assess whether these payable amounts are growing or shrinking, similar to the manner in which receivables can be analyzed. (See financial efficiency ratios in Part Fourteen.) Are particular payables growing or shrinking faster than others? Could this mean that a government is paying its bills slower? What does this say about its financial health? In this way, tracking payables may highlight potential issues about which you can seek further clarification from the government.

For example, a state government's ratio of grants payable to local governments divided by grant expense might be 10.9 percent. The lower this ratio, the less the state still owes relative to the total amount it is supposed to pay. If this ratio were to rise over time, it might indicate that the state is having greater difficulty making its grant payments. Alternatively, the office that processes grant payments may be understaffed and, therefore, unable to process requests from local governments for grant payments as quickly as it has in the past.

Figure 14. Payables Note Disclosure

Payables at June 30, 2017, for the Town of Lakeville Green were as follows:

	① Vendors	Salaries and Benefits	Accrued Interest	Other	Total Payables
Governmental activities:					
General	$ 3,892,000	$ 3,651,000	$ —	$ 415,000	$ 7,958,000
Gas tax	536,000	—	—	—	536,000
Community redevelopment	4,328,000	11,000	—	—	4,339,000
Other governmental	561,000	51,000	—	75,000	687,000
Internal service	1,197,000	204,000	2,169,000	—	3,570,000
Reconciliation of balances in fund financial statements to government-wide financial statements	—	—	1,681,000	—	1,681,000
Total—governmental activities	$ 10,514,000	$ 3,917,000	$ 3,850,000	$ 490,000	$ 18,771,000
Business-type activities:					
Wastewater	$ 6,523,000	$ 289,000	$ 3,525,000	$ 65,000	$ 10,402,000
Solid waste	870,000	132,000	—	—	1,002,000
Other proprietary	1,490,000	196,000	523,000	—	2,209,000
Total—business-type activities	$ 8,883,000	$ 617,000	$ 4,048,000	$ 65,000	$ 13,613,000

Figures 13 and 14 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

As with the receivables ratios, you would need to pursue the matter further with the government to determine the causes of changes over time, but the payables ratios give you a heads up that the issue may require further exploration.

Short-Term Debt

Government revenues often do not come in evenly throughout the year, and the timing of revenue collection often does not match when a government's bills are due to be paid. In order to match up cash flows during the year, a government may engage in short-term borrowing—raising cash at one point in the year to pay bills, and repaying it later in the year when taxes and other revenues are collected. Short-term borrowing most often takes the form of a government selling notes to the public. Notes "anticipate" the receipt of a particular type of revenue—investors buy them from a government and are repaid, with interest, typically in less than a year.

Because short-term debt usually is repaid before the end of the fiscal year, there typically is no short-term debt outstanding shown in the financial statements. Consequently, it is difficult to tell if a government engaged in short-term borrowing during the year. If it did, it presents a note disclosure of its borrowing activity, including notes it sold, lines of credit, and similar loans. The government shows the amount of short-term debt (if any) outstanding at the beginning of the year, new short-term debt issued, repayments, and the ending balance (if any). (See Figure 15.) The note disclosure also should explain the purpose for which the debt was issued.

Figure 15. Short-Term Debt Note Disclosure

The City issues tax anticipation notes in advance of property tax collections, depositing the proceeds in its general fund. These notes are necessary because the City's payments to the school system and other local agencies are made on January 1 and July 1, whereas tax collections are received shortly before their April 1 and October 1 due dates.

Short-term debt activity for the year ended June 30, 2017, was as follows (amounts in thousands):

①	Beginning Balance	Issued	Redeemed	Ending Balance
Tax anticipation notes	$ 0	$ 11,000	$ (11,000)	$ 0

Figure 15 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

What can you do with short-term debt information?

This note disclosure will let you know whether a government borrowed short term and the reasons why it did so. You also can tell how much it borrowed and whether any short-term debt remained unpaid as of the end of the year. You might track the amount borrowed short term over several years by dividing the total short-term borrowing during the year by total expenses. Growth over time in that percentage could be a sign that the government may be encountering financial difficulties or an economic downturn. That would be your cue to investigate further.

WHAT'S AHEAD?

- WHAT TYPES OF LONG-TERM DEBT DOES A GOVERNMENT HAVE?
- HAS ITS OUTSTANDING DEBT GROWN?
- WHAT IS THE IMPACT OF DEBT REFUNDINGS?
- IS A GOVERNMENT RESPONSIBLE FOR SPECIAL ASSESSMENT DEBT?

Long-Term Liabilities

For its long-term liabilities—bonds and other debts generally paid off over a period longer than a year—a government prepares a note disclosure similar to the changes in capital assets note. (See Figure 16.) The note is arranged similarly: governmental and business-type activities are shown separately, and major categories of long-term liabilities are listed for each. The list of liabilities begins with outstanding bonds, loans, and other long-term debt instruments, and also includes other long-term liabilities such as compensated absences and claims and judgments. The first four columns show:

- How much was owed for each type of liability *at the beginning of the year*
- New liabilities incurred *during the year* (additions)
- Amounts paid *during the year* (reductions), and
- Amounts still outstanding *at the end of the year.*

The right-hand column then shows the portion of the total debt outstanding at the end of the year that is due to be repaid *within the next year.* The note also identifies the funds in which the repayment of those liabilities has been reported.

Figure 16: $19,800,000 of redevelopment agency bonds were issued during the year for governmental activities. Repayment of water and sewer debt amounted to $2,178,000.

It should be noted that this disclosure generally does not include all of a government's long-term liabilities. Retirement benefit liabilities do not have to be included because governments are required to present significant disclosures specifically about those liabilities elsewhere in the notes. (See the discussion later in Part Five.) Consequently, a government may include pension and OPEB liabilities in this disclosure but they typically do not.

What can you do with information about changes in long-term liabilities?

The central point of this disclosure is to tell you whether a government's long-term liabilities (other than for retirement benefits) increased or decreased over the past year and why. Even if you located the outstanding amount for the end of the previous year, you would not be able to determine what caused the long-term liabilities to be greater or less than before. This note disclosure shows how much new debt was issued and the amount of other long-term liabilities incurred, as well as how much of each kind of liability was repaid. If this note disclosure is examined in several consecutive financial reports, you can compare the amount of new debt issued to see whether it is growing or shrinking, or whether an unusually large liability has been incurred. The trends you see might lead you to ask further questions about the causes of the changes, such as a government's capital investment activity.

Figure 16. Long-Term Liabilities Note Disclosure

Long-term liability activity for the year ended December 31, 2017, was as follows (in thousands):

	Beginning Balance	② Additions	③ Reductions	① Ending Balance *	④ Amounts Due within One Year
GOVERNMENTAL ACTIVITIES					
Bonds and notes payable:					
General obligation debt	$ 32,670	$ 3,061	$ (4,404)	$ 31,327	$ 2,729
Revenue bonds	14,485	—	(1,000)	13,485	1,040
Redevelopment agency bonds	14,965	19,800	(540)	34,225	1,300
Special assessment bonds	—	3,100	—	3,100	92
Equipment note	1,203	—	(954)	249	249
Less deferred amount on refundings	—	(3,409)	341	(3,068)	—
Total bonds and notes payable	63,323	22,552	(6,557)	79,318	5,410
Other liabilities:					
Compensated absences	5,537	2,744	(2,939)	5,342	2,138
Claims and judgments ⑤	8,070	2,669	(2,864)	7,875	1,688
Total other liabilities	13,607	5,413	(5,803)	13,217	3,826
Governmental activities long-term liabilities	$ 76,930	$ 27,965	$ (12,360)	$ 92,535	$ 9,236

* Payments on the bonds and notes payable that pertain to governmental activities are made by the debt service funds except for the equipment note, which is being repaid directly from the telecommunications internal service fund. (See Notes Y and Z.) The compensated absences liability attributable to governmental activities will be liquidated by several governmental and internal service funds (Note X). The claims and judgments liability will generally be liquidated through the casualty insurance internal service fund (Note W).

	Beginning Balance	Additions	Reductions	⑥ Ending Balance	Amounts Due within One Year
BUSINESS-TYPE ACTIVITIES					
Bonds and notes payable:					
Water and sewer debt	$ 56,975	$ 3,600	$ (2,178)	$ 58,397	$ 3,944
Parking facilities debt	21,567	1,029	(410)	22,186	360
Less deferred amount on refundings	(1,207)	(1,329)	254	(2,282)	—
Total bonds and notes payable	77,335	3,300	(2,334)	78,301	4,304
Compensated absences ⑦	572	1,286	(1,250)	608	122
Business-type activities long-term liabilities	$ 77,907	$ 4,586	$ (3,584)	$ 78,909	$ 4,426

Figure 16 Notes

① NOTE: These amounts have been rounded to thousands of dollars, whereas the amounts in Figure 1 are in whole dollars.

② Additions predominantly are the issuance of new bonds and notes, new claims and judgments, and additional accruals of compensated absences.

③ Reductions predominantly are repayments of debt, payments against outstanding claims and judgments, and compensation of departing employees.

④ The numbers in this column are referred to in the statement of net position as the *current portion of long-term obligations.* These amounts are due to be repaid during fiscal year 2018.

⑤ Claims and judgments might include, for instance, pending insurance claims and legal judgments.

⑥ The amounts in this column are included in the statement of net position (see Figure 1). However, the totals are different because this disclosure generally does not include the net pension liability and net OPEB liability (see the next section on pensions and OPEB), but the long-term liability totals in the financial statements *do* include them.

⑦ The compensated absences item represents unused vacation and other leave time for which employees will be compensated when they retire or leave the government.

Debt refundings

A **DEBT REFUNDING** typically involves selling new debt and using the proceeds to repay existing debt. (Sometimes governments use existing resources rather than selling new debt.) Governments usually do this to replace higher interest debt with lower interest debt and, thereby, reduce annual debt service payments. A government also may refund debt in order to stretch out or rearrange its payment schedule or to eliminate restrictions connected with existing debt.

Debt refundings take two forms. When the proceeds of the new debt are used to repay the old debt right away, it is a **CURRENT REFUNDING.** By contrast, the proceeds of an **ADVANCE REFUNDING** are placed with an escrow agent and invested, and the regular debt service payments are made from the proceeds in escrow. (It should be noted that the federal tax changes signed into law in December 2017 appear to have eliminated the ability to advance refund debt beginning in 2018.) Occasionally, an advance refunding may take the form of a **CROSSOVER REFUNDING,** in which the escrowed proceeds do not begin to repay the refunding bonds until a specific future date. Prior to that date, the revenue stream repaying the original debt (or another revenue stream) is used to repay the refunding bonds.

Under a current refunding, the old debt has been repaid and, therefore, the liability is removed from the financial statements. Under an advance refunding, the debt normally is considered "defeased." **DEFEASANCE** means that either the debt has been *legally* satisfied based on the provisions of the original debt issuance or the debt has been satisfied *in substance* because the proceeds of the new bonds have been used to acquire qualified securities that have been placed with the escrow agent and are not

available to the government. The liability related to debt that is defeased legally or in substance also is removed from the financial statements.

- If a government engages in an advance refunding, it presents a note disclosure that:
- Describes the transaction
- Identifies the difference between the cash flows for debt service under the old bonds and the refunding bonds, and
- Reports the economic gain or loss from the transaction.

(To understand what an economic gain or loss is, see **Upon further review…the time value of money** on page 86.) In subsequent years, the note disclosure for debt defeased in substance reports the amount of defeased debt still outstanding.

The first paragraph of the illustrative note in Figure 17 contains the description of the transaction. In the second paragraph, you learn that the difference in the debt service payments is $6.4 million and the economic gain is $2.9 million.

Figure 17. Advance Refunding Note Disclosure

①

On March 31, 2017, Jerilyn County issued $42.9 million in general obligation bonds with an average interest rate of 3.5 percent to advance refund $35 million of outstanding 2007 Series bonds with an average interest rate of 5.1 percent. The net proceeds of $41.3 million (after payment of $1.6 million in underwriting fees, insurance, and other issuance costs) plus an additional $1.8 million of 2007 Series sinking fund monies were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 2007 Series bonds. As a result, the 2007 Series bonds are considered to be defeased, and the liability for those bonds has been removed from the government-wide statement of net position.

The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $8.1 million. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2042 using the effective-interest method. The County completed the advance refunding to reduce its total debt service payments over the next 25 years by $6.4 million and to obtain an economic gain (difference between the present values of the old and new debt service payments) of $2.9 million.

② ③

Figure 17 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② The reacquisition price equals the amount of old bonds outstanding plus whatever premium the government must pay to call the bonds.

③ The effective interest method is an approach to amortizing or allocating costs over multiple years.

What can you do with information about debt refundings? If a government has engaged in a refunding, the first thing you may want to know is why. The second question you may ask is, did it save money or cost money? Although issuing lower interest debt to replace higher interest debt should reduce annual debt service costs, all other considerations being equal, refundings that change payment schedules could reduce or *increase* debt service payments and result in either an economic gain or loss. For example, it is not uncommon during difficult financial times for governments to refund debt in order to produce short-term savings by extending the repayment schedule or shifting payments to later years. Depending on the terms of the refunding bonds, these changes could increase the present value cost of the government's debt, resulting in an economic loss.

These disclosures are important because they highlight the consequences of the refunding. If a refunding takes place, the note will tell you the particulars of the transaction and what its financial impact is. Then you can judge for yourself.

Special assessment debt

Sometimes a government may issue debt that is to be repaid with a SPECIAL ASSESSMENT against a specific group of persons or businesses. A common example of such an arrangement is when a residential neighborhood seeks to finance area improvements such as sidewalk repairs, new street lighting, and so on. The residents agree to pay a special assessment that the government collects and uses to repay the debt.

If a government provides a portion of the resources needed to repay SPECIAL ASSESSMENT DEBT above and beyond the special assessment collections, or if it indicates that it will make up the difference in the event special assessment collections are insufficient, it includes the debt in its long-term debt note disclosures and SI. If a government is *not obligated in any manner* for special assessment debt it has issued, the notes (1) disclose the amount of the debt and any related services the government provides (such as collecting the special assessments and conveying them to the bondholders) and (2) make clear that the government is in no way responsible for repaying the debt.

What can you do with information about special assessment debt? Some analysts want to know about all debt issued in a particular government's name. Others might argue, though, that there is no need to be concerned about special assessment debt because the taxpayers paying the special assessment will take care of it. This may, in fact, be true of special assessment debt for which a government has no stated financial commitment whatsoever. However, if the possibility exists that a government might have to step in to pay all or some of the debt service on those bonds, you should have information about it. Consider the special assessment debt that is reported in the illustrative statistical section schedule of pledged-revenue coverage in Figure 40. (This schedule is discussed in the section on debt capacity in Part Six.) In fiscal years 20X2–20X5, the special assessment collections were insufficient to cover the annual debt service payments. Conceivably, that government had to make up the difference with general revenues that were intended to finance public services.

Demand bonds

A demand bond is a type of debt that includes a PUT provision allowing the bondholder to demand, after a given time and with sufficient notice, immediate repayment. Demand bonds are included in the long-term liabilities note disclosures described above and statistical section debt schedules discussed in Part Six. In addition, a government discloses the following information in the notes (see Figure 18):

- A general description of the demand bonds
- Any "standby liquidity agreements" or similar arrangement the government has to ensure that resources are available to redeem any bonds that are "put," and
- A description of the government's "take out" agreement, in which it obtains replacement financing if the redeemed demand bonds cannot immediately be resold, including the debt service requirements if the government takes advantage of the take out agreement.

Figure 18. Demand Bond Note Disclosure

①

Included in long-term debt is $100,000,000 of general obligation demand bonds maturing serially through December 31, 2031, and backed by the full faith, credit, and taxing power of the City. The bonds were issued pursuant to an ordinance adopted by the City Council on July 1, 2006. The proceeds of the bonds were used to (a) refund certain general obligation bond anticipation notes, (b) provide funds for certain capital improvements, (c) establish a bond reserve fund in accordance with the trust agreement, and (d) pay costs incurred to issue the bonds. The redemption schedule for these bonds is included in the bond redemption schedule in Note X.

The bonds are subject to purchase on the demand of the holder at a price equal to principal plus accrued interest on three days' notice and delivery to the City's remarketing agent, John Doe and Company. The remarketing agent is authorized to use its best efforts to sell the repurchased bonds at a price equal to 100 percent of the principal amount by adjusting the interest rate.

Under an irrevocable letter of credit issued by ABC Bank, the trustee or the remarketing agent is entitled to draw an amount sufficient to pay the purchase price of bonds delivered to it. The letter of credit is valid through December 31, 2031, and carries a variable interest rate equal to the difference between the institution's prime lending rate (currently 12 percent) and the rate payable on the bonds.

If the remarketing agent is unable to resell any bonds that are "put" within six months of the put date, the City has a take out agreement with ABC Bank to convert the bonds to an installment loan payable over a five-year period bearing an adjustable interest rate equal to the bank's prime lending rate. The take out agreement expires December 31, 2031. If the take out agreement were to be exercised because the entire issue of $100,000,000 of demand bonds was put and not resold, the City would be required to pay $27,740,973 a year for 5 years under the installment loan agreement assuming a 12 percent interest rate.

The City is required to pay to the ABC Bank an annual commitment fee for the letter of credit of 1 percent of the outstanding principal amount of the bonds, plus 124 days of interest at an interest rate of 12 percent unless subsequently changed. The City has paid a take out agreement fee of $125,000 (one-eighth of 1 percent of $100,000,000) to ABC Bank. In addition, the remarketing agent receives an annual fee of one-eighth of 1 percent of the outstanding principal amount of the bonds.

Figure 18 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

What can you do with demand bond information? The primary purposes of these disclosures are to let you know (1) whether a government has bonds that it might have to repay sooner than their ultimate maturity and (2) whether steps have been taken to provide the government with the liquidity it needs to make those payments and to replace any of the long-term financing provided by the bonds. Essentially, you want some assurance that, in an effort to lower its borrowing costs, the government has not inadvertently exposed itself to greater costs related to servicing the put provisions. The disclosures should help you to understand what it costs to arrange for standby liquidity arrangements, take out agreements, and the other administrative requirements of issuing demand bonds.

WHAT'S AHEAD?

- WHAT COMPLEX FINANCIAL INSTRUMENTS HAS A GOVERNMENT ENTERED INTO?
- WHAT RISKS ARE ASSOCIATED WITH THESE TRANSACTIONS?

Derivatives

A **DERIVATIVE** is a financial instrument or a transaction that a government enters into that is based on some other instrument or agreement, such as an investment or outstanding debt. The value of the derivative is predicated on the performance of the underlying instrument or agreement. For example, the payments from the derivative might increase as interest rates rise on the underlying liability, or payments might decrease as the liability's interest rates fall. Although some derivatives are intended for investment purposes, some derivatives that governments engage in are for the purpose of hedging against (protecting the government from) uncertainty and future cost increases.

Governments enter into derivatives for at least four reasons:

1. Governments may intend derivatives to be *hedges against risk*. This type of derivative is an attempt to significantly reduce a specific financial risk that a government may be exposed to, such as the risk of increasing costs for fuel and other commodities.
2. Some governments attempt to *lower their borrowing costs* by entering into a derivative in connection with debt they issue.
3. Some governments engage in derivatives that are investments—governments are trying to *generate income,* as they would by buying other types of investments.
4. Some governments enter into derivatives to *manage their cash flows*. These derivatives may include an up-front cash payment to the government from the other party. The payment arrangements or

terms of the derivative agreement essentially provide for the repayment of the up-front cash; in other words, this kind of derivative is a form of borrowing, like a loan.

The most common derivative for governments is the **INTEREST RATE SWAP**. If a government has **VARIABLE-RATE DEBT**—debt with an interest rate that fluctuates with market conditions—it may wish to protect itself against the possibility that interest rates will rise in the future (which would increase its debt service costs). With an interest rate swap, a government essentially locks in a fixed rate, as if it had issued **FIXED-RATE DEBT** in the first place. In simple terms:

- A government arranges to pay fixed, unchanging amounts to an external party on basically the same schedule as the variable-rate debt.
- In return, the other party agrees to pay the government a variable amount that is equal to the interest the government must pay on the variable-rate debt.
- The only payment actually made is the *net* difference between the agreed upon fixed and variable payments (fees are sometimes paid as well)—if the fixed amount is greater, the government pays the net difference; if the variable amount is greater, the other party pays the government the net difference.

If interest rates rise, the government will be protected because it continues to make the same fixed payment, while receiving from the other party an amount intended to be sufficient to pay the higher interest. If interest rates fall, the government's fixed payments end up being greater than what the variable interest payments would have been—however, the government considers this an acceptable price for the assurance that its payments will not rise if interest rates go up.

Other derivatives that governments engage in include **OPTIONS** and **FORWARD CONTRACTS**. An option is the right to buy or sell an asset at a particular price, by a specific date in the future. Some governments enter into option agreements that give them the right to issue bonds at a certain price, without obliging them to do so. Such arrangements resemble a "rate lock" that a home buyer might obtain when arranging mortgage financing. Municipal bonds sometimes include options known as puts and **CALLS**. A put gives the bondholder the right to demand payment at a particular point in time prior to the ultimate maturity of the bond. (See the discussion of demand bonds on page 87.) A call gives a government the right to redeem the bonds at a particular point in time prior to their ultimate maturity.

Forward contracts are agreements to purchase or sell assets in the future at an agreed-upon price. It is not uncommon for governments to enter into forward contracts for commodities such as heating oil in order to hedge against price increases. A school district might want to lock in a price on heating oil in advance; the price likely would be greater than at the time of the agreement, but less than the level the district anticipates or is concerned that the price will rise to. The difference between the cost per gallon the district pays and the cost per gallon on the open market effectively is the price the district is willing to pay to ensure that its heating oil costs do not rise above a certain level.

In general, the fair value of a derivative as of the end of the fiscal year covered by the financial statements will be reported in the statement of net position. Changes in that fair value from one year to the next are reported in the statement of activities (Figure 42) as part of investment income. However, the annual changes in the fair value of a HEDGING DERIVATIVE INSTRUMENT are required to be *deferred*—reported as deferred inflows and deferred outflows. A hedging derivative instrument significantly reduces financial risk by substantially offsetting the changes in cash flows or fair values of the item the derivative is associated with. (For more about the characteristics of a hedging derivative instrument, see **By the numbers…how a hedging derivative instrument is identified** on pages 96 and 97.) Hedging derivative instruments begin with zero fair value; the fair value subsequently may rise or fall but, if the derivative reaches its maturity date as planned, its fair value will return to zero. Deferring the increases and decreases in the derivative's fair value helps to avoid reporting investment income that never actually comes to fruition.

Deferral of changes in fair value generally will last until the transaction involving the hedged item ends. However, if something happens prior to the expected conclusion of the hedged transaction to cause the derivative agreement to be terminated, or if the hedge ceases to be effective (that is, it no longer significantly reduces risk), the accumulated gains or losses of fair value (the deferred inflows and outflows, respectively), if any, will be added to or netted from investment income in the statement of activities.

Governments with derivatives present a note disclosure that divides the derivatives among those related to governmental activities, BTAs, and fiduciary funds. (See Figure 19.) Within each of those three groups, the derivatives are sorted into (1) hedging derivative instruments (distinguishing between hedges of fair value and hedges of cash flows) and (2) investment derivative instruments. Under those two categories, individual derivative instruments are totaled by type (interest rate swaps, forward contracts, and so on), and governments present the following information about them:

- NOTIONAL AMOUNT (that is, the amount—stated in dollars, shares, gallons, and so on—on which payments depend, similar to the principal amount of a loan)
- Fair value as of the date of the financial statements and the locations in the financial statements where it is reported (this disclosure is helpful because the amounts are aggregated in the financial statements)
- Changes in fair value during the year and the locations in the financial statements where those changes are reported
- The fair value of derivatives that were reclassified from hedging derivative instruments to investment derivative instruments during the year because they no longer meet the criteria to be reported as hedging derivative instruments
- The amount removed from the deferred inflows and deferred outflows in the financial statements and reported in investment income during the year (for instance, because a derivative is terminated).

Governments provide additional information about their *hedging* derivative instruments. The information includes:

- An explanation of a government's objective for entering into the hedging derivative instrument and how it plans to achieve that objective
- Significant terms of the derivative, such as:
  - Notional amount
  - The indexes or interest rates it is based on, including any limitations on the impact that changes in the indexes or rates can have on the derivative
  - Options embedded in the derivative
  - Starting and ending dates, and
  - The amount of cash that changed hands, if any, when the derivative was initiated
- If the item being hedged is debt, the government discloses the net cash flows of the hedging derivative. (See Figure 20.)

Figure 19. Note Disclosure of Summary Derivatives Information

①	Changes in Fair Value		② Fair Value at June 30, 2017		
	Classification	Amount	Classification	Amount	Notional
Governmental activities					
Fair value hedges:					
Receive-fixed interest rate swap	Deferred inflow	③ $ (277)	Debt	$ 1,572	$ 30,000
Cash flow hedges:					
Pay-fixed interest rate swap	Deferred outflow	$ (143)	Debt	$ (1,330)	$ 84,000
Rate cap	Deferred inflow	$ 28	Debt	$ 377	$ 1,000
Investment derivatives:					
Pay-fixed interest rate swap	Investment revenue	$ 1,277	Investment	$ (1,277)	$ 18,000
Business-type activities					
Cash flow hedges:					
Pay-fixed interest rate swap	Deferred inflow	$ (548)	Debt	$ 4,236	$ 37,000
Commodity forward	Deferred inflow	$ (111)	Derivative instruments	$ 111	1,000 MMBTUs
Fiduciary funds					④
Investment derivatives:					
Foreign currency forward	Investment revenue	$ 721	Investment	$ (721)	£20,000

Figure 19 Notes

① NOTE: This is a different government from Local City and the governments in Figures 20 and 21. Therefore, this illustration does not tie to the financial statements or those figures.

② The fair value of the derivatives at the *beginning* of the period can be determined by subtracting the change in fair value in this disclosure from the fair value as of the end of the period.

③ The dollar amounts in this disclosure are stated in thousands.

④ The notional amount is stated in the relevant terms of the derivative and underlying instrument, such as dollars or commodities. The commodity forward contract here, involving the purchase of fuel, is stated in millions of BTUs (MMBTUs).

Figure 20. Note Disclosure of Hedging Derivatives Net Cash Flows

Fiscal Year Ending June 30	Principal	② Interest	Hedging Derivatives, Net	Total
2018	$ 6,000	$ 7,786	$ (1,253)	$ 12,533
2019 ①	10,000	7,525	(1,211)	16,314
2020	27,000	7,090	(1,141)	32,949
2021	33,000	5,916	③ (952)	37,964
2022	15,000	4,480	(721)	18,759
2023–2027	29,000	19,140	(3,080)	45,060
2028–2032	15,000	12,385	1,475	28,860
2033–2037	14,000	9,570	(528)	23,042
2038–2040	30,000	6,310	(300)	36,010
Total	$ 179,000	$ 80,202	$ (7,711)	$ 251,491

Figure 20 Notes

① NOTE: This is a different government from Local City and the governments in Figures 19 and 21. Therefore, this illustration does not tie to the financial statements or those figures.

② The dollar amounts in this disclosure are stated in thousands.

③ The amounts in parentheses indicate that the government is in a liability position with respect to these derivatives. In other words, the government would have to make a net payment to the counterparty on these derivatives if they were terminated on this date.

Figure 21. Note Disclosure of Hedging Derivatives Risks

① ②

Credit risk. The City is exposed to credit risk on hedging derivative instruments that are in asset positions. To minimize its exposure to loss related to credit risk, it is the City's policy to require counterparty collateral posting provisions in its non-exchange-traded hedging derivative instruments. These terms require full collateralization of the fair value of hedging derivative instruments in asset positions (net of the effect of applicable netting arrangements) should the counterparty's credit rating fall below AA as issued by Fitch Ratings and Standard & Poor's or Aa as issued by Moody's Investors Service. Collateral posted is to be in the form of U.S. Treasury securities held by a third-party custodian. The City has never failed to access collateral when required.

It is the City's policy to enter into netting arrangements whenever it has entered into more than one derivative instrument transaction with a counterparty. Under the terms of these arrangements, should one party become insolvent or otherwise default on its obligations, close-out netting provisions permit the nondefaulting party to accelerate and terminate all outstanding transactions and net the transactions' fair values so that a single sum will be owed by, or owed to, the nondefaulting party.

The aggregate fair value of hedging derivative instruments in asset positions at June 30, 2017, was $7,308,000. This represents the maximum loss that would be recognized at the reporting date if all counterparties failed to perform as contracted. This maximum exposure is reduced by $1,572,000 of collateral held and $2,342,000 of liabilities included in netting arrangements with those counterparties, resulting in a net exposure to credit risk of $3,394,000.

Although the City executes hedging derivative instruments with various counterparties, three contracts comprising approximately 86 percent of the net exposure to credit risk are held with one counterparty. That counterparty is rated AAA/Aaa.

Interest rate risk. The City is exposed to interest rate risk on its interest rate swap. On its pay-variable, received-fixed interest rate swap, as LIBOR increases, the City's net payment on the swap increases. Alternatively, on its pay-fixed, receive-variable interest rate swap, as LIBOR or the SIFMA swap index decreases, the City's net payment on the swap increases.

Basis risk. The City is exposed to basis risk on its pay-fixed interest rate swap and rate cap hedging derivative instruments because the variable-rate payments received by the City on these hedging derivative instruments are based on a rate or index other than interest rates the City pays on its hedged variable-rate debt, which is remarketed every 30 days. As of June 30, 2017, the weighted-average interest rate on the City's hedged variable-rate debt is 1.05 percent, while the SIFMA swap index rate is 0.82 percent and 67 percent of LIBOR is 1.15 percent.

The City is exposed to basis risk on its commodity forward contract because the expected commodity purchase being hedged will price based on a pricing point (Texas Trunk) different than the pricing point at which the forward contract is expected to settle (Henry Hub). At June 30, 2017, the Texas Trunk price is $2.89 per MMBTU and the Henry Hub price is $2.94 per MMBTU.

Termination risk. The City or its counterparties may terminate a derivative instrument if the other party fails to perform under the terms of the contract. In addition, the City is exposed to termination risk on its receive-fixed interest rate swap scheduled to mature in September 2021 because the contract provides the counterparty with the option to terminate the contract each September 30, commencing September 30, 2016. The City is exposed to termination risk on its rate cap because the counterparty has the option to terminate the contract if the SIFMA swap index exceeds 5 percent. If at the time of termination, a hedging derivative instrument is in a liability position, the City would be liable to the counterparty for a payment equal to the liability, subject to netting arrangements.

Rollover risk. The City is exposed to rollover risk on hedging derivative instruments that are hedges of debt that mature or may be terminated prior to the maturity of the hedged debt. When these hedging derivative instruments terminate or, in the case of a termination option, if the counterparty exercises its option, the City will be re-exposed to the risks being hedged by the hedging derivative instrument. The City is exposed to rollover risk on the pay-variable, receive-fixed interest rate swap scheduled to mature in September 2021. With this swap, the counterparty has the option to terminate the contract each September 30, commencing September 30, 2016, while the hedged debt matures in September 2021. The City also is exposed to rollover risk on the pay-fixed, receive-variable interest rate swap scheduled to mature in February 2018 because the hedged debt is scheduled to mature in February 2023.

Figure 21 Notes

① NOTE: This is a different government from Local City and the governments in Figures 19 and 20. Therefore, this illustration does not tie to the financial statements or those figures.

② Derivatives in an asset position pose credit risk because the government would be *owed* money if they were terminated on this date. Derivatives in a liability position do not expose the government to credit risk because the government would owe money to the counterparty.

Risks associated with derivatives

A government's note addresses the risks to which the hedging derivatives expose it. (See Figure 21.) As with investments, those may be risks of loss; alternatively, they may be a risk of losing the effectiveness of the derivative. For example, if a government engages in an interest-rate swap to protect itself from rising interest on its variable-rate debt, but the swap is terminated before the debt is fully repaid, the government loses its protection. The risk of such adverse results from a derivative ending early is called TERMINATION RISK. A government discloses any terminations that occurred during the year, dates that its remaining derivatives may be terminated, and unusual provisions for termination.

Figure 19: The change in fair value of the governmental activities' investment derivatives was $1,277,000.

BASIS RISK is the product of the variable interest rates on a derivative and the underlying instrument being based on different indexes (for example, one might be based on a percentage of the London Interbank Offered Rate [LIBOR] and the other on the Securities Industry and Financial Markets Association Rate [SIFMA]). Changes in the relationships between two different indexes could adversely affect the value of the derivative. A government discloses the derivative's payment terms and any payment terms of the associated debt.

ROLLOVER RISK exists when the derivative's maturity is shorter than the associated debt's maturity; for instance, an interest-rate swap might have a 10-year term, but the variable-rate debt matures in 30

years. Consequently, after the derivative ends, the government no longer is protected against rising interest rates and may not be able to "roll over" into a new derivative with similar terms.

A government discloses the maturity of the derivative and the subsequent maturity of the associated debt. MARKET-ACCESS RISK is the chance that a government will not be able to issue debt or that doing so will become more expensive. A government will indicate if it is exposed to the risk of being unable to borrow.

Credit risk, interest rate risk, and foreign currency risk also may be issues for derivatives, as they may be for investments. If a derivative exposes a government to credit risk, it reports:

- The credit rating of the firm involved in the transaction
- The maximum potential loss if the firm fails to fulfill its obligations
- The collateral or other security supporting the derivatives, and
- Significant concentrations of credit risk with a particular firm or group of firms.

If a government is exposed to interest rate risk by a derivative, it describes the terms of its derivatives that increase its exposure to interest rate risk. Lastly, a government discloses the U.S. dollar balances of derivatives that expose it to foreign currency risk, organized by type of currency and type of derivative. Like the investment risk disclosures, this information is disclosed only if the government is exposed to the specific type of risk because of its derivatives.

What can you do with derivatives information?

As with investments, it is important to know when a government has been exposed to risk. Although interest-rate swaps and other forms of hedging against risk can be prudent financial measures, they nonetheless involve risks to which the government might not otherwise be exposed. Furthermore, some derivatives may expose a government to the very risks it was attempting to alleviate. This note disclosure identifies the extent of a government's involvement in derivatives, as well as any manner in which that involvement has increased the government's risk exposure. Based on this information, you can assess the degree of risk to which the transactions expose a government and balance that risk against the potential benefits of the transactions.

Regarding the derivatives themselves, you can tell what types of derivatives a government has entered into and whether its transactions have grown in number or amount over time. The derivatives note will help you to understand whether a government's hedging derivatives are effectively protecting it against the loss of the fair value or cash flows of the debt or other items being hedged. The information disclosed regarding deferred inflows of resources and deferred outflows of resources reflects whether a government is in the position of potentially being owed money by the firm involved in the transaction (deferred inflow) or potentially owing money to the firm (deferred outflow). The disclosure of information about derivatives that are no longer effective hedges can help you distinguish

the portion of investment income related to previously deferred inflows and outflows of resources now being reported in investment income.

WHAT'S AHEAD?

- WHAT FINANCIAL COMMITMENTS ARE RELATED TO A GOVERNMENT'S LEASES?
- HAS A GOVERNMENT ISSUED DEBT ON BEHALF OF OTHER ENTITIES?

Leases

Long-term **CAPITAL LEASES** essentially are borrowings. (See **Upon further review…long-term leases** on page 42.) When a government signs a capital lease, it takes into its possession and has a right to use an asset—property, office space, vehicles, equipment, and so on. In return, it makes payments to the suppliers of the leased items, generally over several years; the government has, in essence, financed the acquisition of the capital asset with a lease instead of bonds or loans. Because of these similarities, the government makes note disclosures that are similar to those for long-term debt.

Capital leases are distinguished from **OPERATING LEASES** in that they closely resemble the purchase of a capital asset financed by long-term borrowing. (See **Upon further review…major changes in lease accounting.**) For instance, just as a government cannot simply walk away from its obligation to repay long-term debt, capital leases cannot be unilaterally canceled. If a lease exhibits one or more of the following characteristics, it is considered a capital lease (all other leases are operating leases):

- The government becomes the owner of the asset when the lease ends
- The government can purchase the asset at a significant discount
- The term of the lease covers 75 percent or more of the remaining useful life of the asset
- The value of the lease is close (greater than 90 percent) to the value of the asset if purchased.

A further consideration relates to what are called **FISCAL FUNDING CLAUSES.** These are provisions in a lease that allow a government to cancel the lease on an annual basis if funds are not appropriated in the budget to make the lease payments. These clauses appear in some governmental leases because of legal limitations on the ability of those governments to incur long-term debts. The existence of these clauses should not prevent a government from reporting a lease as a capital lease, as long as the possibility of cancellation is remote.

When a government enters into a capital lease, it reports it as a capital asset and balances it with a long-term liability; both are equal to the present value of future minimum lease payments. Over time, the lease is amortized (a process that allocates the cost of the lease over its term, as depreciation does with capital assets) and the liability is reduced by the annual lease payments the government makes. Operating leases (those that do not meet the capital lease criteria) are charged as expenses when they are payable; no capital asset or long-term liability is recorded.

Lease disclosures

If a government has capital leases or NONCANCELABLE OPERATING LEASES, it discloses the amounts of the leases, organized by nature or function, as well as a description of the lease arrangements. The description includes any existing provisions for renewal of the lease, purchase of the asset, or circumstances under which the lease payments would increase. It also mentions any restrictions imposed by the leases. Furthermore, if the government has lease arrangements with other governmental entities, these are specifically disclosed and their features and provisions explained. (Additional disclosures related to minimum future payments under those types of leases are discussed in Part Eight.)

Conduit Debt

Certain debt issued by governments is intended to provide financing for entities that are not a part of the government or one of its component units. Although the government is the issuer of this CONDUIT DEBT, it is not obligated to provide resources to repay the debt—repayment of the debt is the obligation of the entity on whose behalf the debt was issued. For this reason, many governments do not report conduit debt among their liabilities, although they are allowed to.

Conduit debt often is issued on behalf of private companies for economic development purposes. If a government has conduit debt, it presents a note disclosure with the following information:

- A general description of its conduit debt arrangements
- The total amount of conduit debt outstanding, and
- A clear statement that the government is not responsible for repaying the debt.

As with special assessment debt, you may wish to obtain a sense of all of the debt that has a particular government's name on it, even if the debt is expected to be repaid by someone other than the government.

WHAT'S AHEAD?

- WHAT RETIREMENT BENEFITS HAS A GOVERNMENT PROMISED TO ITS EMPLOYEES?
- HOW MUCH DO RETIREMENT BENEFITS COST?
- TO WHAT EXTENT HAS A GOVERNMENT SET ASIDE RESOURCES TO FUND PENSIONS, HEALTH INSURANCE, AND OTHER RETIREMENT BENEFITS?

Pensions and Other Postemployment Benefits

Employees of state and local governments may be compensated in a variety of ways in exchange for their services. In addition to a salary, many employees earn benefits over their years of service that will not be received until after their employment with the government ends through retirement or other

reason for separation. The most common type of these postemployment benefits is a pension. As the name suggests, other postemployment benefits are postemployment benefits *other than pensions*. OPEB generally takes the form of health insurance and dental, vision, prescription, or other healthcare benefits provided to eligible retirees, including in some cases their beneficiaries. It also may include some types of life insurance, legal services, and other benefits.

There are two basic forms of postemployment benefit plans—defined contribution and defined benefit. **DEFINED CONTRIBUTION PLANS** stipulate the *amounts a government has to contribute to a plan member's individual account* each year. The amount of benefits employees will receive when they retire depends only on how much was contributed and the earnings on those contributions when invested. The information that is reported by governments with defined contribution plans is discussed further on page 109.

The descriptions that follow relate to most governments, which participate in one or more **DEFINED BENEFIT PLANS.** For accounting purposes, a defined benefit plan is one that does not meet the definition of a defined contribution plan. Defined benefit plans generally specify the *amount of benefits* to be provided to the employees after the end of their employment.

Defined benefit plans also may be distinguished by how many employers participate in them. As their name indicates, a **SINGLE-EMPLOYER PLAN** involves only one government employer (and its component units, if they participate in the same plan). In a **COST-SHARING MULTIPLE-EMPLOYER PLAN,** governments pool (share) (1) the costs of providing benefits and administering the plan and (2) the assets accumulated to pay benefits. A single actuarial valuation is conducted for the employees of all the participating governments *combined*. In an **AGENT MULTIPLE-EMPLOYER PLAN,** separate accounts are maintained to ensure that each employer's contributions (and those of its employees and other entities on its behalf) are used to provide benefits only for the employees of that government. Individual employers are responsible for benefits associated with their own employees only, and separate actuarial calculations are made for each participating government in the plan. It is like a collection of single-employer plans. However, to take advantage of economies of scale, the cost of administering the plan is shared by the participating governments, and the plan assets generally are pooled for investment purposes.

Costs and obligations related to pensions and OPEB

Governments disclose important information in the notes about the long-term liabilities for pensions and OPEB that they report in the statement of net position. You may be able to see the **NET PENSION LIABILITY (NPL)** or **NET OPEB LIABILITY (NOL)** on the face of the statement, but often they are combined with the other long-term liabilities. Governments disclose the amounts of pension and OPEB liabilities, information about how they are calculated and what caused them to increase or decrease during the year, and much more.

The NPL and NOL are measurements of obligations that a government may satisfy over a very long period. As such, they are very complex measurements that are based on an actuary's estimate or *valuation,* which involves many assumptions, based on historical experience and future expectations, regarding the factors that determine the cost of the benefits that have been earned. These factors may include, but are not limited to, number of employees, average length of employment with the government, trends in compensation levels, life expectancy, trends in healthcare costs, and returns on investments.

In simple terms, the actuary does the following:

- *Projects* the future cash outflows for pensions and OPEB based on the benefit terms and economic and demographic assumptions such as those mentioned above
- *Discounts* the projected cash outflows to their *actuarial present value*—their estimated value today, and
- *Allocates* the actuarial present value generally between past years of service and future years of service.

The portion of the actuarial present value allocated to prior years of employment is called the TOTAL PENSION LIABILITY (TPL) or TOTAL OPEB LIABILITY (TOL). This basically is the total amount owed for pensions and OPEB that already have been earned. For accounting purposes, any money a government has set aside in a trust to pay pension or OPEB benefits (referred to as the FIDUCIARY NET POSITION of the plan) offsets the TPL or TOL. The excess of the TPL or TOL over the fiduciary net position is the NPL or NOL. (See **Upon further review…special funding situations** on page 100.)

Although the vast majority of governments provide pensions by putting assets in a trust that meets certain criteria, far fewer do so for OPEB (this may be because state law does not allow them to create such trusts, or because they choose not to set money aside in advance for OPEB). (See **Upon further review…criteria for pension and OPEB trusts** on page 105.) If a government provides OPEB, but not through such a trust, the amount it reports in the statement of net position will be the TOL instead of the NOL. This is because there are no OPEB plan assets in a trust that meets the criteria to offset the TOL.

The annual cost for pensions and OPEB is reported as expense in the statement of activities. The amount of expense is based on the change in the NPL or NOL during the year. The items that generally cause the NPL or NOL to increase the most in any given year are included in pension or OPEB expense right away—SERVICE COST and interest on the total liability. Service cost essentially is the cost of new benefits earned by a government's employees during the year for which the liability is measured. If a government changes the benefit terms of its pension or OPEB plan in a way that causes the NPL or NOL to increase or decrease, that change in the liability is reported in pension expense immediately as well. For example, this year, a government increases the retirement age for newly hired employees—consequently, they will have to work longer before they can retire and receive benefits,

which would reduce projected benefit payments and, therefore, the pension or OPEB liability. The amount by which the NPL (NOL) is reduced would be subtracted from pension (OPEB) expense this year. On the other hand, if a government provides a cost-of-living increase that is not required by the terms of the pension plan, normally the liability would increase and the amount of the increase would be added to pension expense this year.

Other common causes of increases and decreases in the NPL (NOL) initially are reported in the statement of net position as deferred outflows of resources or deferred inflows of resources and then added to or subtracted from expense, respectively, over multiple years. There are three such causes—changes in assumptions about economic and demographic factors, differences between assumed and actual economic and demographic factors, and differences between assumed and actual returns on plan investments. (See **Upon further review…deferrals related to pensions and OPEB**.)

Costs and obligations for cost-sharing governments. The actuarial valuation for a cost-sharing multiple-employer plan generally is conducted for all of the members of the plan combined. That produces an overall NPL or NOL, pension or OPEB expense, and pension- or OPEB-related deferrals for *all of the participating governments in the aggregate*. If a government participates in a cost-sharing plan, it has to determine its proportionate share and report it in its financial statements.

To determine the amounts it should report in its financial statements, a government multiplies the aggregate NPL or NOL, expense, and deferrals by its proportion. The proportion is based on contributions made to the plan. In other words, cost-sharing governments compare the money they contribute to the plan with the contributions made by all participating governments and other entities. For instance, a county might total its contributions to the plan for the past year ($5 million) and divide them by the total contributions of all participating governments and other entities ($100 million) to determine that its proportion is 5 percent.

That proportion is applied to the aggregate liability, expense, and deferrals. For example, the aggregate NPL for all participants in the pension plan is $500 million and the county's proportion is 5 percent. Therefore, the county will report a $25 million NPL in its own statement of net position ($500 million times 0.05). In notes to financial statements, the county discloses its proportion and its proportionate share of the NPL or NOL, pension or OPEB expense, and pension or OPEB-related deferrals. It also describes how it determined its proportion.

Descriptive information

Governments disclose certain basic information about their pension and OPEB plans regardless of what type of plan they participate in. The note disclosure (1) identifies the plan and (2) describes the types of benefits provided and the authority under which benefit provisions and obligations to contribute to the plan are established or may be amended. (See Figure 22.) For example, the pension note disclosure might reveal that the pension plan provides retirement, disability, and death benefits

to plan members and their beneficiaries and that a specific section of state law regulates the changing of benefit provisions. The disclosure tells you (3) if the pension or OPEB plan issues its own financial report or if the plan is included in the report of a public employee retirement system or another entity and, if so, (4) how to obtain the report. The note disclosure also (5) reports the required contribution rates of employees and the government.

If a government has a single-employer pension or OPEB plan or participates in an agent multiple-employer plan, its disclosure of basic descriptive information also includes the number of members in its plan. At a minimum, the government shows the number of (1) inactive employees and their beneficiaries who are receiving benefits, (2) inactive employees not yet receiving benefits (perhaps they have not yet reached the required retirement age), and (3) active employees.

Figure 22. Descriptive Note Disclosures about Pensions

General Information about the Pension Plan ① ②

Plan description. Merritt County's defined benefit pension plan, the Merritt Employee Pension Plan (MEPP), provides pensions for all permanent full-time general and public safety employees of the County. MEPP is a single-employer defined benefit pension plan administered by the Merritt Employee Retirement System (MERS). Article 15 of the Regulations of the State grants the authority to establish and amend the benefit terms to the MERS Board of Trustees (MERS Board). MERS issues a publicly available financial report that can be obtained at www.merritt.mepp.gov.

Benefits provided. MEPP provides retirement, disability, and death benefits. Retirement benefits for general employees are calculated as 2 percent of the employee's final 5-year average salary times the employee's years of service. Benefits for public safety employees are calculated as 3 percent of the employee's final 3-year average salary times the employee's years of service. General employees with 10 years of continuous service are eligible to retire at age 60. Public safety employees with 10 years of continuous service are eligible to retire at age 55. General employees may retire at any age after 30 years of service. Public safety employees may retire at any age after 20 years of service. All employees are eligible for non-duty disability benefits after 10 years of service and for duty-related disability benefits upon hire. Disability retirement benefits are determined in the same manner as retirement benefits but are payable immediately without an actuarial reduction. Death benefits equal two times the employee's final full-year salary. An employee who leaves County service may withdraw his or her contributions, plus any accumulated interest.

Benefit terms provide for annual cost-of-living adjustments to each employee's retirement allowance subsequent to the employee's retirement date. The annual adjustments are one-half of the change in the Consumer Price Index, limited to a maximum increase in retirement allowance of 2 percent for general employees and 3 percent for public safety employees.

Employees covered by benefit terms. At June 30, 2017, the following employees were covered by the benefit terms:

Inactive employees and beneficiaries currently receiving benefits	4,002
Inactive employees entitled to but not yet receiving benefits	1,207
Active employees	5,347
Total plan members	10,556

Contributions. Article 15 of the Regulations of the State grants the authority to establish and amend the contribution requirements of the County and active employees to the MERS Board. The Board establishes rates based on an actuarially determined rate recommended by an independent actuary. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The County is required to contribute the difference between the actuarially determined rate and the contribution rate of employees. For the year ended June 30, 2017, the average active employee contribution rate was 7.0 percent of annual pay, and the County's average percent of annual pay, and the County's average contribution rate was 17.74 percent of annual payroll.

Figure 22 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② This illustration of the note disclosure for a government's pension plan would be virtually identical for an OPEB plan.

Information about the measurement of the liability

The next section of the disclosures about pensions and OPEB relates to the measurement of the NPL (or NOL). As noted above, calculating the pension and OPEB liabilities requires making assumptions about what will happen to relevant economic and demographic factors in the future—such as how much salaries will increase, the pace at which healthcare costs will rise, and how long former employees will live and collect benefits. This section of the pension and OPEB notes identifies those assumptions. In Figure 23, you can see that this County government assumes that inflation will be 3.5 percent per year and the investments of the pension plan will average 7.75 percent annually. Governments will not disclose detailed information about life expectancy, because it typically comprises extensive tables of mortality data. They will, however, identify the "mortality tables" that it used.

Figure 23. Pension Liability Measurement Note Disclosure

Net Pension Liability ① ②

The County's net pension liability was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date.

Actuarial assumptions. The total pension liability in the June 30, 2016 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement: ③

Inflation	3.0 percent
Salary increases	4.0 percent, average, including inflation
Investment rate of return	7.25 percent, net of pension plan investment expense, including inflation

Mortality rates were based on the RP-2000 Healthy Annuitant Mortality Table for Males or Females, as appropriate, with adjustments for mortality improvements based on Scale AA. The actuarial assumptions used in the June 30, 2016 valuation were based on the results of an actuarial experience study for the period July 1, 2012–April 30, 2014.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return ④
Domestic equity	46%	5.4%
International equity	21	5.5
Fixed income	26	1.3
Real estate	6	4.5
Cash	1	0.0
Total	100%	

Discount rate. The discount rate used to measure the total pension liability was 7.25 percent. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that County contributions will be made at rates equal to the difference between actuarially determined contribution rates and the employee rate. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability to changes in the discount rate. The following presents the net pension liability of the County, calculated using the discount rate of 7.25 percent, as well as what it would be if calculated using a discount rate that is 1-percentage-point lower (6.25 percent) or 1-percentage-point higher (8.25 percent) than the current rate:

	1% Decrease (6.25%)	Current Discount Rate (7.25%)	1% Increase (8.25%)
County's net pension liability ⑤	$826,928	$751,753	$661,543

Pension plan fiduciary net position. Detailed information about the pension plan's fiduciary net position is available in the separately issued MERS financial report.

Figure 23 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② This illustration of the note disclosure for a government's pension plan would be virtually identical for an OPEB plan.

③ The note for an OPEB plan would include the assumption regarding the healthcare cost trend rate here as well.

④ A *real* rate of return does not include inflation. The assumed inflation rate of 3.0 percent is shown above in the note disclosure, and it is included in the assumed overall investment rate of return of 7.25 percent. To convert the real rates of return for each of these asset classes to amounts that are directly comparable to the overall investment rate of return, add the inflation rate. For instance, adding 3.0 percent to the expected real rate of return of 1.3 percent for fixed income investments produces an expected rate of return of 4.3 percent.

⑤ A lower discount rate produces a larger present value and, therefore, a larger NPL.

With respect to the assumed rate of return, a government does not simply identify the rate. It also explains how it determined the rate. A key part of the explanation is the presentation of the individual rates of return the government expects on the major types of investments the pension or OPEB plan holds. For instance, the County in Figure 23 expects that 46 percent of its pension plan assets will be investments in U.S. companies that will have a return of 5.4 percent (not including inflation).

The information you receive about the assumed rate of return can help you to assess the potential impact of changes in the rate. The implications of that consideration can be significant—if the government's pension plan does not earn as much as it is assuming, it may mean that the government will need to contribute additional money to the plan.

The assumed rate of return also is very important because it serves as the rate for discounting the projected future benefit payments to their value today. Mathematically, the smaller the discount rate

used, the larger the present value today. Because that present value is the basis for the amount reported as a government's pension or OPEB liability, the choice of the assumed rate of return also affects how big the liability is. For example, a lower rate would increase the total liability. Lower investment returns also would reduce the plan's fiduciary net position. Both of those impacts would increase the NPL or NOL that is reported in the statement of net position.

You can get a sense of the impact that changes in the assumed rate of return could have on a government's NPL or NOL by looking at the disclosure in Figure 23 that shows what the liability would be if the discount rate were 1-percentage-point higher and 1-percentage-point lower than the rate the government actually used. If the illustrative government's discount rate were 6.25 percent instead of 7.25 percent, its NPL would increase from almost $752 million to nearly $827 million. On the other hand, if its discount rate were 8.25 percent, the government's NPL would decrease to less than $662 million. Governments present a similar disclosure of the impact on the NOL of its assumption about how much healthcare costs will rise. (See Figure 24.)

Figure 24. Note Disclosure of the Effect of the Healthcare Cost Trend Rate on the Net OPEB Liability

Sensitivity of the net OPEB liability to changes in the healthcare cost trend rate.

The healthcare cost trend rate assumed in the calculation of the new OPEB liability is 9.5 percent for 2018, decreasing 0.5 percentage points per year to an ultimate rate of 5.5 percent in 2026. The following presents the net OPEB liability of the County, as well as what the County's net OPEB liability would be if it were calculated using healthcare cost trend rates that are 1-percentage-point lower (8.5 percent decreasing to 4.5 percent) or 1-percentage-point higher (10.5 percent decreasing to 6.5 percent) than the current healthcare cost trend rates:

	1% Decrease (8.5% / 4.5%)	Current Rate (9.5% / 5.5%)	1% Increase (10.5% / 6.5%)
①			
Net OPEB liability (asset)	$ (35,797,841)	$ 24,528,260	$ 97,780,369

Figure 24 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Information about changes in the net liability

The NPL and NOL increase or decrease each year for a variety of reasons. As mentioned previously, service cost and interest add to the liability each year. Other factors—such as changes in the benefits provided by the plan and changes in the assumptions used to measure the liability—may add to or reduce the amount of the liability. If a government participates in a single-employer or agent multiple-employer plan, it provides a note like the one in Figure 25. This note tells you not just how much the NPL or NOL changed from last year, but *what caused the change*. The note shows you the dollar impact of each factor on (1) the total liability, (2) the fiduciary net position of the plan, and (3) the NPL or NOL (the combination of 1 and 2).

Contributions to the plan from a government and its employees increase the plan's fiduciary net position. (See **Upon further review…contributions after the NPL/NOL is measured** on page 103.) Investment earnings also increase net position, though a loss on investments would reduce net position. The payment of benefits to retirees reduces both the total liability (those amounts are no longer owed) and net position (those assets are no longer held by the plan).

Governments in defined contribution plans

The requirements discussed above apply to a government participating in a defined benefit plan. If a government participates in a defined *contribution* plan, the note disclosures are limited to basic information about the plan and contribution requirements. These include (1) the name of the plan; (2) plan provisions; (3) the contribution rate (in dollars or a percentage of salary) of the government, employees, and others (such as a state government that pays for a portion of a school district's contributions for teachers); (4) the amounts actually contributed by the government and its employees; (5) expense for the year; and (6) the government's liability to the plan, if any.

What can you do with pension and OPEB information?

The first step in understanding retirement benefits is to *identify what benefits a government promises*—various levels of pension income, disability benefits, health insurance coverage, and so on—and *to which employees and other beneficiaries*. What is the basis for determining the amounts of these benefits? For instance, is pension income a function of the final year's salary, or an average of the final three years? Who pays the health insurance premiums, the government or the retirees?

The notes offer insight into the process of *determining how much a government is obligated for and how much it needs to contribute each year to fund that obligation.* First of all, the notes inform you about the basics of a government's pension and OPEB plans: What benefits are provided and to what types of employees? How long do employees have to work to become eligible to receive benefits? How is the amount of benefits determined?

Figure 25. Changes in Net Pension Liability Note Disclosure

Changes in the Net Pension Liability

① ②

	Increase (Decrease)		
	Total Pension Liability (a)	Plan Fiduciary Net Position (b)	Net Pension Liability (a) – (b)
Balances at 6/30/16	$ 2,853,455	$ 2,052,589	$ 800,866
Changes for the year:			
Service cost	75,864	—	75,864
Interest	216,515	—	216,515
Differences between expected and actual experience	(37,539)	—	(37,539)
Contributions—employer	—	79,713	(79,713)
Contributions—employee	—	31,451	(31,451)
Net investment income	—	196,154	(196,154)
Benefit payments, including refunds of employee contributions	(119,434)	(119,434)	—
Administrative expense	—	(3,373)	3,373
Other changes	—	8	(8)
Net changes	135,406	184,519	(49,113)
Balances at 6/30/17	$ 2,988,861	$ 2,237,108	$ 751,753

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended June 30, 2017, the County recognized pension expense of $158,356. At June 30, 2017, the County reported pension-related deferred outflows of resources and deferred inflows of resources from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 33,329	$ 53,995
Changes of assumptions	62,949	—
Net difference between projected and actual earnings on pension plan investments	133,976	—
Total	$ 230,254	$ 53,995

Amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended June 30:	
2018	$ 57,966
2019	86,466
2020	43,069
2021	(1,778)
2022	1,465
Thereafter	(10,929)

Figure 25 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② This illustration of the note disclosure for a government's pension plan would be virtually identical for an OPEB plan.

You can *question the underlying assumptions that went into measuring the NPL and NOL*. All things being equal, a higher assumed rate of return—and thus a higher discount rate—will result in a lower NPL or NOL. However, if the investment earnings turn out to be less than assumed, the plan's future fiduciary net position will be less than expected, which will increase the NPL or NOL and ultimately may require the government to make larger annual contributions to the plan. The amounts a government is reporting for the NPL and NOL are sensitive to the assumptions it made when measuring them—the disclosure of the impacts of increasing and decreasing the discount rate and the healthcare cost rate helps you to understand *how sensitive those measurements are* to two of the most significant factors that go into them.

If a government participates in a single-employer or agent multiple-employer plan, the disclosures will help you to understand what caused the NPL or NOL to increase or decrease. If you see that the net liability has changed significantly as a result of a change in assumptions, you may want to seek further information about the nature of those changes. The notes on pensions and OPEB highlight the nature of significant changes a government has made to its methods and assumptions for measuring the pension and OPEB liabilities. One benefit of being able to distinguish the causes of increases in the NPL or NOL is that you can assess how much of the increase relates to factors within the government's control versus those that it has little or no control over. For instance, the dollar amount by which the NPL or NOL increases or decreases because of changes in the benefits promised to employees is shown separately. You may be interested in how much the liability decreased as a result of benefit changes made by the government as cost-saving measures.

WHAT'S AHEAD?

- WHAT COSTS HAS A GOVERNMENT INCURRED BY OFFERING EARLY RETIREMENT TO EMPLOYEES?
- WHAT ARE THE AMOUNTS OF JUDGMENTS AND CLAIMS AGAINST A GOVERNMENT?
- UNDER WHAT CIRCUMSTANCES MIGHT A GOVERNMENT FACE ADDITIONAL LIABILITIES NOT INCLUDED IN THE FINANCIAL STATEMENTS?

Termination Benefits

TERMINATION BENEFITS are offered to employees by governments to induce the employees to voluntarily leave their employment earlier than they might have otherwise. (They also may include benefits a government provides to employees that depart involuntarily through layoffs.) Offers of termination benefits—often called *early-retirement incentives*—typically last for a short time and are made with the expectation of lowering a government's operating costs and closing a budget gap. Benefits offered may include cash payments or enhancements to existing pension benefits or OPEB; for instance, a government may offer employees due to retire in the next five years their full pension benefits, including credit for the years until their normal retirement age without having to work those years, if they retire immediately. It should be emphasized, however, that offers involving retirement benefits are temporary, and not a part of the regular benefits of a government's pension or OPEB plan; that is what distinguishes *termination benefits* from normal pensions and OPEB, which are a part of an employee's compensation.

Offers that involve pension benefits and OPEB are factored into the actuarial calculations performed to determine a government's pension and OPEB costs and obligations. (See the preceding discussion of pensions and OPEB.) Other types of termination benefits are recognized as expenses and liabilities when they can be measured and (1) an employee has accepted the offer (for voluntary terminations) or (2) the offer has been approved and communicated to the employees (for involuntary terminations).

When a government becomes obligated for termination benefits it has offered, it prepares a note disclosure that describes the benefits, the number of employees affected, the period when the benefits will be provided, the cost of the benefits (if not identifiable in the financial statements), and the significant assumptions and methods used to determine the cost of the termination benefits. If the benefits involved pensions or OPEB, a government also will disclose the resulting change in the TPL or TOL. Lastly, if the cost of the termination benefits cannot be determined yet (because, for example, it is not yet clear how many employees will accept the offer) and, therefore, expenses and liabilities are not reported, governments disclose this fact in the note.

Landfill Closure and Postclosure Care

If a government operates a municipal landfill where household waste and potentially other types of waste are disposed of, it is subject to a variety of laws and regulations dictating precautions it must

take to protect the environment—both while the landfill is in operation and after it is closed and no longer receives solid waste. Such a government is required to report a liability related to its obligation to perform the prescribed activities to close the landfill and maintain it after closure. The amount of that liability is based on an estimate of what it would cost today to perform those legally required actions—ESTIMATED TOTAL CURRENT COST. The information a government is required to include in the notes about the liability and how it is measured is discussed further in Part Eight. (See **Upon further review…reporting asset retirement obligations.**)

Claims and Judgments

Each year, claims may be submitted and judgments rendered against a government, such as lawsuits for personal injury on public property. Some governments guard against the risk of loss related to claims and judgments by organizing or participating in a risk pool. A PUBLIC ENTITY RISK POOL is an arrangement by which multiple governments join together to finance activities that involve risk or a liability, such as providing health or life insurance to employees, or insuring against property loss or financial claims. There are four basic types of risk pools:

- RISK-SHARING POOL
- INSURANCE-PURCHASING POOL
- BANKING POOL, and
- CLAIMS-SERVICING POOL or ACCOUNT POOL.

A risk pool (in its own financial report) or a government—if the risk pool does not issue its own report—makes disclosures similar to what is illustrated for a county government in Figure 26. The county operates the Public Insurance Fund, which provides two kinds of coverage to the local governments in the county—property and loss insurance, and employee health and accident insurance.

- A government's note disclosures include information about how it manages risk, including:
- Description of the types of risks of loss the government is exposed to and how it handles them, such as by purchasing insurance, participating in a risk pool, or risk retention (in other words, the government simply absorbs the losses as they occur)
- Description of significant reductions in insurance coverage from the previous year, organized by major category of risk, if applicable
- Indication that total settlements were greater than the government's insurance coverage in any of the past three fiscal years, if applicable. This is important for assessing whether the government has purchased a sufficient amount of insurance or weighing how much risk it has retained.

By the numbers…public entity risk pools

Type of risk pool	Example
Risk-sharing pool—governments pool their risks and share the costs of losses by paying into a central account from which losses are paid, similar to a cost-sharing multiple-employer pension plan.	Local governments and their county government establish a pool to insure against accidents on public property; claims would be paid from the pool.
Claims-servicing pool—this arrangement seeks economies of scale from centralized management but does not involve mixing of resources; separate accounts are managed for each participating government from which that government's losses are paid, similar to an agent multiple-employer pension plan.	A state manages a health insurance plan for its small local governments; the local governments contribute to the plan based on levels agreed to with their current employees, and employee claims are paid from only that government's contributions.
Insurance-purchasing pool—governments combine resources to purchase commercial insurance; such an arrangement provides (1) economies of scale that lower administrative costs and (2) increased purchasing power that helps obtain lower premiums and better benefits.	Counties and other local governments make contributions to a statewide life insurance fund, based on a flat amount per government employee.
Banking pool—an entity holds resources that can be used to make loans to member governments experiencing losses.	Towns and villages in a coastal region participate in a disaster relief pool that lends money to those governments for repairs to public property damaged by hurricanes.

If a government *participates* in a risk pool, it describes in a note disclosure the nature of its participation, its rights and responsibilities, and those of the pool. If a government retains the risk of loss, it explains how it estimates liabilities for unpaid claims, the amounts it reports in the financial statements, and the range of rates used (if any) for discounting future payments to their present value (the basis of the amount of the liabilities). Governments also disclose the total outstanding liabilities for which annuity contracts have been purchased in the name of the persons filing claims. Annuity contracts provide regular payments over a period, which can be used to pay claims. When an annuity contract has been obtained, the related liability is removed from the financial statements. Finally, a government presents a reconciliation of changes in the total claims liabilities for the current and prior year. (This reconciliation is described in the section on public entity risk pools in Part Six.)

Figure 26: Incurred claims and claim adjustment expenses were $1,931,000 in 2017.

- A government *operating* a risk pool also discloses the following information:
- A description of the agreement governing the risk pool and the number and types of governments participating in it

- An explanation of how certain amounts are estimated or determined, including unpaid claims liabilities, claim ADJUSTMENT EXPENSES, and the costs related to new or renewal insurance or pool participation contracts
- A statement of whether the risk pool included anticipated investment income when determining there was a PREMIUM DEFICIENCY
- A description of the nature and magnitude of reinsurance or excess insurance transactions to the pool's operations—excess insurance is similar to reinsurance in that it cedes risk loss to another risk pool or firm; however, it does so only for losses above a specific, typically large amount, and
- The total outstanding liabilities for which annuity contracts have been purchased in the name of the persons filing claims. When an annuity contract has been obtained, the related liability is removed from the financial statements.

The note also includes a reconciliation of claims liabilities that aggregates the information shown for individual contracts in the RSI schedule. (See Figure 34 in Part Six.)

Figure 26. Risk Pool Note Disclosure

①

The Public Insurance Fund (Fund) was organized in October 1987 to provide a program of property and casualty insurance and employee health and accident coverage for its member organizations. In accordance with Local Law XX-123(a)[k], all political subdivisions in the county are eligible to participate. The program's general objectives are to formulate, develop, and administer, on behalf of the member political subdivisions, a program of insurance; to obtain lower costs for that coverage; and to develop a comprehensive loss control program. Political subdivisions joining the Fund must remain members for a minimum of three years; a member may withdraw from the Fund after that time by giving six months' notice. Subdivisions applying for membership in the Fund may do so on approval of a two-thirds vote of the board of the Fund. Fund underwriting and rate-setting policies have been established after consultation with actuaries. Fund members are not subject to a supplemental assessment in the event of deficiencies. Annual premium increases are limited to 20 percent of the prior year's premium. If the assets of the Fund were to be exhausted, members would not be responsible for the Fund's liabilities. Fund members currently include 9 cities with populations ranging from 60,000 to 140,000.

Unpaid claims liabilities. The Fund establishes claims liabilities based on estimates of the ultimate cost of claims (including future claim adjustment expenses) that have been reported but not settled and of claims that have been incurred but not reported. The length of time for which such costs must be estimated varies depending on the coverage involved. Estimated amounts of salvage and subrogation and reinsurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Because actual claims costs depend on such complex factors as inflation, changes in doctrines of legal liability, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount, particularly for coverages such as general liability. Claims liabilities are recomputed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, frequency of claims, and other economic and social factors. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed on actual historical data that reflect past inflation and on other factors that are considered to be appropriate modifiers of past experience. Adjustments to claims liabilities are charged or credited to expense in the periods in which they are made.

Deferred policy acquisition costs. Acquisition costs, which consist primarily of salaries, inspection and medical exam fees, and certain underwriting expenses, vary with, and are primarily related to, the issuance of new insurance policies. These costs are deferred and amortized on a straight-line basis over the life of the insurance contract. Deferred acquisition costs are reviewed periodically to determine if they are recoverable from future income, including investment income. If the deferred costs are not recoverable, they are charged to expense in the period of the review. Amortization of deferred costs in 2017 was $133,000.

Reinsurance. The Fund uses reinsurance agreements to reduce its exposure to large losses on all types of insured events. Reinsurance permits recovery of a portion of losses from reinsurers, although it does not discharge the primary liability of the Fund as direct insurer of the risks reinsured. The Fund does not report reinsured risks as liabilities unless it is probable that those risks will not be covered by reinsurers. Premiums ceded to reinsurers during 2017 were $1,004,000, and the amount deducted from claims liabilities as of December 31, 2017, for reinsurance was $377,000.

Unpaid claims liabilities. The Fund establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses, both allocated and unallocated. The following represents changes in those aggregate liabilities for the Fund during the past two years (in thousands):

	2017	2016
Unpaid claims and claim adjustment expenses at beginning of year	$ 1,421	$ 1,189
Incurred claims and claim adjustment expenses:		
Provision for insured events of current year	1,282	900
Increases in provision for insured events of prior years	649	540
Total incurred claims and claim adjustment expenses	1,931	1,440
Payments:		
Claims and claim adjustment expenses attributable to insured events of current year	641	450
Claims and claim adjustment expenses attributable to insured events of prior years	904	758
Total payments	1,545	1,208
Total unpaid claims and claim adjustment expenses at end of the year	$ 1,807	$ 1,421

At year-end 2017, $718,000 of unpaid claims and claim adjustment expenses are presented at their net present value of $576,000. These claims are discounted at annual rates ranging from 8.5 to 11.0 percent. Unpaid claims expenses of $249,000 are not reported in the 2017 year-end balances because the Fund has purchased annuities in claimants' names to settle those claims.

Figure 26 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② Dollar amounts in this disclosure are stated in thousands.

WHAT'S AHEAD?

- DOES A GOVERNMENT GUARANTEE THE FINANCIAL OBLIGATIONS OF OTHER GOVERNMENTS? HOW MUCH MIGHT THE GOVERNMENT HAVE TO PAY ON THOSE OBLIGATIONS?
- DOES A GOVERNMENT HAVE OUTSTANDING FINANCIAL OBLIGATIONS THAT ARE GUARANTEED BY ANOTHER GOVERNMENT?
- UNDER WHAT CIRCUMSTANCES COULD A GOVERNMENT BE OBLIGATED FOR OTHER PAYMENTS?

Nonexchange Financial Guarantees

Some governments guarantee the outstanding debt and other financial obligations of other governments, and sometimes of companies and not-for-profit organizations as well. For instance, a state government may have a program in which it agrees to step in and make debt service payments on a local government's behalf if the local government fails to do so. The agreement with the local government may or may not require the locality to subsequently repay the state for any guarantee payments the state has made. This type of arrangement may function like the purchase of bond insurance from a private company; however, the locality will pay little or nothing to the state in return for the guarantee it receives. For this reason, the arrangement is called a **NONEXCHANGE FINANCIAL GUARANTEE.**

As long as the government or other entity receiving the guarantee—the obligor—continues to make payments on its financial obligation, it continues to report the obligation as a liability in its statement of net position. The government providing the guarantee—the guarantor—does not report anything in its financial statement related to the guarantee unless it concludes that it is *more likely than not* (a greater than 50 percent chance) that it will have to make a payment on the guarantee.

The guarantor reaches this conclusion based on an assessment of qualitative factors that indicate the obligor will not make a payment on its own. For example, if the obligor files for bankruptcy, that may be a strong indication that the guarantor will have to act on its guarantee. Alternatively, there may be evidence that the obligor is experiencing severe financial difficulties, such as drawing down on a debt service reserve to make debt payments, or losing a major revenue source. If a guarantor government has a large number of similar guarantees, rather than individually assessing each guarantee, it likely will

evaluate factors relevant to the group of guarantees as a whole, such as the frequency with which the guarantor has had to make payments on those guarantees in the past.

Figure 27. Nonexchange Financial Guarantees Note Disclosure

In accordance with the School Construction Act, Central State has guaranteed outstanding bond obligations of school districts within the State in the amount of $14.25 billion at June 30, 2017. The guarantees extend through the maturity dates of the bonds with the last maturity date being June 30, 2028. If a school district is unable to make a required debt service payment on a guaranteed bond, Central State is required to make the payment. Central State considered historic experience of defaults and qualitative factors in determining its guarantee liability.

The liability recognized for nonexchange financial guarantees by Central State at June 30, 2017, is as follows:

①	Beginning of Year	Increases	Decreases	End of Year
	$ 18,500,000	$ 4,875,000	$ 5,000,000	$ 18,375,000

For nonexchange financial guarantees outstanding at June 30, 2017, Central State has paid $32.675 million in debt service payments. Central State expects to recover $16.485 million of this amount in future years.

Figure 27 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

When the guarantor government reports a liability related to a nonexchange financial guarantee, it estimates what its future cash outlays related to the guarantee will be and then calculates the value of those payments as of the date of the financial statements. That does not mean that the obligor removes the obligation from its own financial statements. On the contrary, it continues to report the obligation as a liability, and reduces it to reflect payments made by the guarantor, until it has been legally released from the obligation. If the terms of the agreement with the guarantor require the obligor to repay any guarantee payments that have been made, the obligor also will report a payable to the guarantor.

Note disclosures for guarantors

Any government that provides a nonexchange financial guarantee discloses the total amount guaranteed and descriptive information, including the authority for making it, limits on making guarantees, how long the guarantee lasts, and the types of obligations guaranteed. (See Figure 27.) The disclosure is organized by type of guarantee if the guarantor has more than one type. If a guarantor

government recognizes a liability or makes a payment related to a nonexchange financial guarantee, it discloses the following as well:

- When the liability was recognized and how it was measured
- The amount of the liability at the start of the year, increases and decreases during the year, and the year-end amount
- The cumulative amount (this fiscal year and all prior years) of payments made related to guaranteed obligations that remain outstanding at the end of the fiscal year, and
- Amounts of those payments expected to be repaid to the guarantor.

Note disclosures for obligors

Any government with obligations outstanding at the end of the fiscal year that are subject to a nonexchange financial guarantee discloses the following (organized by type of guarantee, if the government has received more than one type):

- Name of the guarantor
- Amount of the guarantee
- How long the guarantee will last
- The amount paid, if any, by the guarantor *during the fiscal year* and the *cumulative amount* paid to date on guaranteed obligations that are outstanding at the end of the fiscal year, and
- If there are provisions for repaying the guarantor, a description of those provisions and any repayment amount owed to the guarantor.

What can you do with information about nonexchange financial guarantees?

There may be potential claims on a government's resources that do not show up yet as liabilities in the statement of net position because they are contingent on certain events occurring in the future. (See more in the following section on contingencies.) However, the fact that they are not reported as liabilities at present does not mean you should not be concerned about them. The disclosures made by a government that extends nonexchange financial guarantees will help you to evaluate the likelihood that it will need to find resources to make payments on those guarantees in the future. To the extent that the government has had to make payments on its guarantees, it is important to understand the magnitude of the burden placed on the guarantor government, how long the burden is likely to last, and the prospects for recouping some or all of the payments from the obligors.

From the perspective of a government that has issued obligations that are guaranteed under these arrangements, the guarantee represents a potential resource that will be available if the government needs it. This is relevant to understanding a government's ability to meet its financial obligations as they come due.

Contingent Liabilities

Claims and judgments often take several years to be resolved. An accident may occur in one year, but final payment may not be made to the victim until after investigations or legal actions have run their course. These uncertainties regarding claims and judgments mean that it may not always be possible to accurately reflect the losses related to them in the financial statements. If information is not available at the time the financial statements are prepared that a payment probably will have to be made, and unless the amount to be paid can be reasonably estimated, a government cannot report the claim or judgment as a cost or an amount owed in the financial statements. (This also applies to asset impairments—no loss can be reported if the government does not have information showing the impairment likely occurred and allowing it to reasonably estimate the amount of the loss.)

This is where note disclosure comes in. If it is *probable* that a loss has occurred, but the amount cannot be reasonably estimated, or if the amount can be estimated but the loss is just *reasonably possible,* not probable, the government discloses the nature of the contingent liability and an estimate of the potential loss or range of potential loss (or it states that an estimate cannot be made). (See **Upon further review…the vocabulary of contingencies.**) If the government is exposed to the risk of further loss beyond what is reported in the financial statements, it makes a similar disclosure.

What can you do with information about contingent liabilities?

If there is a chance that a government may be facing additional losses that are not reflected in the financial statements, it could affect your assessment of its financial outlook. You may want to consider the costs or liabilities related to such contingencies in your analysis of financial position or debt burden if estimates are available, or at least be able to note that the results of these calculations might worsen because the contingency may become reality.

Deferred Inflows and Outflows of Resources

Most of the disclosures related to the statement of net position address assets and liabilities. Certain deferred inflows and deferred outflows of resources may be disclosed in association with specific transactions such as derivatives, service concession arrangements, and pensions and OPEB, as described earlier.

As with other financial statement items, such as capital assets, long-term liabilities, receivables, and payables, a government discloses details about the different types of deferrals it has if they are not evident on the face of the financial statements. Local City disaggregates its deferrals by their associated transactions in Figure 1, but the state illustrated in Figure B-1 shows just total deferred outflows and total deferred inflows. The state would need to present a note disclosure that breaks down the deferrals by type.

NET POSITION

If a government has both restricted and unrestricted resources that can be spent for a particular purpose, it discloses in the SSAP its policy for which it spends first—restricted or unrestricted. In reality, these monies are likely deposited in the same bank account and are indistinguishable from each other. The order-of-spending policy, therefore, actually is an *assumption* about which resources are spent first. This is needed for determining whether the resources available at the end of the fiscal year are constrained to a particular use or not, for the purpose of reporting net position. Consider, for example, a government with $100 restricted to social programs and another $100 that is unrestricted: If the government spends $150 on social programs, is the remaining $50 restricted or unrestricted? The answer depends on the policy (assumption) regarding whether restricted or unrestricted amounts are spent first.

As described in Part Four, resources generally are restricted by external parties, most often higher levels of government that provided the resources. Another source of restrictions is enabling legislation, a form of statute that both creates a revenue source and limits the use of the revenue to a specific purpose. This limitation is legally enforceable, meaning that a government cannot use the revenue for any other purpose and, if it does, it can be compelled to restore the resources. For instance, a citizen group could sue and successfully win a court judgment barring the government from the unauthorized use of the resources for purposes not specified by the enabling legislation. If a government has net position that is restricted by enabling legislation, it makes a disclosure in the notes similar to the following:

> **Net Position.** The government-wide statement of net position reports $10,758,421 of restricted net position, of which $3,124,021 is restricted by enabling legislation.

FAIR VALUE is the amount that would be received if an item were sold (or the amount paid to transfer a liability) between willing participants in an active market

INTEREST RATE RISK is the risk that changing interest rates will lead to investment losses

IMPAIRMENT is a substantial and unexpected reduction in the service capacity of a capital asset

CURRENT REFUNDING involves using the proceeds of refunding bonds or other resources to immediately repay outstanding bonds

ADVANCE REFUNDING involves placing the proceeds of the refunding bonds or other resources with an escrow agent, which invests the proceeds and makes the regular debt service payments on the outstanding debt

a DERIVATIVE is a financial instrument with a value based on the performance of an underlying instrument or agreement, such as an investment or outstanding debt

an INTEREST RATE SWAP is a derivative in which a government agrees to make fixed payments to another party in return for payments equal to the government's payments on the variable-rate debt (or variable payments in return for payments equal to its fixed-rate debt)

a **HEDGING DERIVATIVE INSTRUMENT** substantially offsets the changes in cash flows or fair values of the item the derivative is associated with a **TOTAL PENSION LIABILITY (TOTAL OPEB LIABILITY)** is the value today of a government's obligation to provide current and former employees with pension benefits (OPEB) that already have been earned

a **NET PENSION LIABILITY (NET OPEB LIABILITY)** equals the TPL (TOL) minus the fiduciary net position of the pension (OPEB) plan

FIDUCIARY NET POSITION is the value of resources set aside for the purpose of making benefit payments in a pension or OPEB trust that meets certain criteria

a **PREMIUM DEFICIENCY** occurs when the cumulative costs a risk pool expects to have are greater than the premiums that are expected to be received

a **CONTINGENT LIABILITY** is a potential liability if specific conditions arise in the future

Upon further review...amortized cost

AMORTIZATION, like depreciation, allocates costs over the life of an asset. In the case of certain qualifying investments not reported at fair value, amortization involves allocating associated discounts and premiums in installments over the years between when a government acquired the investments and when they mature. Amortized cost, then, is the original cost of acquiring the investment plus the annual amortized discount or premium amounts accumulated thus far.

By the numbers...level of detail for deposit and investment disclosures

Deposit and investment disclosures generally are made for the primary government as a whole. However, if the investments reported in one of the financial statement columns—governmental activities, BTAs, major funds, nonmajor funds in the aggregate, internal service funds, or fiduciary fund types—are exposed to significantly greater risk than those of the government as a whole, more specific disclosures should be made for those investments. For example, a government's total investments may not be exposed to significant concentration risk. However, the investments of its capital projects fund all may be bonds from a single issuer, which would lead the government to disclose exposure to concentration risk for that fund

By the numbers...capital asset policies

Check a government's SSAP note for the assumptions it makes about the estimated useful lives of its assets when calculating depreciation. (The government in the SSAP in Figure E-2, for instance, estimates a useful life of 7–10 years for equipment.) A government also identifies the depreciation method it employs—the most common is the "straight-line method," which allocates the original cost in equal installments each year of the asset's life. Finally, a government describes its capitalization threshold, which is the dollar value above which long-lived assets are "capitalized"—in other words, reported as capital assets when purchased or constructed and depreciated over their lifetimes. The cost of assets that fall below the threshold is reported as expense in the year of acquisition, rather than depreciated. (The government in Figure E-2 capitalizes all equipment purchases of $5,000 or more.)

By the numbers...examples of short-term debt

BOND ANTICIPATION NOTES (BANs)—issued in advance of receiving proceeds from the sale of long-term bonds

GRANT ANTICIPATION NOTES (GANs)—issued in advance of receiving an intergovernmental grant

GRANT ANTICIPATION REVENUE VEHICLES (GARVEEs)—issued in advance of receiving federal transportation aid

REVENUE ANTICIPATION NOTES (RANs)—issued in advance of receipts from a specific revenue source or sources

TAX AND REVENUE ANTICIPATION NOTES (TRANs)—issued in advance of expected receipts from a combination of tax and nontax revenues

TAX ANTICIPATION NOTES (TANs)—issued in advance of expected tax receipts

By the numbers…conditions for in-substance defeasance

In order for debt to be considered defeased in substance, the proceeds of the refunding must be placed with an escrow agent in a trust, such that a government has no further access to them. The trust has to (1) be restricted solely to the payment of debt service; (2) be limited to owning only monetary assets that are essentially risk-free, including U.S. government obligations (such as Treasury bills), obligations guaranteed by the U.S. government, and certain securities backed by U.S. government obligations; and (3) produce cash flows that approximate the debt service payments.

Upon further review…the time value of money

It is a basic fact that, over time, the value of money diminishes. One hundred dollars today is worth more than one hundred dollars five years from now because today's money can be invested, earn interest, and be greater than one hundred dollars in five years. That hundred dollars invested at 5 percent annual compounded interest would be worth $127.63 in 5 years ($100 × 1.05 × 1.05 × 1.05 × 1.05 × 1.05). The fact that the value of money changes with time makes it difficult to compare debt service payment schedules: Since dollars in the future are not worth the same as dollars in the present, you cannot simply add up the future payments of two debt issues and compare them. In order to make comparisons, analysts convert the future amounts into their present value.

Here is a simple example: One bond requires an annual payment of $100 for each of the next 5 years. Another bond requires a single payment of $500 in the fifth year. Each involves a total cash outlay of $500, so they must be equal, right? Wrong. Assuming a 3 percent interest rate, the annual $100 payments are worth $457.97 in present value terms; the single $500 payment is worth $431.31. Stated differently, a government would need to invest $457.97 today at 3 percent interest in order to have the resources necessary to pay $100 a year for 5 years, or it would need to invest $431.31 today at 3 percent interest in order to have the resources to make a $500 payment 5 years from now. In present value terms, the single payment five years from now is less expensive.

Economic gains and losses are the difference between the present value of the debt service payments for existing debt and the debt service payments for the bonds issued to refund that debt. If the present value of the *refunding* bonds' debt service is lower, there is an economic gain—the refunding bonds are less costly. If, however, the present value of the *original* bonds' debt service is lower, there is an economic *loss*—the refunding bonds are *costlier*.

By the numbers…how a hedging derivative instrument is identified

To determine whether a derivative is a *hedging* derivative instrument, a government evaluates its effectiveness at the end of each year it exists. If it continues to be effective—meaning the derivative substantially offsets the changes in the fair values or cash flows of the item it is associated with—the changes in the derivative's fair value are deferred (reported as deferred inflows or deferred outflows of resources in the statement of net position rather than included in investment revenues). Governments are allowed to use two basic types of approaches to evaluating effectiveness—consistent critical terms or quantitative methods.

If the critical terms of the derivative and the terms of the item it is hedging are the same—for instance, the ending date of an interest rate swap is the same as the maturity date of the bonds, both are based on the same index, and so on—the derivative is presumed to be effective. Under such circumstances, any change in the cash flows or fair value of the item being hedged is offset by changes in the cash flows or fair value of the potential hedging derivative because they change based on the same terms.

Three quantitative methods are specifically identified in the accounting standards—synthetic instruments, dollar-offset, and regression analysis. These methods measure the degree to which the changes in the fair value or cash flows of the potential hedging derivative instrument offset those of the item being hedged. The standards also allow for other acceptable quantitative methods that meet certain qualifying criteria.

Upon further review…major changes in lease accounting

Beginning in fiscal years ending December 31, 2020, and later, the distinction between capital and operating will be eliminated. Under accounting standards issued in 2017, leases will be reported in a manner that reflects the fact that they are a form of borrowing to finance the acquisition of a capital asset.

With certain exceptions based on practicality or cost–benefit considerations, government lessees will report a long-term liability in the accrual financial statements based on the present value of their future lease payments and an **INTANGIBLE**

ASSET related to its right to use the leased asset (rather than recognizing the leased asset itself). Each year, lessees will report a lease expense based on amortization of the intangible capital asset (spread over the shorter of the useful life of the asset or the length of the lease) and interest expense.

Government lessors will continue to report leased assets as their own capital assets, applying relevant accounting requirements such as depreciation (unless the lessee is required to return the capital asset in the same or better condition at the end of the lease). Lessors also will report a long-term lease receivable related to the future payments it will receive and a deferred inflow of resources to reflect that those future payments relate to future years. Each year, lessors will report lease revenue based on amortization of the lease receivable (spread over the years of the lease) and interest revenue.

The most common exception to these requirements likely will be for **SHORT-TERM LEASES**—those with a maximum term at inception of 12 months or less, including any options for renewal. Inflows and outflows related to short-term leases will be reported in the flows statements, such as the statement of activities, but no intangible capital assets, long-term liabilities, lease receivables, or deferred inflows will be reported for those leases. Exceptions also are made for (1) contracts that transfer ownership of the capital asset and (2) certain regulated leases, such as those entered into by municipal airports as lessors with airlines.

Upon further review…special funding situations

It may be the case that an entity other than the employer—called a **NONEMPLOYER CONTRIBUTING ENTITY**—such as the state government, is legally responsible for a part of the pension or OPEB benefits of a government's employees. If the state government is the only entity that is legally responsible for making contributions directly to the pension or OPEB plan, the accounting standards call this a **SPECIAL FUNDING SITUATION**. If the state government is just one of the entities responsible for making contributions, it is a special funding situation if the amount of the state's contribution is based only on factors related to pensions or OPEB (for instance, the state provides half of the contributions to the plan). It is not a special funding situation if the state's contribution is based on factors unrelated to pensions or OPEB (such as a certain percentage of the revenue from a sales tax).

For accounting purposes, special funding situations are handled similarly to cost-sharing plans—the employer reports its proportionate share of the NPL or NOL and deferrals in its financial statements. (See **Upon further review…contributions after the NPL or NOL is measured** on page 103.) The nonemployer contributing entity, if it is a government, reports *its* proportionate share in its own financial statements. The employer reports the entire pension or OPEB expense because it reflects the cost of providing services no matter who is paying for it. However, the employer also reports revenue for the support provided by the nonemployer contributing entity, so the *net* impact on the employer's financial statements reflects only the part of the obligation that it is responsible for.

Upon further review…deferrals related to pensions and OPEB

As explained on this page, certain parts of the changes in the NPL or NOL initially are reported as deferred outflows or deferred inflows of resources and included in pension or OPEB expense over multiple years. (**Upon further review…contributions after the NPL or NOL is measured** on page 103 describes another circumstance under which deferred outflows of resources related to pensions and OPEB are reported.)

If you look at the government-wide statement of net position, you are likely to see a single line among the deferred outflows for those related to pensions and a single line for OPEB; likewise, there would be a single line among the deferred inflows for those related to pensions and a single line for OPEB. (It also is possible that your government reports a single amount for total deferred outflows and a single amount for total deferred inflows, as explained in **Upon further review…level of detail for reporting deferrals** on page 43.)

Figure 25 includes a disclosure that identifies the specific sources of the deferrals related to pensions. The disclosure also tells you the net impact of those deferrals on pension expense for each of the next five years and in the aggregate for all years beyond that. (Deferred outflows related to contributions made after the measurement date are not included here—they reduce the next year's NPL.) For example, the deferrals in Figure 25 will add a net $86.5 million to pension expense in 2019 but will reduce pension expense by $1.8 million in 2021.

Upon further review…contributions after the NPL or NOL is measured

The NPL or NOL reported in your government's statement of net position often is calculated on a date (called the MEASUREMENT DATE) earlier than the date of the financial statements—as early as one year prior. For example, the NPL or NOL in a government's financial statements for June 30, 2017, may be measured as early as June 30, 2016. This is allowed for practical reasons, most notably because of the need for governments to coordinate with pension plans, which may have a different fiscal year-end. Governments disclose the measurement date in the pension and OPEB notes. (Look at the first sentence in Figure 23.)

If a government's NPL or NOL is measured as of a date one year prior to the date of the financial statements, any contributions the government made during the fiscal year to its pension or OPEB plan are not reflected in the NPL or NOL amounts reported in the statement of net position because they occurred *after* the NPL or NOL was measured. Those contributions will be subtracted from the measurement of *next year's* NPL or NOL. This means the contributions made after the measurement date (but before the end of the fiscal year) relate to a future year, so the government reports a deferred outflow of resources equal to the amount of the contributions. In the next fiscal year, when the amount of the contributions is subtracted from the NPL or NOL, the deferred outflow from the prior year is eliminated.

Upon further review…criteria for pension and OPEB trusts

To be considered a part of the plan's fiduciary net position that is subtracted from the total liability to obtain the NPL or NOL, assets are required to be held in a trust or equivalent arrangement that meets all three of the following criteria:

- Contributions to the plan from the government and nonemployer contributing entities are irrevocable. In other words, assets contributed to the plan cannot be taken back (with the exception of certain refunds).
- The assets in the plan can be used only to provide benefits to plan members (or for administrative costs).
- The assets are protected from creditors.

Upon further review…selecting a discount rate

In general, governments discount projected benefit payments to their value today using a discount rate equal to what they expect the long-term rate of return on the investments of the plan to be. This is true as long as a government projects that there will be enough assets in the plan to make long-term investments and cover the projected benefit payments. However, if a government projects that a time will come in the future when the assets in the plan related to existing plan members will *not* be enough to cover the projected benefit payments, it will begin to discount using a different rate—one for a 20-year, tax-exempt general obligation municipal bond that is rated AA or higher (or its equivalent) by a bond rating agency. If this is the case, the government will tell you which years' projected benefit payments were discounted using the expected long-term rate of return and which years were discounted using the general obligation bond rate.

Upon further review…eligibility for the OPEB alternative measurement method

Certain governments in single-employer and agent multiple-employer OPEB plans may use simplified methods and assumptions to measure the TOL. To be eligible to use the *alternative measurement method,* a government either:

- Has its own plan with fewer than 100 members, or
- Participates in a plan with fewer than 100 members that (1) is not required by GAAP to obtain an actuarial valuation or (2) does not prepare a financial report in accordance with GAAP.

If a government qualifies to use the alternative measurement method and elects to do so, it tells you it did in its SSAP.

Keep in mind…implementation dates for OPEB reporting

The sample statement of net position in Figure 1, for the fiscal year ending December 31, 2017, includes an NOL. However, if you are looking at an actual government's financial statements for that date or any fiscal year ending prior to June 30, 2018, you may not see an NOL. This is because the standards for reporting OPEB in the same manner as pensions were issued later (in June 2015) and are required to be implemented beginning with fiscal years ending June 30, 2018, and later (September 30, 2018; December 31, 2018). In order to present all retirement benefits using the same approach, as ultimately intended by the accounting standards, this guide presumes that the OPEB standards already have been implemented by the illustrative governments depicted in the financial statements and notes.

The most significant difference between the new and old OPEB standards is the reporting of the NOL in the financial statements. Previously, the difference between the total obligation for OPEB—called the **ACTUARIAL ACCRUED LIABILITY (AAL)**—and the assets set aside in a trust—called the **ACTUARIAL VALUE OF ASSETS (AVA)**—was disclosed in the notes, not reported in the financial statements. This difference was called the **UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL)**. The OPEB related liability that appeared in the financial statements was called the **NET OPEB OBLIGATION,** and was equal to the difference between (1) the **ANNUAL REQUIRED CONTRIBUTION (ARC)** to the OPEB plan, as determined by an actuary, and (2) the amounts *actually contributed* by the government or paid for retiree health benefits and other OPEB.

The ARC comprised two parts—the service cost and a portion of UAAL (which could be divided over a period of up to 30 years). The amount reported as OPEB expense was based on the ARC rather than on the annual change in the OPEB liability.

The same basic approach of the actuary to measuring the OPEB liability—project, discount, allocate—is used in both the old and new OPEB standards. However, the new standards are more limiting in terms of the assumptions that governments may employ, with the intention of making the resulting liability more comparable across governments. Although the amounts reported under the new standards are not directly comparable to those under the old standards, it can be said that the AAL is analogous to the TOL, the AVA to the fiduciary net position of the plan, and the UAAL to the NOL.

Upon further review…reporting asset retirement obligations

The legal requirements related to closing and caring for a municipal solid waste landfill are a type of **ASSET RETIREMENT OBLIGATION** or **ARO**—and, until recently, the only kind of ARO specifically addressed in the accounting standards for state and local governments. Beginning in fiscal years ending June 30, 2019, and later, however, governments will begin to apply government-specific standards for AROs. (Some governments, such as public power utilities, already have been reporting liabilities for AROs by applying standards issued by the FASB for companies and nongovernmental not-for-profits.)

As a result, liabilities related to AROs other than those related to landfills will begin to appear in some governments' financial statements. Examples of such AROs are liabilities that stem from federal regulations related to decommissioning nuclear power plants or a court order to dismantle and remove a toxic facility. AROs will be measured similarly to landfill-related liabilities—an estimate of what it would cost to perform the retirement activities today.

Upon further review…the vocabulary of contingencies

The determination of how to report contingent liabilities rests on two terms, *probable* and *reasonably possible.* Broadly, those terms mean the following:

- Probable: likely to occur
- Reasonably possible: less than likely, but the chances of occurrence are more than remote or slight.

Probable amounts are reported in the financial statements and reasonably possible amounts are disclosed in the notes.

PART SIX

SUPPORTING INFORMATION RELATED TO THE STATEMENT OF NET POSITION

Assets, liabilities, and net position are addressed by both RSI and SI that follow notes to financial statements in the annual financial report. Specific presentations relate to the modified approach to reporting capital assets, risk pools, outstanding debt, pensions and OPEB, and trends in net position.

REQUIRED SUPPLEMENTARY INFORMATION

WHAT'S AHEAD?

- HOW HAVE A GOVERNMENT'S OBLIGATIONS FOR RETIREMENT BENEFITS CHANGED OVER TIME?
- HAS THE FINANCIAL STATUS OF RETIREMENT PLANS IMPROVED OR DETERIORATED?
- IS A GOVERNMENT KEEPING PACE WITH THE FUNDING REQUIREMENTS OF ITS RETIREMENT PLANS?

Pensions and OPEB

There are four sets of RSI that a government may present regarding its defined benefit pension and OPEB plans, depending on the type of plan:

- Changes in the NPL or NOL
- Pension or OPEB ratios
- Employer contributions, and
- Notes to the schedules.

Changes in the liability and related ratios

If a government participates in a single-employer or agent multiple-employer pension or OPEB plan, it presents a schedule with information very similar to the note disclosure of changes in the NPL or NOL. In fact, the schedule essentially presents the right-hand column of Figure 25 for the past 10 years. (See **Keep in mind…the number of years in pension and OPEB RSI schedules**.)

Typically, this schedule also includes two ratios calculated using information from the explanation of the changes in the NPL or NOL. (This information may, however, be presented in a separate schedule.) The first ratio divides the fiduciary net position of the pension or OPEB plan by the TPL or TOL, respectively. This ratio—which may be called an **ASSET SUFFICIENCY RATIO**—is a measurement of the sufficiency of the assets already held by the plan to cover the existing pension or OPEB liability. The government illustrated in Figure 28 has a ratio of 74.85 percent, meaning the resources in the plan that can be used to make benefit payments equal roughly three-quarters of the value of those

benefit payments (the TPL or TOL). Conversely, it means that there are no resources in the plan for one-quarter of the liability.

Governments next present COVERED PAYROLL and a second ratio: the NPL or NOL divided by covered payroll. Covered payroll is the total pay on which contributions to the plan are based. The intention of this ratio is to give you a sense of the magnitude of the net liability and to enable you to compare governments. For instance, is the NPL of almost $752 million for the government in Figure 28 a big liability or a small one? The ratio of 167 percent helps you by showing that the NPL is the equivalent of the government payroll for 20 months (1.67 years). (See **By the numbers…OPEB and covered-employee payroll**.)

Governments in cost-sharing plans. In a cost-sharing plan, the information about changes in the NPL or NOL is available only for all of the governments in the plan combined, not for the individual governments. Therefore, the governments present a schedule for the past 10 fiscal years containing the following information (see Figure 29):

- The government's proportion (the percentage) of the plan's NPL or NOL
- The government's proportionate share (the dollar amount) of the NPL or NOL
- Covered payroll
- A ratio of the NPL or NOL divided by covered payroll, and
- A ratio of plan fiduciary net position divided by the total liability for the plan as a whole.

What can you do with this information? The information in a government's RSI schedule can be used to answer the same questions as the pension and OPEB note disclosures—but for the past decade rather than just the past year. You can see what is driving longer run trends in the NPL or NOL. The changes in the liability shown in any given year's note may be a one-time occurrence or part of a continuing trend; this schedule helps you to determine which.

The ratios help you to determine whether a government has set aside sufficient resources to finance the retirement benefit promises it has made to its employees. If the resources are not sufficient, you can see the size of the shortfall. The NPL or NOL is compared with the covered payroll to give you a sense of the magnitude of the liability—to catch up with its obligations, the illustrative government in Figure 28 would need to contribute an amount equivalent to 20 months of its payroll. If a government were allowed to contribute more to the plan (many governments in cost-sharing plans are not), how long would it take to catch up with a liability of that size?

Figure 28. Schedule of Changes in the Net Pension Liability and Related Ratios

Merritt County
Schedule of Changes in the Net Pension Liability and Related Ratios
Past 10 Fiscal Years
(dollars in thousands)

	20X9	20X8	20X7	20X6	20X5	20X4	20X3	20X2	20X1	20X0
Total pension liability										
Service cost	$ 75,864	$ 74,276	$ 71,157	$ 69,344	$ 66,875	$ 62,784	$ 59,463	$ 52,111	$ 49,258	$ 40,577
Interest	216,515	205,038	188,845	174,694	162,509	147,973	136,457	127,251	106,311	97,756
Changes of benefit terms	—	—	—	—	—	—	—	—	119,513	—
Differences between expected and actual experience	(37,539)	(15,211)	(3,562)	38,438	19,927	(28,228)	34,335	13,464	30,981	35,780
Changes of assumptions	—	—	61,011	—	—	92,500	—	—	32,979	—
Benefit payments, including refunds of employee contributions	(119,434)	(112,603)	(104,403)	(95,376)	(88,790)	(86,139)	(77,185)	(70,907)	(66,789)	(60,653)
Net change in total pension liability	135,406	151,500	213,048	187,100	160,521	188,890	153,070	121,919	272,253	113,460
Total pension liability—beginning	2,853,455	2,701,955	2,488,907	2,301,807	2,141,286	1,952,396	1,799,326	1,677,407	1,405,154	1,291,694
Total pension liability—ending (a)	$ 2,988,861	$ 2,853,455	$ 2,701,955	$ 2,488,907	$ 2,301,807	$ 2,141,286	$ 1,952,396	$ 1,799,326	$ 1,677,407	$ 1,405,154
Plan fiduciary net position										
Contributions—employer	$ 79,713	$ 86,607	$ 89,828	$ 91,963	$ 93,541	$ 85,681	$ 68,866	$ 29,849	$ 25,086	$ 22,826
Contributions—employee	31,451	30,550	29,137	28,547	27,743	26,709	25,577	22,673	21,132	19,202
Net investment income	196,154	(44,099)	(16,138)	298,260	166,826	140,132	193,107	39,142	(22,410)	(5,750)
Benefit payments, including refunds of employee contributions	(119,434)	(112,603)	(104,403)	(95,376)	(88,790)	(86,139)	(77,185)	(70,907)	(66,789)	(60,653)
Administrative expense	(3,373)	(3,287)	(2,774)	(2,582)	(2,086)	(2,235)	(1,912)	(1,887)	(1,509)	(1,491)
Other	8	(83)	173	(175)	9	75	(493)	8	—	—
Net change in plan fiduciary net position	184,519	(42,915)	(4,177)	320,637	197,243	164,223	207,960	18,878	(44,490)	(25,866)
Plan fiduciary net position—beginning	2,052,589	2,095,504	2,099,681	1,779,044	1,581,801	1,417,578	1,209,618	1,190,740	1,235,230	1,261,096
Plan fiduciary net position—ending (b)	$ 2,237,108	$ 2,052,589	$ 2,095,504	$ 2,099,681	$ 1,779,044	$ 1,581,801	$ 1,417,578	$ 1,209,618	$ 1,190,740	$ 1,235,230
County's net pension liability—ending (a) – (b)	$ 751,753	$ 800,866	$ 606,451	$ 389,226	$ 522,763	$ 559,485	$ 534,818	$ 589,708	$ 486,667	$ 169,924
Plan fiduciary net position as a percentage of the total pension liability	74.85%	71.93%	77.56%	84.36%	77.29%	73.87%	72.61%	67.23%	70.99%	87.91%
Covered payroll	$ 449,293	$ 436,424	$ 416,243	$ 407,812	$ 396,332	$ 381,554	$ 365,385	$ 323,896	$ 301,891	$ 274,318
County's net pension liability as a percentage of covered payroll	167.32%	183.51%	145.70%	95.44%	131.90%	146.63%	146.37%	182.07%	161.21%	61.94%

Notes to Schedule:

Benefit changes. In 20X1, benefit terms were modified to base public safety employee pensions on a final three-year average salary instead of a final five-year average salary.

Changes of assumptions. In 20X7, amounts reported as changes of assumptions resulted primarily from adjustments to expected retirement ages of general employees. In 20X4, amounts reported as changes of assumptions resulted primarily from adjustments to expected retirement ages of public safety employees. In 20X1, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the RP-2000 Healthy Annuitant Mortality Table for purposes of developing mortality rates.

Figure 28 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② If a government participates in an OPEB plan administered through a trust that meets the required criteria, it presents a schedule like this for OPEB as well.

③ This sample schedule presents a full 10 years for illustrative purposes. However, a government will build this schedule prospectively and, therefore, may present only a few years at this time.

④ Dollar amounts have been rounded to the nearest thousand.

⑤ These amounts are the same as those presented in the current-year note disclosure in Figure 25.

⑥ As explained later in this section, a government adds notes to the schedule to explain any changes during the 10-year period that affect the trends in the information.

The value of the 10-year trend is that it shows you not only where a government stands now, but how it got there and where it may be headed. It may be difficult to judge the asset sufficiency ratio of 74.85 percent for 20X9 in Figure 28. If you compare it with other governments, however, you begin to comprehend the status that amount conveys. Is a government better or worse off than other governments? Is the ratio trending upward (more of the liability is covered by plan resources) or downward over time?

Employer contributions

The SCHEDULE OF EMPLOYER CONTRIBUTIONS compares a government's actual contributions over the past 10 years to its pension or OPEB plan with either (1) the contribution amounts that its actuary calculated or (2) the amounts it was required to contribute by law or contract. If a government participates in a single-employer or agent multiple-employer plan, it most likely compares its actual annual contributions with amounts an actuary determined should be put in the plan each year (called an ACTUARIALLY DETERMINED CONTRIBUTION). (See Figure 30.) To provide context for understanding the size of the contributions, the government also presents a ratio that divides its actual contribution by covered payroll.

If a government participates in a cost-sharing multiple-employer pension or OPEB plan, its annual contribution amount probably is determined by (1) law or statute or (2) the terms of its contract with the plan. Therefore, its RSI schedule compares the contribution it actually made to the plan with its statutory or contractual contribution requirement. (See Figure E-3.) This schedule, too, contains a ratio of actual contributions divided by covered payroll.

Figure 29. Schedule of Net Pension Liability Information for a Government in a Cost-Sharing Plan

Himalaya Village
Schedule of Proportionate Share of the Net Pension Liability ①②
Past 10 Fiscal Years ③
(dollars in thousands) ④

	⑤ 20Y7	20Y6	20Y5	20Y4	20Y3	20Y2	20Y1	20Y0	20X9	20X8
District's proportion of the net pension liability (asset)	0.20%	0.19%	0.19%	0.19%	0.20%	0.20%	0.20%	0.21%	0.21%	0.21%
District's proportionate share of the net pension liability (asset)	$ 14,910	$ 11,738	$ 12,972	$ 13,495	$ 14,892	$ 11,605	$ 4,372	$ (2,355)	$ (1,264)	$ (926)
District's covered payroll	$ 11,512	$ 10,412	$ 9,715	$ 9,553	$ 9,522	$ 9,299	$ 8,709	$ 8,175	$ 7,909	$ 7,659
District's proportionate share of the net pension liability (asset) as a percentage of its covered payroll	129.52%	112.74%	133.53%	141.26%	156.40%	124.80%	50.20%	(28.81%)	(15.98%)	(12.09%)
Plan fiduciary net position as a percentage of the total pension liability	81.38%	83.20%	80.41%	78.53%	75.79%	79.74%	91.78%	104.52%	102.63%	102.10%

* The amounts presented for each fiscal year were determined as of 12/31.

Figure 30. Schedule of Actuarially Determined Employer Pension Contributions

Merritt County
① Schedule of Pension Plan Contributions ②
③ Past 10 Fiscal Years
(dollars in thousands) ④

	20X9	20X8	20X7	20X6	20X5	20X4	20X3	20X2	20X1	20X0
Actuarially determined contribution	$ 79,713	$ 86,607	$ 89,828	$ 91,963	$ 93,541	$ 85,681	$ 68,866	$ 29,849	$ 25,086	$ 22,826
Contributions in relation to the actuarially determined contribution	79,713	86,607	89,828	91,963	93,541	85,681	68,866	29,849	25,086	22,826
Contribution deficiency (excess)	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Covered payroll	$449,293	$436,424	$416,243	$407,812	$396,332	$381,554	$365,385	$323,896	$301,891	$274,318
Contributions as a percentage of covered payroll	17.74%	19.84%	21.58%	22.55%	23.60%	22.46%	18.85%	9.22%	8.31%	8.32%

⑤

Figure 29 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② If a government participates in a cost-sharing OPEB plan administered through a trust that meets the required criteria, it presents a schedule like this for OPEB as well.

③ This sample schedule presents a full 10 years for illustrative purposes. However, a government will build this schedule prospectively and, therefore, may present only a few years at this time.

④ Dollar amounts have been rounded off to the nearest thousand.

⑤ These amounts will be the same as those presented in the government's current-year note disclosure.

Figure 30 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② If a government has an actuarially determined contribution amount for its OPEB plan, it presents a schedule like this for OPEB as well.

③ This sample schedule presents a full 10 years for illustrative purposes. A government should have all of the information necessary to present all 10 years. However, it may build this schedule prospectively under certain circumstances and, therefore, may present only a few years at this time.

④ Dollar amounts have been rounded off to the nearest thousand.

⑤ As explained later in this section, a government adds notes to the schedule to explain how its actuarially determined contributions are established. (See Figure 31.) The note may appear here or on the next page.

What can you do with employer contribution information? You might use the information in these two schedules to determine whether additional resources need to be devoted to improving the funding of the pension plan. Alternatively, you might determine that the government should explore a reduction of contributions to an overfunded pension plan if the funding situation has been improving without providing additional contributions beyond those actuarially required.

Notes to the schedules

Figure 31 shows a note that a government adds to the schedule of actuarially determined contributions. It discloses the methodology and assumptions used to determine the contribution amounts. The methods and assumptions a government uses to calculate its contributions to the pension or OPEB

plan likely are different in some respects from the methods and assumptions it uses to measure the liability (and discloses in notes to financial statements).

If a government is aware of any factors that have a significant effect on the trend information in any of the RSI schedules—such as improvements or reductions to benefit provisions, expansion or reduction of the eligible population, or changes in the actuarial methods—it describes the factors in a note to the schedules. Such a note can be seen at the bottom of Figure 31.

Figure 31. Notes to Pension Schedule

Notes to Schedules

Valuation date: ①

Actuarially determined contribution rates are calculated as of June 30, two years prior to the end of the fiscal year in which contributions are reported.

Methods and assumptions used to determine contribution rates:

Actuarial cost method	Entry age
Amortization method	Level percentage of payroll, closed
Remaining amortization period	15 years
Asset valuation method	5-year smoothed market
Inflation	3.0%
Salary increases	4.0%, average, including inflation
Investment rate of return	7.75%, net of pension plan investment expense, including inflation
Retirement age	In the 20X7 actuarial valuation, expected retirement ages of general employees were adjusted to more closely reflect actual experience. In the 20X4 actuarial valuation, expected retirement ages of public safety employees were adjusted to more closely reflect actual experience.
Mortality	In the 20X1 actuarial valuation, assumed life expectancies were adjusted as a result of adopting the RP-2000 Healthy Annuitant Mortality Table. In prior years, those assumptions were based on the 1994 Group Annuity Mortality Table.

Other information:

In 20X1, benefit terms were modified to base public safety employee pensions on a final three-year average salary instead of a final five-year average salary.

Figure 31 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

- WHAT IS THE CONDITION OF GENERAL INFRASTRUCTURE ASSETS?
- IS THE CONDITION OF THESE ASSETS IMPROVING OR DETERIORATING?
- IS THE GOVERNMENT KEEPING PACE WITH THE NEED FOR PRESERVATION AND MAINTENANCE SPENDING?

Modified Approach Information about Infrastructure

If a government can demonstrate that its general infrastructure assets are preserved at or above the government's chosen condition level, the accounting standards allow it to report annual maintenance and preservation expenses (instead of depreciation) for those assets in the government-wide statement of net position. (Refer to the discussion of the modified approach in Part Four.) If a government uses the modified approach, it describes the approach in the SSAP note disclosure and presents the following RSI (see Figure 32):

- A schedule showing the physical condition of infrastructure for at least the three most recent condition assessments; assessments need to be performed at least every three years
- A schedule comparing for the past five years:
  - The annual amount *estimated* at the start of each year that would be necessary to maintain the infrastructure assets and preserve them at or above the government's chosen condition level *with*
  - The *actual* maintenance and preservation costs for those assets
- Notes to the schedules, disclosing:
  - How the physical condition of the assets is assessed and measured (in other words, the factors the government takes into account)
  - The measurement scale employed (for instance, if it is a 1–10 scale, what 1 means versus what 10 means)
  - The condition level the government has established as its benchmark for the assets
  - Any factors that had a significant effect on the trends in the information in the schedule, such as changes in the assessment methods, the measurement scale, or the government's established condition level
  - The effect on the estimated maintenance and preservation amounts of any changes in the government's established condition level.

Figure 32. Modified Approach Information

Condition Rating of the City's Street System

①	Percentage of Lane-Miles in Good or Better Condition			Percentage of Lane-Miles in Substandard Condition		
②	2017	2016	2015	2017	2016	2015
Main arterial	93.2%	91.5%	92.0%	1.7%	2.6%	3.1%
Arterial	85.2%	81.6%	84.3%	3.5%	6.4%	5.9%
Secondary	87.2%	84.5%	86.8%	2.1%	3.4%	3.8%
Overall system	88.2%	85.5%	87.3%	2.2%	3.6%	3.9%

③

Comparison of Needed-to-Actual Maintenance/Preservation (dollars in thousands)

	2017	2016	2015	2014	2013
Main arterial:					
Needed	$2,476	$2,342	$2,558	$2,401	$2,145
Actual	2,601	2,552	2,432	2,279	2,271
Arterial:					
Needed	1,485	1,405	1,535	1,441	1,287
Actual	1,560	1,531	1,459	1,367	1,362
Secondary:					
Needed	990	937	1,023	960	858
Actual	1,040	1,021	972	911	908
Overall system:					
Needed	$4,951	$4,684	$5,116	$4,802	$4,290
Actual	$5,201	$5,104	$4,863	$4,557	$4,541
Difference	$250	$420	($253)	($245)	$251

Note: The condition of road pavement is measured using the XYZ pavement management system, which is based on a weighted average of six distress factors found in pavement surfaces. The XYZ pavement management system uses a measurement scale that is based on a condition index ranging from zero for a failed pavement to 100 for a pavement in perfect condition. The condition index is used to classify roads in good or better condition (70–100), fair condition (50–69), and substandard condition (less than 50). It is the City's policy to maintain at least 85 percent of its street system at a good or better condition level. No more than 10 percent should be in a substandard condition. Condition assessments are determined every year.

Figure 32 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② This city assesses the physical condition of these infrastructure assets annually. The accounting standards require condition to be assessed at least once every three years.

③ In all three years, this City met its goal of keeping at least 85 percent of streets at good or better condition and less than 10 percent in substandard condition (see the note to the schedule).

What can you do with modified approach information?

A government's presentation about the modified approach provides a variety of useful information. For one thing, the overall physical status of major groups of infrastructure assets is indicated, as well as how conditions have changed over time. A careful crosswalk between the maintenance and preservation spending comparisons and the trend information about asset conditions may explain *how differences between needed and actual spending relate to the improvement or deterioration of the physical state of infrastructure.* This information can help with monitoring *whether a government is meeting targets for maintaining and preserving the assets.* It also alerts you to changes a government makes in its assessment methodology, measurement scale, and chosen level at which to maintain condition, and helps with assessing the impact those changes had on the trends in financial and asset condition information.

WHAT'S AHEAD?

- HOW DOES A GOVERNMENT MANAGE ITS RISK?
- WHAT LOSSES HAS A GOVERNMENT INCURRED FROM INSURANCE CLAIMS AND COURT JUDGMENTS?
- WHAT CLAIMS AND JUDGMENTS ARE LOOMING OVER THE HORIZON?

Public Entity Risk Pools

Risk pools were introduced in Part Five in the section on claims and judgments note disclosures. **By the numbers…reporting by risk pools** explains the circumstances under which a government would need to present RSI for a risk pool.

Reconciliation of claims liabilities by contract

Figure 33 illustrates one of the two RSI schedules presented by a risk pool: a **RECONCILIATION OF CLAIMS LIABILITIES BY CONTRACT.** This schedule takes cumulative information that a government discloses in its notes about a risk pool's **UNPAID CLAIMS LIABILITIES** (see Figure 26) and divides it into columns, one for each kind of insurance contract the pool offers. For each kind of contract, the schedule provides data for the current and immediately prior year.

The schedule is reminiscent of the note disclosures presenting changes in long-term liabilities. It begins with the outstanding balance of claims made to the fund that have not yet been settled and paid, which includes the fund's adjustment expenses for investigating and settling those unpaid claims. It then adds to the balance the amounts of claims and related adjustment expenses that were incurred during the year, before subtracting payments made during the year (1) on claims and (2) to the government for its expenses. In the case of both the incurred claims and payments, the schedule makes a distinction between those for the current year and those related to prior years. Insurance claims sometimes take a while to be resolved, which is why the schedule distinguishes between new claims activity for the current year and actions to resolve claims carried over from prior years.

What can you do with this information? One use for this information may be to track a risk pool's ability to keep pace with claims. Percentage change ratios can be calculated for unpaid claims and other data in the schedule to inform this issue. You may have noticed that the schedule actually has *three* years of unpaid claims data: the *beginning* balances for the earlier year (2016) are the same as the *ending* balances for the year prior to that (2015). Two sets of percentage changes could be calculated and compared—one for 2015–2016 and another for 2016–2017.

Figure 33. Reconciliation of Claims Liabilities by Contract

The schedule below presents the changes in claims liabilities for the past two years for the fund's two types of contracts: property and casualty, and employee health and accident benefits. *(dollars in thousands)*

① ②

	Property and Casualty		Employee Health and Accident	
	2017	2016	2017	2016
Unpaid claims and claim adjustment expenses, beginning of fiscal year	$ 762	$ 713	$ 659	$ 476
Incurred claims and claim adjustment expenses:				
Provision for insured events of the current year	513	360	769	540
Increases in provision for insured events of prior fiscal years	389	324	260	216
Total incurred claims and claim adjustment expenses	902	684	1,029	756
Payments:				
Claims and claim adjustment expenses attributable to insured events of the current fiscal year	256	180	385	270
Claims and claim adjustment expenses attributable to insured events of prior fiscal years	542	455	362	303
Total payments	798	635	747	573
Total unpaid claims and claim adjustment expenses, end of fiscal year	$ 866	$ 762	$ 941	$ 659

Figure 33 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② In order to obtain the unpaid claims and claims adjustment expenses amount for the end of the fiscal year, the balance of unpaid claims and claims adjustment expenses at the beginning of the fiscal year is added to total incurred claims and claims adjustment expenses for the year; then, total payments for the year are subtracted.

Ten-year claims development information

The second RSI schedule begins with a narrative that walks you through the information in the table that follows. (See Figure 34.) With a little bit of translation, it can be quite an informative description. Reinsurance is the process of "ceding" a portion of the risk of loss the fund faces. In other words, the fund takes out insurance of its own with a commercial firm (a "reinsurer") or another pool for a portion of the risk it has insured for the participating governments. Because the reinsurance firm (or another pool) has assumed that risk, it is removed or "netted" from the fund's information in the schedule.

The schedule essentially demonstrates how the process of estimating and eventually settling claims for "events" (for instance, employee illnesses and accidents) in a given year stretches over time. For example, according to row three, the claims incurred in 2008 were estimated as of the end of that year to be $235,000 (not including the $52,000 of claims the fund reinsured). During 2008, the fund paid $118,000 against those claims (in the row labeled "end of accident year"). Over the next 7 years (through 2015, "seven years later"), the fund eventually paid a total of $473,000 for those claims.

The total change from the original estimate to the most recent actual figure is listed in row seven. At first blush it appears that the fund's original estimates (line 7 of Figure 34) became less accurate between 2008 and 2012, and then became more accurate—the difference between the original estimate and the current actual rose from $238,000 to $400,000 before declining to $220,000 in 2016 and then zero. Further review should reveal the issue here—the most recent seven or eight years' actual payment figures will continue to grow and the difference between them and each year's original estimate will grow along with them. Can this information be useful, then, if it is incomplete? Yes, though it requires some technical massaging.

Figure 34: Net claims paid for the 2009 accident year were $124,000 in the first year and rose to $499,000 by the seventh year.

What can you do with this information? A relatively sophisticated trend analysis could be done that compares year-to-year percentage changes in the cumulative actual payment amount for each "policy year" to determine if the actual figures are veering away from the original estimates faster or slower

over time. Such an analysis is beyond the scope of this guide. However, we can consider what the results of this analysis could be used for without actually performing the calculations.

Figure 34. Schedule of 10-Year Claims Redevelopment Information

Ten-Year Loss Development Information (1)

The following table illustrates how the Plan's earned revenue (net of reinsurance) and investment income compare to related costs of loss (net of loss assumed by reinsurers) and other expenses assumed by the Program as of the end of the previous 10 years. The rows of the table are defined as follows:

(1) This line shows the total of each fiscal year's gross earned premiums and reported investment revenue, amounts of premiums ceded, and reported premiums (net of reinsurance) and reported investment revenue.

(2) This line shows each fiscal year's other operating costs of the Program including overhead and loss adjustment expenses not allocable to individual claims.

(3) This line shows the Program's gross incurred losses and allocated loss adjustment expense, losses assumed by reinsurers, and net incurred losses and loss adjustment expense (both paid and accrued) as orignially reported at the end of the year in which that event triggered coverage occurred (called accident year).

(4) This section of 10 rows shows the cumulative net amounts paid as of the end of successive years for each accident year.

(5) This line shows the latest reestimated amount of losses assumed by reinsurers for each accident year.

(6) This section of 10 rows shows how each accident year's net incurred losses increased or decreased as of the end of successive years. (This annual reestimation results from new information received on known losses, reevaluation of existing information on known losses, and emergence of new losses not previously known).

(7) This line compares the latest reestimated net incurred losses amount to the amound originally established (line 3) and shows whether this latest estimate of losses is greater or less than originally thought. As data for individual accident years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of net incurred losses currently recognized in less mature accident years. The columns of the table show data for successive accident years.

	Fiscal and Accident Year Ended (in thousands of dollars)									
	2008	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
(1) Premiums and investment revenue										
Earned	$ 908	$ 957	$ 1,357	$ 1,493	$ 1,479	$ 1,595	$ 1,811	$ 1,993	$ 2,192	$ 2,411
Ceded	366	387	559	615	624	686	754	830	913	1,004
Net earned	542	570	798	878	855	909	1,057	1,163	1,279	1,407
(2) Unallocated expenses	64	68	81	91	70	81	92	110	123	131
(3) Estimated losses and expenses, end of accident year:										
Incurred	287	303	453	503	569	651	780	909	1,092	1,512
Ceded	52	54	96	111	129	148	168	186	210	251
Net incurred	235	249	357	392	440	503	612	723	882	1,261
(4) Net paid (cumulative) as of:										
End of accident year	118	124	179	196	220	251	306	361	450	641
One year later	177	186	268	294	330	377	459	542	675	
Two years later	247	268	385	422	474	542	660	779		
Three years later	304	321	461	506	568	649	790			
Four years later	359	379	545	597	671	766				
Five years later	404	427	614	673	756					
Six years later	445	469	674	740						
Seven years later	473	499	717							
Eight years later	473	499								
Nine years later	473									
(5) Reestimated ceded losses and expenses	104	109	160	174	184	195	211	217	234	251
(6) Reestimated net incurred losses and expenses:										
End of accident year	235	249	357	392	440	503	612	723	882	1,261
One year later	294	311	447	490	550	628	765	898	1,102	
Two years later	338	357	513	563	632	722	874	1,028		
Three years later	380	401	577	632	710	811	982			
Four years later	422	446	641	703	789	902				
Five years later	449	474	682	748	840					
Six years later	468	494	710	779						
Seven years later	473	499	717							
Eight years later	473	499								
Nine years later	473									
(7) Increase (decrease) in estimated net incurred losses and expenses from end of accident year	238	250	360	387	400	399	370	305	220	

Figure 34 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

It clearly is important to the financial well-being of the risk pool that it accurately predict the level of claims activity and the cost of paying those claims. If it underestimates, it will not charge the participating governments enough in premiums to cover the claims. Analyzing past trends in this schedule should help the fund revise its estimates in later years. Learning from actual experience should enable the fund to make better original estimates over time.

SUPPLEMENTARY INFORMATION

WHAT'S AHEAD?

- WHAT CAPITAL ASSETS DOES A GOVERNMENT USE TO PROVIDE SERVICES?
- WHAT IS THE VOLUME, LEVEL OF USAGE, OR NATURE OF THOSE CAPITAL ASSETS?

Capital Asset Indicators

A government's statistical section includes an SI schedule with information that should enlighten your understanding of its capital assets. This schedule shows indicators of the volume, usage, or nature of the capital assets related to the functions and programs reported in a government's government-wide statement of activities (Figure 42, for example). The illustrative schedule in Figure 35 includes indicators such as the number of miles of streets, water mains, and sewers; the acreage of parks and number of athletic fields; and the number of garbage trucks and minibuses.

What can you do with capital asset indicators?

These indicators add an important layer of meaning to the capital asset information in the financial statements and notes. The indicators in this schedule tell you much more about what those capital assets actually are—not just a category such as "infrastructure," but specifically X,XXX miles of streets and highways, YY number of bridges, and a sewage treatment capacity of ZZZ millions of gallons a day. It gives you a context for analyzing the financial information about capital assets because you know something about what kinds of capital assets a government has and how many of them it owns.

Figure 35. Statistical Section Schedule of Capital Asset Indicators

City of Phenomenal
Capital Asset Statistics by Function/Program
Last 10 Fiscal Years

	Fiscal Year									
Function/Program	**20X0**	**20X1**	**20X2**	**20X3**	**20X4**	**20X5**	**20X6**	**20X7**	**20X8**	**20X9**
Police										
Stations	2	2	2	2	2	2	2	2	2	2
Zone offices	3	3	3	3	3	3	3	4	5	5
Patrol units	24	24	24	25	26	26	25	28	32	33
Fire stations	6	6	6	6	6	6	6	6	6	6
Refuse collection										
Collection trucks	8	8	8	8	7	7	7	8	8	8
Other public works										
Streets (miles)	367.5	371.2	375.0	378.8	382.6	386.4	390.4	394.3	398.3	402.3
Highways (miles) [a]	81.6	81.6	81.6	81.6	81.6	107.4	107.4	107.4	107.4	107.4
Streetlights	7,455	7,531	7,607	7,683	7,761	7,839	7,919	7,999	8,079	8,161
Traffic signals	93	94	98	98	98	101	105	105	106	106
Parks and recreation										
Acreage	309	309	309	309	309	309	309	309	309	309
Playgrounds	23	23	23	23	23	23	25	25	25	25
Baseball/softball diamonds [b]	38	38	38	38	39	30	39	39	39	41
Soccer/football fields [b]	25	25	30	35	35	32	35	35	35	35
Community centers	5	5	5	5	5	5	5	5	5	5
Water										
Water mains (miles)	469.5	474.3	479.1	483.9	488.8	493.7	498.7	503.8	508.9	514.0
Fire hydrants	3,170	3,202	3,234	3,267	3,300	3,333	3,367	3,401	3,435	3,470
Storage capacity (thousands of gallons)	5,500	5,500	5,500	5,500	5,500	5,500	5,500	5,500	5,500	5,500
Wastewater										
Sanitary sewers (miles)	442.5	447.0	451.5	456.1	460.7	465.3	470.0	474.8	479.6	484.4
Storm sewers (miles)	309.2	312.3	315.5	318.7	321.9	325.2	328.4	331.8	335.1	338.5
Treatment capacity (thousands of gallons)	3,200	3,200	3,200	3,200	3,550	3,550	3,550	3,550	3,550	4,200
Transit–minibuses	3	3	3	3	3	4	4	4	4	4

① ② ③

Sources: Various City departments.

Note: No capital asset indicators are available for the general government or library function.

[a] The Seabury Memorial Highway opened in 20X5.

[b] The 12 athletic fields in Schoonmaker Park were out of service during most of 20X5 while they were rehabilitated.

Figure 35 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② A government will identify the source of any information in the statistical section that does not come from elsewhere in the financial report.

③ Only available indicators are required to be reported. If a government does not have capital asset indicators for one of its functions or programs, it will indicate this fact.

Figure 35: Miles of water mains increased from 469.5 in 20X0 to 514.0 in 20X9.

The schedule also helps you to determine whether a government's capital assets are growing. You can tell what has been added during periods with significant capital expenditures by identifying indicators that have increased. You can also get a sense of a government's priorities for capital investment (and how those priorities may have changed) by calculating which indicators have increased by the largest percentages.

WHAT'S AHEAD?

- HOW HAS A GOVERNMENT'S DEBT BURDEN CHANGED OVER THE LAST 10 YEARS?
- WHAT DEBTS OF OTHER GOVERNMENTS ARE A GOVERNMENT'S TAXPAYERS ALSO REPAYING?
- IS A GOVERNMENT RAISING SUFFICIENT REVENUES TO REPAY ITS REVENUE-BACKED DEBT?

Debt Service Ratios

A government's statistical section includes an SI schedule of changes in governmental fund balances. (See Figure 66, which is discussed more fully in Part Nine.) In the expenditures portion of this schedule, a government presents the 10 years of debt service expenditures in separate principal and interest components. A government also presents a debt service ratio for each year—total debt service expenditures divided by total *noncapital* expenditures. (The expenditures for capital assets are removed.) You should be mindful that, because this ratio is calculated from debt service expenditures from the governmental funds, it relates only to the *general bonded debt* of the government. Other long-term debts, such as water bonds and other BTA-related debt, are not encompassed by this information.

What can you do with debt service ratios?

This ratio is a measure of the burden that repaying long-term general debt places on the general resources of the government. The ratio shows the percentage of the government's annual operating expenditures that are related to repaying debt—the portion of the budget that is consumed to repay

long-term bonds. You can monitor this ratio over time to determine if debt service is growing or shrinking relative to the government's other expenditures for providing services.

Some analysts view a ratio of debt service divided by total operating expenditures as an indicator of budget flexibility: the higher the ratio, the less flexibility a government has to determine its spending priorities. By the same token, a rising debt service ratio would indicate to these analysts a declining ability to devote resources to discretionary spending; in other words, spending on purposes a government itself chooses, as opposed to spending on purposes imposed on the government (mandated) by other governments.

Lastly, the ratio can be compared with similar governments to determine the relative size of the government's debt service costs.

Debt Capacity

A government's statistical section contains five SI schedules of information about its outstanding debt. The purpose of this information is to help you understand and assess the government's current debt burden and its ability to issue debt in the future.

Trends in ratios of outstanding debt

Two of the schedules show a government's outstanding debt for the last 10 years. The first includes all of the government's outstanding debt instruments by type—GENERAL OBLIGATION (GO) DEBT, REVENUE-BACKED DEBT, loans, CERTIFICATES OF PARTICIPATION (COPs), capital leases, and so on. (See Figure 36.) The outstanding debt is presented separately for governmental and business-type activities, and a total is shown for the whole government. The total for the government is used to produce two ratios:

- DEBT PER CAPITA (outstanding debt divided by the total population of the government's jurisdiction)
- Outstanding debt as a percentage of personal income.

Figure 36: Total primary government debt as a percentage of personal income was 4.12% in 20X9.

The second SI schedule includes only the government's general bonded debt—GO bonds or other bonded debt that is repaid with the general revenues of the government (as opposed to being repaid with a dedicated revenue source, like revenue-backed debt). (See Figure 37.) This schedule also includes two ratios—per capita debt and debt as a percentage of total ESTIMATED ACTUAL VALUE OF TAXABLE PROPERTY.

What can you do with trends in ratios of outstanding debt? The information in a government's financial report gains new meaning when you place it in a context that allows for comparisons—over time for a particular government, among various governments, or both. These statistical section schedules allow you to follow the government's outstanding debt levels over a decade. One of the first things you may want to do with them is to calculate percentage change ratios. The formula is simple:

(amount from the most recent year – amount from the earliest year)

÷ amount from the earliest year

Figure 36. Statistical Section Schedule of Debt Ratios

City of Monumental
Ratios of Outstanding Debt by Type ①
Last 10 Fiscal Years
(dollars in thousands, except per capita)

	Governmental Activities					Business-Type Activities						
Fiscal Year	General Obligation Bonds	Redevelopment Bonds	Sales Tax Increment Bonds	Lease Revenue Bonds [a]	Special Assessment Bonds	Water Bonds	Term Loan Payable	Certificates of Participation	Capital Leases	Total Primary Government	Percentage of Personal Income [b]	Per Capita [b]
20X0	$ 10,990	$ —	$ 6,176	$ 20,921	$ 34,495	$ —	$ —	$ —	$ 1,023	$ 73,605	3.10%	$ 834
20X1	10,510	—	5,947	20,357	33,095	—	—	—	1,009	70,918	2.86	766
20X2	9,995	47,050	5,700	19,765	31,565	—	—	—	985	115,061	4.41	1,218
20X3	9,455	46,610	5,437	19,145	29,875	—	—	—	951	111,473	4.23	1,136
20X4	9,630	55,455	5,157	18,497	27,995	—	—	—	909	117,642	4.18	1,183
20X5	8,925	54,903	4,859	17,821	25,895	—	—	7,010	860	120,273	4.21	1,170
20X6	8,290	54,251	4,545	17,117	23,545	36,690	—	6,880	804	152,122	4.93	1,364
20X7	7,625	53,335	4,213	16,385	20,915	36,490	22,244	6,615	743	168,566	4.91	1,437
20X8	6,925	52,380	3,865	15,625	17,975	36,245	21,989	6,180	849	162,033	4.31	1,317
20X9	6,190	51,375	3,499	22,810	14,695	35,585	21,097	5,940	801	161,992	4.12	1,234

②

Notes: Details regarding the City's outstanding debt can be found in the notes to financial statements. Totals may not add due to rounding.

[a] In addition to $15.6 million of refunding lease revenue bonds, the City issued over $7 million of new lease revenue bonds in 20X9.

[b] See Schedule R for personal income and population data. These ratios are calculated using personal income and population for the prior calendar year.

Figure 36 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② The personal income and population data used to calculate these ratios can be found in the government's statistical section schedule of demographic and economic statistics (see, for example, Figure 94).

Figure 37. Statistical Section Schedule of General Bonded Debt Ratios

City of Monumental
Ratios of General Bonded Debt Outstanding ①
Last 10 Fiscal Years
(dollars in thousands, except per capita)

Fiscal Year	General Bonded Debt Outstanding: General Obligation Bonds	General Bonded Debt Outstanding: Redevelopment Bonds	General Bonded Debt Outstanding: Total	Percentage of Actual Taxable Value [a] of Property	Per Capita [b]
20X0	$ 10,990	$ —	$ 10,990	0.21%	$ 125
20X1	10,510	—	10,510	0.19	114
20X2	9,995	47,050	57,045	1.08	604
20X3	9,455	46,610	56,065	1.04	571
20X4	9,630	55,455	65,085	1.20	654
20X5	8,925	54,903	63,828	1.12	621
20X6	8,290	54,251	62,541	1.00	561
20X7	7,625	53,335	60,960	0.89	520
20X8	6,925	52,380	59,305	0.76	482
20X9	6,190	51,375	57,565	0.66	439

②

Note: Details regarding the City's outstanding debt can be found in the notes to financial statements.

[a] See Schedule H for property value data. ③

[b] Population data can be found in Schedule R.

Figure 37 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② If a government has resources that are restricted to repaying the *principal* of outstanding general bonded debt, then it shows them between these columns and calculates the debt ratios *net* of the restricted resources.

③ Property values can be found in the government's statistical section schedule of property tax base information (assuming a government's most significant own-source revenue is a property tax). See Figure 48 for an example of that schedule.

Multiply the result by 100 and you have the percentage by which debt increased or decreased over the period. For example, the percentage change from 20X0 to 20X9 in total outstanding debt for the primary government in Figure 36 would be calculated as follows:

$$(\$161{,}992 - 73{,}605) \div 73{,}605 = 1.20 \times 100 = 120 \text{ percent}$$

In other words, outstanding debt increased 120 percent over that 10-year period.

You could calculate the ratios not only for the whole 10 years, but for the first and second 5 years as well. You can begin to answer questions such as: Does the government owe more or less than it did 10 years ago? What kinds of debt accounted for the growth or decline? When did the growth or decline take place?

Figure 37: General bonded debt per capita in 20X7 was $520.

The per capita ratio is useful for cross-government comparisons. All other factors being equal, a government with a higher per capita ratio has a larger debt burden and may be less financially capable of adding more debt. Of course, not all other factors *are* equal, so be careful when you make comparisons and draw conclusions.

The ratios of debt-to-personal-income and debt-to-property-values speak to the burden the outstanding debt load places on the local economy. By comparing outstanding debt with an indicator of the economic base from which it is financed, you get a sense of how much of that particular economic activity would be necessary to repay the debt. For instance, imagine a county with general bonded debt outstanding equal to 10 percent of the actual taxable value of property. How big is its burden? If other counties in the same state had an average ratio of 15 percent, the county would appear relatively less burdened and therefore potentially better able to afford more debt if needed. If the ratios of general bonded debt schedule showed that the county's ratio had grown from 5 percent to 10 percent over the past 10 years, you might temper your assessment of its capacity to issue more debt. Yes, the county compares favorably with other similar governments, but its burden has risen rapidly in recent years.

Direct and overlapping debt

This SI schedule provides more comprehensive information about the debt burden on a particular jurisdiction by adding together not only the debt related to the governmental activities of the reporting government, but also a portion of the governmental activities debt of all other governmental entities that overlap geographically, at least in part, with the reporting government. The outstanding debt amounts for the current year for the overlapping governments are shown in the first of three columns in Figure 38.

Figure 38. Statistical Section Schedule of Direct and Overlapping Debt

City of Monumental
① Direct and Overlapping Governmental Activities Debt
As of June 30, 20X9
(dollars in thousands)

Governmental Unit	② Debt Outstanding	③ Estimated Percentage Applicable [a]	④ Estimated Share of Overlapping Debt
Debt repaid with property taxes			
Willow Pond School District	$ 55,655	75.313%	$ 41,915
Willow Pond School District Facilities District #1	5,247	100.000%	5,247
Willow Pond School District Facilities District #2	3,253	86.622%	2,818
Willow Pond School District Facilities District #3	2,286	90.114%	2,060
Suarez County General Obligation Debt	627,809	10.386%	65,204
Other debt			
Suarez County Capital Leases	11,546	10.386%	1,199
Suarez County Economic Development Bonds	95,688	8.154%	7,802
Suarez County Loan: State Environmental Revolving Fund	31,648	10.386%	3,287
Suarez County—other debt	14,675	10.386%	1,524
Subtotal, overlapping debt			131,057
City direct debt		⑤	98,569
Total direct and overlapping debt			$ 229,626

Sources: Assessed value data used to estimate applicable percentages provided by the Suarez County Board of Equalization and Assessment. Debt outstanding data provided by each governmental unit.

Note: Overlapping governments are those that coincide, at least in part, with the geographic boundaries of the City. This schedule estimates the portion of the outstanding debt of those overlapping governments that is borne by the residents and businesses of Monumental. This process recognizes that, when considering the City's ability to issue and repay long-term debt, the entire debt burden borne by the residents and businesses should be taken into account. However, this does not imply that every taxpayer is a resident, and therefore responsible for repaying the debt, of each overlapping government.

[a] For debt repaid with property taxes, the percentage of overlapping debt applicable is estimated using taxable assessed property values. Applicable percentages were estimated by determining the portion of another governmental unit's taxable assessed value that is within the City's boundaries and dividing it by each unit's total taxable assessed value. This approach also was used for Suarez County's capital lease, loan, and other debt. The applicable percentage of Suarez County Economic Development Bonds, which are backed by County sales taxes, was estimated by dividing the City's retail sales by the County's retail sales.

Figure 38 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② These are the total outstanding debt amounts for the overlapping governments.

③ This column presents the percentage of overlap relevant to each type of outstanding debt.

④ The overlapping debt amounts are calculated by multiplying the first two columns.

⑤ This direct debt amount of the reporting government is the sum of the governmental activities debt in the statistical section schedule of debt ratios (Figure 36).

The middle column shows the percentage of the debt from the overlapping governments that is applicable to the government's geographic jurisdiction. The calculation required to obtain this percentage is fairly straightforward:

The portion of the economic base from which the debt is repaid that is within the area where the government overlaps with the other government

÷

The total of that economic base for the overlapping government.

For example, for debt repaid with property taxes:

The property value in the area of overlap

÷

The property value in the whole overlapping government.

This percentage is multiplied by the outstanding debt amount to produce the amount of **OVERLAPPING DEBT** applicable to the government preparing the schedule (see the third column). The total overlapping debt is then added to the governmental activities debt of that government to obtain a total direct and overlapping debt amount ($229,626,000 in Figure 38).

What can you do with information about direct and overlapping debt? Any given person or corporation resides within the geographic boundaries of multiple governments. For instance, a person may live in a village, within a town, within a county. That person also probably lives in a school district, and could possibly live within several other special districts, such as a fire district or a library district. All of those governments derive their revenues from the same general geographic area and the same economy. If they have debt, the same taxpayers or customers are providing the resources that will be used to repay it. It could be valuable, then, to see all of the debt that the taxpayers in a particular area will have to repay.

Figure 38: Facilities District #1 is located entirely within the City of Monumental and, therefore, 100% of its debt is considered overlapping debt.

You can calculate the same kinds of debt ratios required for total debt and general bonded debt for total direct and overlapping debt, too. You could divide it by population to obtain a per capita ratio, or by total personal income or property value. If you calculate those ratios over time using this schedule from several years' financial reports, you can tell whether the overlapping burden is changing, whether the change has been greater because of the reporting government's debt or that of the overlapping governments, and which overlapping government's debt has had the biggest impact on the growth or reduction in debt over the years.

Debt limitations

One reason for examining a government's debt capacity is to assess whether it has the financial wherewithal to issue more debt (and repay it) should the need arise. However, potential capacity for issuing more debt may not mean anything if the amount of debt a government can issue is legally or constitutionally limited. In fact, most governments are limited by state laws or by constitutional or charter provisions in the amount of debt they can have outstanding at any given time. A government's statistical section includes an SI schedule about such limitations.

For the current year, the schedule a government presents includes the details of how its debt limit is calculated. Quite often, the debt limit is a function of property values—outstanding debt may not exceed a certain percentage of property value. Figure 39 illustrates a typical **LEGAL DEBT LIMIT** calculation. The government in this illustration is limited by state law to total debt that is no more than 15 percent of its assessed property value. The calculation compares the outstanding debt that is applicable to the limit (not all of a government's debt may be covered by the limitation—in fact, legal limitations often apply only to general bonded debt) with the debt limit. In many instances, governments may be allowed by the law to subtract from their outstanding debt any amounts governments have set aside specifically to repay debt. The resulting "net" applicable debt amount is subtracted from the debt limit to obtain the **LEGAL DEBT MARGIN**—the amount of additional debt that a government is legally empowered to issue.

Figure 39: Total net debt equaled 0.84% of the debt limit in 20X4.

Although the calculation is presented only for the most recent year, the debt limitation schedule includes the key pieces of information from that calculation for each of the last 10 years: the debt limit, the total debt applicable to the limit, and the legal debt margin. The government also includes one of two ratios:

- Total debt (or net debt) applicable to the debt limit ÷ the debt limit, or
- Legal debt margin ÷ the debt limit.

What can you do with debt limitation information? If you wish to assess a government's debt capacity, you need to keep two important factors in mind—its *financial ability* to issue debt and its *legal authority* to issue debt. Even if you decide, with the help of the debt ratios described above, that a government can afford to issue more long-term debt, you may find that it has very little legal debt margin left; in other words, it may not be legally allowed to issue as much debt as you believe it could afford. Conversely, the government may have plenty of legal borrowing power available, but your assessment may conclude that it would have difficulty repaying any more debt than it already has.

Figure 39. Statistical Section Schedule of Debt Limitation Information

City of Monumental
① Legal Debt Margin Information
Last 10 Fiscal Years
(dollars in thousands)

② Legal Debt Margin Calculation for Fiscal Year 20X9

Assessed value	$ 8,749,439
Debt limit (15% of assessed value)	1,312,416
Debt applicable to limit:	
General obligation bonds	6,190
Less: Amount set aside for repayment of general obligation debt	(1,862)
Total net debt applicable to limit	4,328
Legal debt margin	$ 1,308,088

	Fiscal Year									
	20X0	20X1	20X2	20X3	20X4	20X5	20X6	20X7	20X8	20X9
Debt limit	$ 778,056	$ 809,183	$ 794,616	$ 806,512	$ 813,273	$ 857,151	$ 935,519	$ 1,027,994	$ 1,173,729	$ 1,312,416
Total net debt applicable to limit	9,234	8,634	7,830	7,241	6,810	6,270	7,144	4,360	1,227	4,328
Legal debt margin	$ 768,822	$ 800,547	$ 786,786	$ 799,271	$ 806,463	$ 850,881	$ 928,375	$ 1,023,634	$ 1,172,502	$ 1,308,088
Total net debt applicable to the limit as a percentage of debt limit ③	1.19%	1.07%	0.99%	0.90%	0.84%	0.73%	0.76%	0.42%	0.10%	0.33%

Note: Under state finance law, the City's outstanding general obligation debt should not exceed 15 percent of total assessed property value. However, the City has established a more conservative internal limit of no more than 5 percent. By law, the general obligation debt subject to the limitation may be offset by amounts set aside for repaying general obligation bonds. ④

Figure 39 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② Governments are required to present the full calculation of the legal debt margin only for the most recent year.

③ Alternatively, a government may report a ratio of the legal debt margin to the debt limit.

④ Governments describe the nature of the legal limitations governing their outstanding debt.

The debt limitation ratio that a government includes in this schedule provides a quick check on its legal ability to issue debt. If the ratio compares outstanding debt to the debt limit (as in Figure 39), you can see how much of the government's borrowing power has been used up. The government in Figure 39 has used only a tiny fraction of its legal borrowing power—one-third of 1 percent. If the government shows the other ratio—legal debt margin divided by the debt limit—you can see how much of the government's legal borrowing power remains. If this ratio had been calculated for the government in Figure 39, the ratio for 20X9 would have been 99.67 percent; in other words, virtually all of its legal borrowing power remains untapped.

As previously noted, an important caveat is that not all of a government's debt may be subject to legal limitations. In fact, only the GO debt of the government in Figure 39 is subject to legal limitations. But it also has other long-term debts, such as water bonds and special assessment bonds. (Refer to Figure 36.) In addition, the taxpayers of that government are responsible for repaying a portion of the outstanding debts of overlapping governments in which they reside. (Refer to Figure 38.) This government has relatively little GO debt outstanding and, therefore, plenty of legal authority to issue more; however, the sum of its other outstanding long-term debts may amount to a financial burden that limits how much more GO debt the government's taxpayers actually can afford to repay.

Pledged-revenue coverage

Underlying your assessments of a government's ability to issue more debt is the concept of affordability—can the government obtain sufficient resources to repay the debt when it comes due? The debt service information described above can help you to understand the financial burden of repaying long-term debt and the demand that repaying debt will place on the government in the future. In order to increase their ability to finance additional outstanding debt, governments often diversify their outstanding debt by issuing debt instruments that are repaid from different revenue sources to lessen the burden on any given revenue. (One should be mindful that diversification may ease the burden on a particular revenue source of repaying debt, but it does not reduce the *overall* financial burden on a government. In fact, it may be quite the opposite—it could lead to a *greater* overall burden if more debt is issued than would have been the case if fewer revenue sources were available to repay debt.)

One way in which governments diversify their debt is to issue long-term bonds and pledge a particular revenue stream to repaying them. A government's statistical section includes an SI schedule that identifies such **PLEDGED-REVENUE DEBT** and compares its annual debt service for the past 10 years with the resources that were raised to pay it. (See Figure 40.) For each type of debt backed by pledged revenues, a government identifies the relevant revenues and shows the amount for each year. That amount is divided by the debt service for that year to produce a **DEBT SERVICE COVERAGE RATIO**. For example, in Figure 40, the debt service in 20X9 for the special assessment bonds was $8,251,000 ($3,280,000 plus 4,971,000), and the special assessment revenues pledged to repay that debt were $8,625,000. The coverage ratio was 1.05—the revenues amounted to 5 percent more than was needed to pay the debt service in that year.

For certain debt backed by pledged revenues, particularly those related to a BTA, the revenue stream also may be used to pay for annual operating costs. In such cases, those operating costs are subtracted from the pledged revenues before the coverage ratio is calculated. The utility service charges pledged to repay the water revenue bonds in Figure 40 were $30,903,000 in 20X9. After subtracting $13,906,000 of operating expenses, the $16,997,000 of "net available revenue" are divided by the debt service (principal plus interest) of $2,288,000 to obtain a coverage ratio of 7.43. In other words, the net pledged revenue was sufficient to pay that year's debt service more than seven times over.

Figure 40: Net available revenue for water revenue bonds was 7.62 times greater than debt service in 20X8.

What can you do with information about pledged-revenue coverage? Sometimes when a decision is made to pledge a revenue stream to repay debt, there is an expectation that the revenue will be sufficient and no general resources will be required. In that way, the debt service is not seen as competing with other costs, particularly public services, for scarce resources. This schedule can help you determine whether the pledged revenues have been sufficient to cover the debt service costs, or whether a government had to use other revenues to make the payments. You can see in Figure 40 that from 20X2 to 20X5, the special assessment did not produce enough revenue to cover the annual debt service—the coverage ratio was below 1.0. You also can tell if coverage has improved or fallen off over time.

Figure 40. Statistical Section Schedule of Pledged-Revenue Coverage

① **City of Monumental**
Pledged-Revenue Coverage
Last 10 Fiscal Years
(dollars in thousands)

Fiscal Year	② Water Revenue Bonds: Utility Service Charge	Less: Operating Expenses	Net Available Revenue	Debt Service: Principal	Debt Service: Interest	Coverage	Special Assessment Bonds: Special Assessment Collections	Debt Service: Principal	Debt Service: Interest	Coverage	Sales Tax Increment Bonds [a]: Sales Tax Increment	Debt Service: Principal	Debt Service: Interest	Coverage
20X0	$ —	$ —	$ —	$ —	$ —	—	$ 9,172	$ 1,300	$ 6,963	1.11	$ 944	$ 310	$ 212	1.81
20X1	—	—	—	—	—	—	9,088	1,400	6,862	1.10	938	300	229	1.78
20X2	—	—	—	—	—	—	7,757	1,530	6,722	0.94	959	288	247	1.79
20X3	—	—	—	—	—	—	7,829	1,690	6,595	③ 0.95	1,178	276	263	2.18
20X4	—	—	—	—	—	—	7,996	1,880	6,363	0.97	1,188	264	280	2.19
20X5	—	—	—	—	—	—	7,531	2,100	6,131	0.92	1,263	250	298	2.31
20X6	30,521	13,734	16,787	710	1,577	7.34	8,444	2,350	5,888	1.03	1,332	236	314	2.42
20X7	31,124	14,006	17,118	735	1,550	7.49	8,568	2,630	5,648	1.04	1,731	220	332	3.13
20X8	31,685	14,258	17,427	765	1,522	7.62	8,688	2,940	5,334	1.05	1,874	204	348	3.39
20X9	30,903	13,906	16,997	795	1,493	7.43	8,625	3,280	4,971	1.05	2,216	187	366	4.00

Note: Details regarding the City's outstanding debt can be found in the notes to financial statements. Operating expenses do not include interest, depreciation, or amortization expenses.

[a] Sales tax increment bonds are backed by the sales tax revenue produced by the sales tax rate in effect when the bonds were issued (2.5 percent) applied to the increase in retail sales in the Commons shopping area since that time. ④

Figure 40 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② If a revenue stream pledged to repay the debt of a particular activity also is used to finance the operating costs of that activity, the operating expenses are removed from the revenues before calculating the coverage ratio.

③ During 20X2–20X5, the special assessment collections were not sufficient to pay the annual debt service. General revenues were needed in those years to cover the shortfall.

④ If the revenue source pledged to repay debt is not clearly identifiable from the column headings, the government describes it in a note to the schedule.

Figure 41 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Figure 41. Statistical Section Schedule of Net Assets/Position

City of Chronological
① Net Assets/Position by Component
Last 10 Fiscal Years
(accrual basis of accounting)

	Fiscal Year									
	20X0	20X1	20X2	20X3	20X4	20X5 [a]	20X6	20X7	20X8	20X9
Governmental activities										
Net investment in capital assets	$ 221,991,132	$ 233,674,876	$ 245,973,553	$ 258,919,530	$ 272,546,873	$ 286,891,446	$ 301,990,995	$ 317,885,258	$ 334,616,061	$ 352,227,433
Restricted	43,936,163	46,248,593	48,682,729	51,244,978	53,942,082	56,781,139	59,769,620	62,915,390	66,226,726	69,712,343
Unrestricted	18,513,223	19,487,604	20,513,267	21,592,913	22,729,382	23,925,665	25,184,910	26,510,432	27,905,718	29,374,440
Total governmental activities net assets/position	$ 284,440,518	$ 299,411,073	$ 315,169,549	$ 331,757,421	$ 349,218,337	$ 367,598,250	$ 386,945,525	$ 407,311,080	$ 428,748,505	$ 451,314,216
Business-type activities										
Net investment in capital assets	$ 81,071,745	$ 85,338,679	$ 89,830,189	$ 94,558,093	$ 99,534,835	$ 104,773,511	$ 110,287,906	$ 116,092,532	$ 122,202,666	$ 128,634,385
Unrestricted	29,767,571	31,334,286	32,983,459	34,719,430	36,546,769	38,470,283	40,495,034	42,626,352	44,869,844	47,231,415
Total business-type activities net assets/position	$ 110,839,316	$ 116,672,965	$ 122,813,648	$ 129,277,523	$ 136,081,604	$ 143,243,794	$ 150,782,940	$ 158,718,884	$ 167,072,510	$ 175,865,800
Primary government										
Net investment in capital assets	$ 303,062,877	$ 319,013,555	$ 335,803,742	$ 353,477,623	$ 372,081,708	$ 391,664,956	$ 412,278,901	$ 433,977,791	$ 456,818,727	$ 480,861,818
Restricted	43,936,163	46,248,593	48,682,729	51,244,978	53,942,082	56,781,139	59,769,620	62,915,390	66,226,726	69,712,343
Unrestricted	48,280,795	50,821,889	53,496,726	56,312,343	59,276,150	62,395,948	65,679,945	69,136,784	72,775,562	76,605,855
Total primary government net assets/position	$ 395,279,835	$ 416,084,037	$ 437,983,197	$ 461,034,944	$ 485,299,940	$ 510,842,043	$ 537,728,466	$ 566,029,965	$ 595,821,015	$ 627,180,016

[a] Beginning in 20X5, the City began reporting net position rather than net assets, in accordance with GASB Statement 63. Prior to that time, net investment in capital assets was labeled invested in capital assets, net of related debt.

WHAT'S AHEAD?

- WHAT RESOURCES CAN A GOVERNMENT USE TO PROVIDE SERVICES IN THE FUTURE?
- ARE THERE ANY LIMITATIONS PLACED ON HOW THOSE RESOURCES CAN BE USED?
- HOW HAVE A GOVERNMENT'S RESIDUAL BALANCES CHANGED OVER TIME?

Trends in Net Position

The statistical section contains an SI schedule that shows the three components of net position—net investment in capital assets, restricted, and unrestricted—for the last 10 years. (See Figure 41.) Net position is shown separately for the governmental and business-type activities and is then totaled.

Figure 41: Net investment in capital assets for the governmental activities in 20X9 was $352,227,433.

What can you do with trends in net position?

This information can help you to understand how a government's net position changed over time, both in the aggregate and for the individual components. Is the portion of the government's assets represented by its infrastructure and other long-lived assets larger or smaller over time? Can more or less of its net position be used for any purpose, or is it restricted to specific uses? As with other trend information, you can compute percentage change ratios for each year, and for multiple years (such as the first and last 5 years or the entire 10-year period).

GENERAL OBLIGATION (GO) DEBT is debt backed by a government's full faith and credit and usually repaid with a government's general resources

ESTIMATED ACTUAL VALUE OF TAXABLE PROPERTY is the market value of real or personal property that is subject to taxation

LEGAL DEBT MARGIN is the amount of debt a government is legally empowered to issue *less* the actual amount of debt it has outstanding

a DEBT SERVICE COVERAGE RATIO is a measure of the degree to which revenues pledged to repay debt are sufficient to cover debt service payments on that debt

Keep in mind...the number of years in pension and OPEB RSI schedules

Ultimately, the RSI schedules for pensions and OPEB will cover the past 10 fiscal years. However, the information about changes in the NPL or NOL and related ratios is not available for the years prior to when governments implemented the existing standards—principally fiscal year 2015 for pensions and (as explained in **Keep in mind...implementation dates for OPEB reporting** on page 110) fiscal year 2018 for OPEB. Consequently, a government will build its schedules prospectively each year until it eventually contains a full 10 years. A government may be able to present a full 10 years from the start for the employer contributions schedules because that information likely was collected and reported previously.

By the numbers...OPEB and covered-employee payroll

If your government presents the schedules described on pages 125–132 for OPEB, the ratios in the schedules may utilize covered payroll. However, if the OPEB your government provides to its employees is *not* determined based on a measure of

pay (for instance, the benefit equals a flat dollar amount per retiree instead of, say, 3 percent of pay), there are two differences in the OPEB schedules:

- There is no ratio of the NOL divided by covered payroll in the schedule of changes in the NOL and related ratios.
- In the schedule of employer contributions, actual contributions are divided by **COVERED-EMPLOYEE PAYROLL** rather than covered payroll. Covered-employee payroll is defined as *total* pay.

By the numbers…freestanding pension plan statements

If a government's pension or OPEB plan produces its own publicly available annual report containing the required information, the government's reporting requirements are reduced, as explained in the text. Governments are required in this situation to explain how readers can obtain a copy of the pension (or OPEB) plan's report.

By the numbers…reporting by risk pools

Risk pools often are separate governmental entities that prepare and publish their own annual financial statements. When they do, they include in their RSI the information discussed in this section. If a risk pool is operated or sponsored by a particular government (say, a state government on behalf of its localities) and is legally a part of that government, it will be reported among that government's enterprise funds in its financial statements. If the risk pool does not issue its own financial statements, the primary government will present these RSI disclosures following the notes to its financial statements.

Upon further review…the claims development schedule

After 2015, the fund in Figure 34 did not pay for any more claims from 2008. (You can see that the amount remains the same in the rows for seven through nine years later.) The same appears to be true for 2009—the original estimate of $249,000 topped out at $499,000 in actual payments 7 years later in 2016. The figures in the remaining columns are still "live," meaning that they may yet grow as more years pass. The $717,000 payment amount for 2010 as of 2017 (7 years later) may be larger in 2018. The amounts for 2011 through 2017 almost certainly will get bigger.

By the numbers…notes to the statistical section schedules

Governments do not expect you to consume all of the information in the statistical section without some aids to digestion. For instance, if the schedules contain information that does not come from another part of the financial report, a government identifies the source of the information. A government also reveals any assumptions underlying the information and explains the methodologies employed to produce it. For instance, in the schedule of direct and overlapping debt (see Figure 38) the government tells you how it calculated the overlapping debt amounts and the economic bases it used to determine the percentage of overlap.

Governments also include explanatory notes with the schedules. These notes serve several purposes, including: to clarify the purpose of the information; to explain unfamiliar concepts and new information; to identify relationships among the information in the schedules and elsewhere in the financial report; and to explain atypical trends and anomalous data caused by out-of-the-ordinary incidents, changes in assumptions or methods, organizational restructuring, major policy changes, or other events. Figure 38 includes a note explaining the meaning of overlapping debt. Figure 66 provides an explanation for a notable increase in police expenditures.

By the numbers…options for debt ratios

A government has a few options when calculating its outstanding debt ratios. If personal income information is not available for the government's jurisdiction, it may use estimated actual value of property or another economic indicator as the denominator in that ratio of total outstanding debt. If the government's general bonded debt is repaid with revenue from a source other than a property tax, it may calculate a general bonded debt ratio using an indicator of the economic base from which the revenue is drawn. For instance, if debt is repaid with sales taxes, the ratio could be calculated as a percentage of taxable retail sales. If resident population is not relevant to a particular government, it may select a more relevant number to calculate a per capita debt ratio. For instance, the users of a public university's financial report might find it more relevant to see a ratio of debt divided by total student enrollment.

By the numbers…overlapping debt—who's in and who's out?

Not all governments are required to include the direct and overlapping debt schedule in their statistical sections, and not all overlapping governments are included in the schedule when it is presented. State government debt is not included in the schedules prepared by localities and other sub-state-level governments, and states are not required to prepare this schedule. County-level and regional governments are encouraged to present this schedule but are not required to do so.

Keep in mind…debt service coverage requirements

It is common for bond issues to include a required level of debt service coverage. In other words, the agreement to sell the bonds includes a requirement that the government pledge revenues that are substantial enough to meet or exceed a certain coverage ratio and, thus, a specific level of debt service coverage. Generally, the higher the coverage ratio, the more comfortable bond-holders feel that they will be paid by a government.

The coverage ratios in the pledged-revenue coverage schedule are not intended to replicate whatever legal coverage requirements apply to a government. The particulars of coverage agreements vary so much among different bond issues that it might not be possible to show them all. Thus, the schedule is not intended to help you assess whether a government is complying with its legal coverage requirements; rather, it applies a single formula to help make uniform judgments about a government's ability to repay those debts with the resources that have been set aside for that purpose. Furthermore, the schedule reveals the ability of a revenue source to cover the debt service of all of the outstanding debt it is pledged to repay, not just a single issue of debt.

PART SEVEN

GOVERNMENT-WIDE STATEMENT OF ACTIVITIES

The statement of activities tracks a government's yearly revenues and expenses, as well as any other transactions that increase or reduce net position. (See Figures 42, B-2, and C-2.) The statement is unlike the top-to-bottom structure of the other financial statements—it begins in the upper left corner, proceeds left to right across the top, and then down the right side. The design has its purposes, which this section describes.

EXPENSES

The first column in the top half of the statement of activities is a list of expenses. These amounts represent the full costs of providing government services. This is a more comprehensive measure than just the amount of cash that has changed hands—it includes employee benefits that are earned during the period covered by the financial statements but are not required to be paid until a future date, the cost of supplies used up during the year to operate the government, as well as a portion of the original purchase cost of long-lived assets like buildings and equipment. (Recall the discussion of depreciation in Part Four.)

The column begins with the expenses of the governmental activities, sorted by major function. The expenses for BTAs are listed separately below the governmental activities, and a total for the primary government is provided. The expenses for the discretely presented component units complete the column at the bottom.

A "function" is an assemblage of similar activities. Local City, for instance, has a functional category called "culture and recreation," which includes parks, recreation centers, senior centers, libraries, museums, and related services. The statement of activities for the State of Seabury (Figure B-2) includes a functional category called "health and welfare," encompassing public health, healthcare, Medicaid, income support, and a host of social service programs. The Luna Independent School District statement of activities (Figure C-2) contains an "instruction and instruction-related services" function, which includes elementary schools, middle and high schools, special education, and transportation, among other services.

Figure 42. Government-Wide Statement of Activities

Local City
Statement of Activities
for the Year Ending December 31, 2017

Functions/Programs	① Expenses	② Program Revenues: Charges for Services	② Program Revenues: Operating Grants and Contributions	② Program Revenues: Capital Grants and Contributions	Net (Expense) Revenue and Changes in Net Position: Primary Government: Governmental Activities	Primary Government: Business-Type Activities	Primary Government: Total	Component Units
Primary government:								
Governmental activities:								
General government	$ 9,571,410	$ 3,146,915	$ 843,617	$ —	$ (5,580,878)	$ —	$ (5,580,878)	$ —
Public safety	34,844,749	1,198,855	1,307,693	62,300	(32,275,901)	—	(32,275,901)	—
Public works	10,128,538	850,000	—	2,252,615	(7,025,923)	—	(7,025,923)	—
Engineering services	1,299,645	704,793	—	—	(594,852)	—	(594,852)	—
Health and sanitation	6,738,672	5,612,267	575,000	—	(551,405)	—	(551,405)	—
Cemetery	735,866	212,496	—	—	(523,370)	—	(523,370)	—
Culture and recreation	11,532,350	3,995,199	2,450,000	—	(5,087,151)	—	(5,087,151)	—
Community development	2,994,389	—	—	2,580,000	(414,389)	—	(414,389)	—
Education (payment to school district)	21,893,273	—	—	—	(21,893,273)	—	(21,893,273)	—
Interest on long-term debt	6,068,121	—	—	—	(6,068,121)	—	(6,068,121)	—
Total governmental activities	105,807,013	15,720,525	5,176,310	4,894,915	(80,015,263)	—	(80,015,263)	—
Business-type activities:						③		
Water	3,595,733	4,159,350	—	1,159,909	—	1,723,526	1,723,526	—
Sewer	4,912,853	7,170,533	—	486,010	—	2,743,690	2,743,690	—
Parking facilities	2,796,283	1,344,087	—	—	—	(1,452,196)	(1,452,196)	—
Total business-type activities	11,304,869	12,673,970	—	1,645,919	—	3,015,020	3,015,020	—
Total primary government	$ 117,111,882	$ 28,394,495	$ 5,176,310	$ 6,540,834	(80,015,263)	3,015,020	(77,000,243)	—
Component units:								
Landfill	$ 3,382,157	$ 3,857,858	$ —	$ 11,397	—	—	—	487,098
Public school system	31,186,498	705,765	3,937,083	—	—	—	—	(26,543,650)
Total component units	$ 34,568,655	$ 4,563,623	$ 3,937,083	$ 11,397	—	—	—	(26,056,552)
General revenues:								
Taxes:								
Property taxes, levied for general purposes					51,693,573	—	51,693,573	—
Property taxes, levied for debt service					4,726,244	—	4,726,244	—
Franchise taxes					4,055,505	—	4,055,505	—
Public service taxes					8,969,887	—	8,969,887	—
Payment from Local City					—	—	—	21,893,273
Grants and contributions not restricted to specific programs					1,457,820	—	1,457,820	6,461,708
Investment earnings					1,958,144	601,349	2,559,493	881,763
Miscellaneous					884,907	104,925	989,832	22,464
Subtotal, excess (deficiency) of revenues over expenses					(6,269,183)	3,721,294	(2,547,889)	3,202,656
④ Special item—gain on sale of park land					2,653,488	—	2,653,488	—
Transfers ⑤					501,409	(501,409)	—	—
Total general revenues, special item, and transfers					76,900,977	204,865	77,105,842	29,259,208
Change in net position				⑥ ⑦	(3,114,286)	3,219,885	105,599	3,202,656
Net position—beginning					35,840,207	80,879,402	116,719,609	1,461,565
Net position—ending				⑧	$ 32,725,921	$ 84,099,287	$ 116,825,208	$ 4,664,221

Figure 42 Notes

① At a minimum, governments report expenses at the same level of detail as in the governmental funds statements (Figure 54). However, they are encouraged in the accounting standards to provide additional detail—for example, police, fire, and ambulance service instead of the broad public safety function.

② Program revenues are produced by a particular function or provided by external parties (such as higher levels of government) for use in that function and thereby reduce the net expense to the public of the function.

③ A (negative) amount represents a net expense to the government: the portion of expenses not covered by program revenues but, instead, financed with taxes and other general revenues. Governmental activities typically have a net expense. A positive amount is a net revenue: program revenues exceed program expenses, and make a net contribution to general revenues.

④ Because special and extraordinary items and transfers are shown separately, you can determine whether common annual revenues were sufficient to meet common annual expenses, or whether unusual costs or resources affected the bottom line.

⑤ In addition to the items shown here, other changes in net position shown separately from general revenues include contributions to term and permanent endowments and contributions to permanent fund principal.

⑥ When these subtotals and totals are positive, revenues exceeded expenses (a surplus) and net position improved. When expenses exceed revenues (a deficit), the amount is negative and net position declined. Governmental activities net position declined despite the sale of park land and a transfer from the BTAs.

⑦ If only the total column for the primary government and its $105,599 increase in net position had been shown, you would not have known that a $3.1 million decrease in governmental activities net position was offset by an increase in BTA net position.

⑧ These net position amounts appear as the total net position amounts in the statement of net position (Figure 1).

Some governments list expenses at different levels of detail without differentiating them, as does Local City. Its 10 lines beneath governmental activities include:

- Five functions (general government, public safety, public works, health and sanitation, and culture and recreation)
- Three specific individual services (engineering, community development, and education)
- One program (cemetery), and
- Interest on long-term debt (which is a "nature" or "object" category of expenses).

Depreciation expenses are allocated among the categories and included within the direct expense amounts, to the extent the depreciation can be connected with capital assets specifically related to the functions or programs. Any remaining, "unallocated" depreciation expense is shown separately. Interest expenses almost always are shown separately in the statement (as in Figure 42) but can be allocated among the functions and programs.

Figure 42: Expenses of the school district component unit were $31,186,498.

PROGRAM REVENUES

As you move from left to right across the statement, the next set of columns presents **PROGRAM REVENUES**. These revenues are directly connected with the functional (programmatic, service specific) expenses listed to their left. They are of two types—charges for services, and grants and contributions.

CHARGES FOR SERVICES are fees and other charges to the users or recipients of the services a government provides. For instance, the nearly $4 million of charges reported in the "culture and recreation" row in Figure 42 represents admission fees to museums and parks, concession proceeds from food and souvenir stands, permit fees for using softball and soccer fields, and similar revenues. For "public safety," program revenues might include permit fees for parades, and traffic and parking fines. "Transportation" charges in the State of Seabury statement (see Figure B-2) include vehicle registration and driver's license fees. In the Luna Independent School District statement (see Figure C-2), "support services—student-based" includes, among other items, rental fees for school buses and charges to students who participate in certain extracurricular activities; for adult education, program revenues include tuition charges for participants in high school equivalency and continuing education courses.

Program revenues include the grants and contributions a government receives that are restricted for use to a particular purpose. The statement divides these grants into two categories:

- **OPERATING GRANTS AND CONTRIBUTIONS**—to finance the annual operating activities of a government, and
- **CAPITAL GRANTS AND CONTRIBUTIONS**—to fund the acquisition, construction, or rehabilitation of capital assets.

Figure 42: Capital grants and contributions for the water system were $1,159,909.

The vast majority of grants are **INTERGOVERNMENTAL AID**—funds provided by state, local, and federal governments to lower levels of government. In the vocabulary of government finance, these are mostly **CATEGORICAL GRANTS**, aid that comes with strings attached—it must be used for its specified purpose or not at all. In fact, governments often have to spend money *first* on a particular purpose before they receive the grant dollars. Well-known examples of categorical operating grants are income support, healthcare, and public education. Capital grants are quite common as well—for building wastewater treatment plants, highways and bridges, and schools, to name a few purposes. Governments also sometimes receive grants and contributions from nongovernmental foundations and private organizations. For example, the Annenberg Foundation provides financial support for

reform and restructuring initiatives in public elementary and secondary schools. State universities regularly receive grants for research from private, not-for-profit foundations.

NET COST OF SERVICES

An important purpose of the design of this statement is to show the degree to which a government's various activities are financed with revenues (principally taxes) raised generally from taxpayers. The remaining four columns in the top part of the statement display this information—**NET (EXPENSE) REVENUE.** These dollar amounts are derived by subtracting expenses from total program revenues for each expense category.

If the expenses of a government's activities surpass its program revenues, negative numbers result in the statement—these are net expenses, or net costs to the general public. (Parentheses indicate a number is less than zero.) These activities generally are dependent upon tax dollars and accumulated resources to finance that additional amount. It should not come as a surprise that the expenses of the governmental activities almost always surpass their program revenues. After all, services like public safety and education are dependent upon tax dollars and are supplied by governments because the private sector does not provide such services in quantities sufficient to meet public demand.

Figure 42: Community development had a net expense of $414,389 ($2,580,000 – $2,994,389).

When program revenues exceed expenses, the resulting number is positive (greater than zero)—the activity is a net contributor of revenues to the general public and generally does not require tax financing. BTAs often fall into this latter category. These functions sometimes are self-sufficient, and sometimes contribute additional resources a government can use to support its governmental activities. The program revenues of both the water and sewer services of Local City are greater than their expenses; as a result, they show a net revenue, or positive figure. The parking facilities, however, are not self-sustaining; their **USER FEES** and other program revenues fall short of expenses, and they require financial support from taxes and other general revenues. Both of the BTAs in the school district had a net expense. The three BTAs listed individually for the state government each generated net revenue; the aggregation of the other BTAs combined to produce a net expense. (See **Upon further review…mass transit** on page 161.)

Figure 42: The water system had a net revenue of $1,723,526 ([$4,159,350 + $1,159,909] – $3,595,733).

The "positive" and "negative" numbers should not be construed as value judgments of good or bad situations, respectively. They merely are indicative of whether a particular function relies on general revenues or accumulated resources for financing or is a net contributor of resources to the government.

GENERAL REVENUES AND OTHER CHANGES IN NET POSITION

The remainder of the statement of activities proceeds downward from the net (expense) revenue columns. Below these columns, the statement presents the GENERAL REVENUES and other items the government employed to finance the net cost of services not funded by program revenues. Most of the general revenues of state and local governments are taxes, of which property and sales taxes are most common for localities, personal and corporate income and sales taxes for states, and property taxes for school districts. (See **By the numbers…dedicated taxes.**) Unrestricted aid from other governments (grants not devoted to a particular program) appears under general revenues, as well as income earned from most investments. Typically, a significant portion of the general revenues of school districts is some type of state formula aid. This is aid that is distributed to school districts based on a statewide formula that may take into account, among other things, the number of students and local household income.

Figure 42: Franchise taxes totaled $4,055,505.

In the lower half of the statement, a government shows several other transactions and events that increase or decrease net position. TRANSFERS are shifts of resources from one part of a government to another part—such as from governmental activities to BTAs (or vice versa)—*without receiving direct and equal benefit in return*. SPECIAL ITEMS and EXTRAORDINARY ITEMS are nontypical increases and decreases in net position. Other items shown separately include contributions to term and permanent endowments and to permanent fund principal.

Extraordinary and special items are identified by two characteristics:

- Extraordinary items are *both* unusual in nature *and* infrequent in occurrence, whereas special items are one *or* the other.
- Special items are within the control of a government, such as the costs of an early-retirement incentive, in the form of a one-time cash payment, offered by a government to its employees in order to reduce the size of its workforce. In most cases, governments have no control over extraordinary items.

Special and extraordinary items are shown separately from revenues and expenses specifically because they are not part of the usual annual flows in and out of a government. To include them might lead to incorrect conclusions about a government's ability to balance its revenues and expenses. Suppose, for example, a New England town has been ravaged by a tornado. The costs of cleaning up after this natural disaster are not common, recurring annual expenses for this government, because tornadoes rarely occur in New England. Would it be fair to include these costs when trying to determine whether this government raised sufficient resources to cover expenses that year? No, it would distort the picture of its ongoing ability to make ends meet. In a similar vein, one would not want to include any federal disaster aid that the government received to finance its clean-up efforts. The information is

nonetheless important, so governments report it and it is considered part of the overall CHANGE IN NET POSITION for the year. (See **Upon further review…selling land.**)

CHANGE IN NET POSITION

The general revenues and other items are totaled in the statement of activities and added to the net (expense) revenue total. This sum is the aggregate change in net position for the year. It is added to the net position balance for the beginning of the year to produce the net position balance for the end of the year. The end-of-year net position amounts are the same as those in the statement of net position.

Take a look at how our three governments fared:

- Overall, Local City's total revenues exceeded total expenses slightly, producing a surplus (or increase in net position) of $105,599. However, although the BTAs produced an increase in net position of $3.2 million, the governmental activities had a deficit that reduced net position nearly as much.
- Both the governmental and business-type activities of the State of Seabury showed a positive change in net position—$657.5 million and $366.9 million, respectively. (See Figure B-2.) Virtually all of the governmental activities change in net position was the product of a $650.7 million transfer from the BTAs.
- Overall, total revenues and the special items exceeded total expenses substantially for the Luna Independent School District, producing a surplus (or increase in net position) of $20,341,902. (See Figure C-2.) The net position of both the business-type and governmental activities increased during the year—$1,266,712 and $19,075,190, respectively.

WHAT CAN YOU DO WITH STATEMENT OF ACTIVITIES INFORMATION?

As we moved through the structure and contents of the statement of activities, we identified seven issues you can use its information to examine:

- Cost of services
- Net costs of services to taxpayers
- Types of expenses and revenues
- Balance between revenues and expenses
- CHANGE IN FINANCIAL POSITION and its causes
- Unusual transactions
- Financial relationships between BTAs and governmental activities.

What Do Services Cost, and How Much of That Cost Must Taxpayers Finance?

Depending on the level of detail provided by a government, you may find in the expenses column information about *how much it costs to perform various functions* and possibly *how much individual services cost to provide*. This kind of information may help to inform basic questions about whether a government is giving and its citizens are receiving good value in public services in return for tax dollars and user fees. When combined with information obtained from other sources about the performance of government services, you can use cost data to *examine how efficiently a government uses public resources to provide services*. (See the discussion is the last section of Part Fourteen.) What did it cost per ton to collect garbage? What was the cost per student in the school system? How do those amounts compare with prior years and other governments?

Furthermore, the comparison of expenses with program revenues tells you the degree to which each function or service raises or receives sufficient program revenues to cover its costs or, alternatively, the degree to which each function or service requires taxes and general revenues for financing. You can use this information to help guide budgetary decisions: Are taxes sufficient to support the government's net expense? Can program revenues be increased?

Where Does a Government Get Its Money, and How Does the Government Use It?

You can examine the composition of total revenues and total expenses, and how they have changed over time. Alternatively, you might want to look at percentage distributions and percentage changes for governmental and business-type activities individually, or program revenues separately from general revenues. Percentage distribution shows the portion of a financial statement total or subtotal represented by individual elements and is calculated as follows:

(individual element amount ÷ total amount for category) × 100
= percentage distribution for individual element

To employ a simplistic example, a government with $1,000,000 of total revenue has $100,000 of operating grants and contributions. To determine the percentage of total revenues represented by operating grants and contributions:

(operating grants and contributions ÷ total revenue) × 100
= percentage distribution for operating grants and contributions

($100,000 ÷ 1,000,000) × 100 = 10 percent

An important use for percentage distribution is determining a government's level of **REVENUE DISPERSION.** The degree of dispersion or diversity in a government's sources of revenue can tell you something about its *exposure to financial difficulty* if a particular revenue source dries up. Examining the

individual components of total revenues, you might find that a government relies on a broad range of revenues to support its activities and, therefore, is relatively less likely to be dramatically affected if one type of revenue does not meet expectations. Alternatively, you might find that it relies heavily on one or two sources of revenue—reductions in those kinds of revenues could harm the government financially because it is very dependent on those revenues to run its operations.

Revenue dispersion is another type of information that may be useful for making or assessing budget decisions. An important part of budgeting is identifying sufficient revenues to cover a government's costs during the coming year. That determination requires a decision about the certainty of receiving the projected revenues and providing some assurance that balance still can be achieved if one or more revenue sources do not live up to projections.

Is a Government Better or Worse Off Financially, and Why?

A basic function of the statement of activities is to let you know whether a government raised sufficient revenues to cover the expenses incurred by its activities. *Did the government live within its means?* The statement helps to answer this question because it shows other types of changes in net position separately from revenues and expenses. Because transfers and out-of-the-ordinary inflows and outflows are kept apart, you can determine whether a government's basic, ongoing revenues matched its recurring annual expenses.

This information is particularly useful for judging *whether a government is financing each year's services and activities with revenues from that year,* as opposed to using resources accumulated from previous years or passing the costs of today's services onto future taxpayers. That is the concept introduced in Part Four as interperiod equity. You can use statement of activities information to help answer this question, but you will need information from other sources (particularly about the circumstances of any shifting of resources from one year to the next) to produce a satisfactorily complete answer. (See the discussion of surpluses and deficits in Part Nine.)

Changes in a government's financial position also may be considered part of the evidence of a government's financial acumen. *The ability of government officials to manage finances* may be a factor in voting decisions. For example, you might look at a government's financial statements for the period a mayor has been in office. What happened to financial position during the mayor's tenure? Did it improve, decline, or remain stable? How or why did it improve, decline, or remain stable? In light of a particular government's circumstances, this could be a factor that contributes to your decision.

What Unusual Transactions Occurred During the Year? Was There Financial Activity between the Governmental and Business-Type Activities?

The fact that a government shows unusual transactions apart from other changes in net position provides important information about *why net position changed* during the year. It identifies not only atypical resources like the proceeds from selling capital assets or a windfall judgment from a lawsuit, but also uncommon costs. The transfers line on the statement begins to give the reader a sense of *how the BTAs and governmental activities relate* to one another financially.

Will a Government Be Able to Finance Services in the Future?

Some of the information necessary to assess a government's ability to finance long-term debt can be found in the statement of activities. The remaining information comes from the fund statements, so this issue is discussed in later sections as well.

You can compare revenue and expense information to economic and demographic data to produce measures of future financing capability. For instance, any expense category could be divided by population to produce a *cost per person* (see Part Fourteen):

- Local City's expenses for health and sanitation amounted to $75 per person.
- Dividing the payment to the school district by the number of students produces a financial support per pupil figure of $1,609.
- Total taxes divided by population were $772 per person. You also could divide an *individual* tax by its relevant tax base—for example, property tax revenue was $1.44 per $100 of property value.

Information like this can help you ascertain a government's potential need for resources. The economy's ability to bear additional financial burdens may be important for deciding how to vote on a public referendum or ballot question related to a proposed tax increase (or tax cut). This information and the results of examining the statement of net position also could help you decide how to vote on a referendum calling for new long-term debt to finance a particular kind of capital investment (such as water pollution control projects). What are current debt levels? What financial burden does the public bear to repay debt each year?

All of the analyses discussed in this section can be used together to inform investment decisions about buying municipal bonds from a government. In particular, you may find very useful information about the likelihood that a government will be able to repay the interest and principal on its bonds. That information would be equally valuable for deciding whether to hold or sell bonds already owned.

PROGRAM REVENUES are produced by an activity's fees and charges or received as operating or capital grants specifically for that activity

NET EXPENSE is the portion of service costs not covered by related program revenues and which, therefore, requires financing from general revenues

NET REVENUE is the portion of program revenues in excess of related service costs

GENERAL REVENUES are those that do not qualify as program revenues; they typically are taxes and unrestricted aid

a SPECIAL ITEM is a revenue or expense that is within the control of a government and is either unusual in nature or infrequent in occurrence

an EXTRAORDINARY ITEM is a revenue or expense that is both unusual in nature and infrequent in occurrence

Upon further review…mass transit

Mass transit activities, such as bus and subway service, do not fit the theory that governmental activities place a burden on taxpayers while BTAs are net contributors to general revenue. Mass transit typically is operated and accounted for as a BTA—passengers are charged a fare. However, that fare rarely comes close to covering the cost of ridership. Rather, mass transit tends to be subsidized by tax revenues and grants. If mass transit appeared in Figure 42, it would show a sizable net expense, like Local City's parking facilities.

By the numbers…dedicated taxes

Accounting standards require that *all* taxes be reported as general revenues. What about DEDICATED TAXES, though, which by law can be used only for a specific purpose? A common example is a motor fuel tax that is used to fund road repairs. But those fuel taxes are generated by a driver's purchase of gas, not a government's provision of road services.

Consequently, dedicated taxes do not meet the definition of program revenues: They are not program-specific grants and contributions; nor are they charges for services generated by a program. Therefore, they are considered part of the general revenues governments use to finance the portion of program costs not covered by program revenues.

Upon further review…selling land

Consider the scenario presented in the illustrative financial statements. Local City sold several parcels of park land during 2017. The gain on the sale of that land (the sales price less what the land originally cost the City) increased its net position. However, Local City cannot sell park land every year to balance its budget; eventually, it will run out. That transaction, which some might call a "one-shot," should not be taken into account when trying to assess a government's recurring capacity to live within its means.

By the numbers…categorizing revenues

Government programs generally are financed from four sources:

a. The purchasers, users, or direct beneficiaries of the program
b. Those outside the government's citizenry, such as other governments and nongovernmental entities
c. The taxpayers
d. The government itself (for example, via investing).

The accounting standards lay out criteria for determining where these financing sources belong in the statement of activities:

- Type **a** always is program revenue.
- Type **b** is program revenue if restricted to specific programs; otherwise it is general revenue.
- Type **c** always is general revenue (see **By the numbers…dedicated taxes** on page 162).
- Type **d** usually is general revenue; an exception is earnings on endowments or permanent fund investments that are specifically restricted to a program or programs in the endowment or fund's agreement or contract.

PART EIGHT

NOTES AND SUPPORTING INFORMATION RELATED TO THE STATEMENT OF ACTIVITIES

Revenue and expense items are touched upon in many of the note disclosures already discussed in this guide. For instance, the annual cost (expense) of pension and OPEB benefits is disclosed in the notes on retirement benefits. Items in the statement of activities specifically are addressed in a less voluminous set of note disclosures and supporting information than those addressing items in the statement of net position. Specific notes and supporting information covered in this section include depreciation, future debt service and lease payments, landfill costs, trends in revenues and expenses, special and extraordinary items, tax abatements, and revenue capacity schedules.

NOTES TO FINANCIAL STATEMENTS

Depreciation Expenses

The note disclosure that details how capital assets changed during the year is discussed in Part Five. (Refer to Figure 12.) That disclosure contains useful details regarding depreciation expense.

Because depreciation expense is a direct cost that is included with other direct costs such as salaries in each function or program reported in the statement of activities, you cannot tell how much depreciation was for the year. The additions column in the changes in capital assets note disclosure includes the depreciation expense *for each kind of capital asset* and a total. The bottom part of the note then shows how depreciation expense is allocated *among the functional expense categories* in the statement of activities.

WHAT'S AHEAD?

- WHAT DOES IT COST TO REPAY LONG-TERM DEBTS?
- WHAT RESOURCES WILL BE NEEDED IN THE FUTURE TO REPAY DEBT AND PAY FOR LEASES?
- WHAT WILL IT COST TO CLOSE AND CARE FOR LANDFILLS?

Debt Service

Debt service is the repayment of the principal of outstanding debt, plus interest. A government presents a note to the financial statements that lays out the future debt service payments for its existing long-term debts until they have been completely repaid. (See Figure 43.) The principal and interest amounts are shown separately for each of the first five years and then in five-year increments thereafter. If a government has variable-rate debt, it also discloses the terms under which interest rates change for that debt.

Figure 43. Debt Service Requirements Note Disclosure

Debt service requirements at August 31, 2017, were as follows (amounts in thousands):

①

Year Ended August 31	Governmental Activities		Business-Type Activities			
	General Obligation		Revenue Bonds			
			Water and Sewer		Parking	
	Principal	Interest	Principal	Interest	Principal	Interest
2018	$ 3,769	$ 4,042	$ 3,944	$ 3,034	$ 360	$ 995
2019	4,135	3,854	3,410	2,837	415	977
2020	5,640	3,647	5,193	2,666	485	957
2021	6,135	3,365	5,744	2,407	535	932
2022	5,962	3,058	5,508	2,139	545	914
2023–2027	26,625	10,472	22,406	9,030	3,845	4,300
2028–2032	15,645	5,188	8,330	2,779	4,445	2,634
2033–2037	6,175	2,460	3,210	1,147	4,755	1,673
2038–2042	4,850	1,082	2,934	438	2,870	674
2043–2045	1,904	238	—	—	1,649	180
Total	$ 80,840	$ 37,406	$ 60,679	$ 26,477	$ 19,904	$ 14,236

Interest on the variable-rate parking facility revenue bonds is paid at Securities Industry and Financial Markets Association™ Municipal Swap Index rate and is reset semiannually. ②

Figure 43 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② Outstanding fixed-rate debt has a known future debt service schedule because the interest rate does not change. For variable-rate debt, the debt service requirements are based on the interest rate as of the date of the financial statements.

What can you do with debt service information?

Knowing the demands that repaying long-term debts will present in the future can help you assess whether a government will have sufficient resources to make these payments. The note disclosure also can help you determine whether there are any unusually large annual payments looming. Although debt service schedules often are smooth over time, requiring generally similar payments each year, it

is not unusual for there to be a "balloon" payment in a given year that is significantly larger than the typical annual payment. For example, ZERO-COUPON BONDS do not pay off until the end of the maturity of the bonds; consequently, a single, large payment is made rather than smaller payments each year the bonds are outstanding. If such a large payment exists, you can inquire as to whether resources are being set aside to make that payment when it comes due.

When examining this information about debt service requirements, one should be mindful that they relate only to debt that already has been issued. The amounts include no provision for the repayment of debt that will be issued in the future.

Lease Payments

Governments prepare a note disclosure for future payments on capital leases and noncancelable operating leases, like the debt service requirements note just described. A government discloses the minimum payment required for each of the next five fiscal years and in five-year increments thereafter until the end of the lease. (See Figure 44.) This information can be useful for assessing the affordability of the long-term commitments the government has made under its leases, as well as for identifying unusually large annual payments that are looming down the road. The information about the lease payments also should help you determine the potential that the required payments could change significantly in the future. (Refer to **Upon further review…major changes in lease accounting** on page 98.)

Figure 44. Future Minimum Lease Payments Note Disclosure

Obligations of governmental activities under capital leases at June 30, 2017, were as follows (amounts in thousands): ①

Year Ending June 30	Total
2018	$ 496
2019	366
2020	319
2021	278
2022	218
2023–2027	894
2028–2031	71
Total minimum lease payments	2,642
Less: Amount representing interest costs	(1,093)
Present value of minimum lease payments	$ 1,549

Figure 44 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

What can you do with information about leases?

Because leases essentially are a form of borrowing, it is equally important to be aware of the demands that paying for leases will present in the future. This can help you assess whether a government will have sufficient resources to make the payments. Leases generally will not have the kinds of balloon payments you might find in the debt service schedule of outstanding bonds, but they may contain provisions for periodic increases in payments. This disclosure of future lease payments can alert you to increasing cash demands.

Landfill Closure and Postclosure Care Costs

As previously mentioned in Part Five, a government is required to report a long-term liability if it is legally required to perform certain actions to close a municipal solid waste landfill and to care for it after it is closed and no longer receives solid waste. The amount of the liability is based on the estimated total current cost—an estimate of what it would cost today to perform those actions. A portion of that cost is reported as expense in the financial statements every year until the landfill ceases to accept waste (similar to the way depreciation allocates the cost of capital assets over the years they are in use).

Governments with solid waste landfills provide a note disclosure (Figure 45) with the following information:

- A description of the laws and regulations governing closure of the landfill and care after it is closed
- A statement that the liability for landfill closure and postclosure care is determined based on the amount of landfill capacity already used

1. The amount of the liability (if it is not apparent from the financial statements) and the portion of estimated total current cost that has not yet been reported
2. The percentage of landfill capacity that has been used and an estimate of the number of years of useful life remaining for the landfill
3. An explanation of how the estimates were made and the possibility that inflation, technology, existing laws and regulations, or other factors might lead to changes in the estimates, and
4. If the government is required to provide financial assurances that landfill costs will be met by placing assets in a trust or with an external party, it describes how those requirements are being

addressed; it also discloses any assets it has that are restricted to paying for landfill closure and postclosure costs, if they cannot be identified in the financial statements.

Figure 45. Landfill Closure and Postclosure Care Cost Note Disclosure

① State and federal laws and regulations require the Swarthy Waste Disposal Authority to place a final cover on its Swill Street landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although closure and postclosure care costs will be paid only near or after the date that the landfill stops accepting waste, the Authority reports a portion of these closure and postclosure care costs as an operating expense in each period based on landfill capacity used as of each statement of net position date. The $10.4 million reported as landfill closure and postclosure care liability at April 30, 2017, represents the cumulative amount reported to date based on the use of 80 percent of the estimated capacity of the landfill. The Authority will recognize the remaining estimated cost of closure and postclosure care of $3.1 million as the remaining estimated capacity is filled. Those amounts are based on what it would have cost to perform all closure and postclosure care in 2017. The Authority expects to close the landfill in the year 2021. Actual cost may be higher or lower due to inflation, changes in technology, or changes in regulations.

The Authority is required by state and federal laws and regulations to make annual contributions to a trust to finance closure and postclosure care. The Authority is in compliance with those requirements and, at April 30, 2017, investments with a fair value of $7,900,115 were held for those purposes. Those are reported as restricted assets on the statement of net position. The Authority expects that future inflation costs will be paid from interest earnings on those annual contributions. However, if interest earnings are inadequate or additional postclosure care requirements are determined (due to changes in technology or applicable laws or regulations, for example), those costs may need to be covered by charges to future landfill users or from future tax reveue.

Figure 45 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

What can you do with information about landfill costs?

One can imagine that, for any capital asset that has reached the end of its useful life, there might be costs involved in disposing of the asset or ensuring that it is not a danger to anyone. Typically, such costs are speculative—we do not know how much they will be, nor whether any actions will need to be taken at all. However, the establishment of federal regulations specifying how landfills should be closed and cared for made clear that governments with municipal landfills eventually would have to take certain actions. This degree of certainty that costs will be incurred suggests that the users of

financial statements would want to know about them. Even if the required actions will not take place for several years, the reporting of the cost makes clear that a long-term obligation exists.

On-Behalf Payments

A government may make payments for fringe benefits and salaries *on behalf* of another government or a nongovernmental organization. For instance, a state government might make **ON-BEHALF PAYMENTS** in the form of pension contributions for teachers in local school districts, or perhaps salary enhancements directly paid to the teachers. Each of these payments is made *on behalf* of the separate school districts. Another example might be health insurance premium payments made by a city government on behalf of the employees of a separate library system. On-behalf payments are distinguishable from more common transactions in which a government incurs costs that are paid for by other governments or organizations. More commonly, a government would incur expenditures and then seek reimbursement from another governmental entity. With on-behalf payments, however, the other governmental entity makes payment directly to the insurance company or pension plan, bypassing the government that is the beneficiary of the on-behalf payments.

Regardless of how the resources flow, the substance of the transaction is the same. In other words, even though on-behalf payments bypass the government that employs the workers benefiting from the payments, that employer government nevertheless reports revenues, expenses, and expenditures (the latter in the government funds) related to those on-behalf payments in the financial statements. If it did not do so, the cost of employing those workers to operate the government and provide its services would be understated.

In order to clearly identify on-behalf payments, the employer government presents a note disclosure with the amounts of on-behalf payments made by another government for salaries and fringe benefits. If any of the on-behalf payments were contributions to a pension plan for which the employer government is not legally responsible, it discloses the name of the plan and the name of the entity that made the payments. **Upon further review…special funding situations** on page 100 further explains how on-behalf payments related to pensions and OPEB are reported and disclosed.

Special and Extraordinary Items

As explained in Part Seven, extraordinary items are revenues, expenses, and other changes in net position that are beyond a government's control and are both unusual in nature and infrequent in occurrence. Special items are one or the other, and are within the control of government.

Any significant transaction or event that is *either* unusual *or* infrequent (like special items) *but* also is outside the control of a government (unlike special items) is disclosed in the notes to financial statements.

WHAT'S AHEAD?

- FIND OUT WHY A GOVERNMENT IS PROVIDING CERTAIN TAX BREAKS TO INDIVIDUALS AND BUSINESSES.
- LEARN HOW MUCH A GOVERNMENT'S TAXES ARE REDUCED AS A RESULT.

Tax Abatements

Governments use a variety of tools to encourage individuals and businesses to do things that are beneficial to the public (or to *not* do things that are detrimental). For example:

- Income tax deductions are provided for charitable donations.
- Senior citizens may be exempt from some or all property taxes.
- Sales taxes on certain purchases may be fully or partially refunded to businesses.
- Businesses that employ local residents may receive credits that reduce their corporation taxes.

Such reductions of taxes are referred to in the aggregate as "tax expenditures." One of the most common forms of tax expenditure is called a **TAX ABATEMENT**. (See **Keep in mind...an abatement by any other name.**) Tax abatements are agreements between one or more governments and an individual or business in which (1) the governments forgo taxes to which they otherwise would have been entitled and (2) the individual or business promises to subsequently do something that will benefit the public. Most often, those beneficial actions take the form of economic development. For example, a business agrees to relocate to the city providing the tax abatement, or to remain in the city, or to expand within the city.

If a government enters into a tax abatement agreement—or if its taxes are reduced by a tax abatement agreement entered into by another government—it discloses information about the abatement and its financial impact. (See Figure 46.) The note begins with descriptive information about the government's own tax abatement agreements, including (1) the name and purpose of the program or programs under which tax abatements are provided, (2) the tax or taxes that are being abated, (3) the law that authorizes the government to abate taxes, (4) the types of actions the recipients promise to take, (5) eligibility requirements for receiving an abatement, and (6) provisions for getting abated taxes back if the recipient does not perform the promised action. For other governments' tax abatements that affect the reporting government's taxes, the reporting government discloses the names of those governments and the tax or taxes being abated.

This disclosure helps you to understand the financial impact of all tax abatements that reduce a government's taxes by disclosing the dollar amount of taxes forgone during the fiscal year. It also includes any other commitments the government has made as part of its own tax abatement agreements. For instance, a government may agree to improve surrounding highways as part of a tax abatement agreement to entice a company to build a new headquarters.

What can you do with tax abatement information?

Tax abatement agreements are significant transactions both in terms of the tax dollars forgone and the number of governments that are affected by them. In most cases, the taxes that are abated are never billed to the individual or business. That means the transactions are not recorded in a government's accounting system and, therefore, are not reflected in its financial statements. Without this note disclosure, you might not know anything about these agreements that lower the amount of resources available to governments.

Figure 46. Tax Abatement Note Disclosure

As of December 31, 2017, the County provides tax abatements through six programs—the Residential Improvement Program, Film and Television Production Incentives, the Economic Assistance Initiative, the High-Tech Investment Program, the Competitive County Credit, and the Renewable Energy Incentive: (1)

- The Residential Improvement Program provides property tax abatements to encourage improvements to single-family and multiple-unit dwellings, under State Law, Code 14, Section 201.1. Abatements are obtained through application by the property owner, including proof that the improvements have been made, and equal 100 percent of the additional property tax resulting from the increase in assessed value as a result of the improvements. The amount of the abatement is deducted from the recipient's tax bill.
- Under the County Economic Development Act of 2003, two divisions of the County government administer tax abatements:
  - The Office of Film and Television Production Incentives provide abatements of the County's sales and corporate income tax to attract television, movie, and commercial productions. Production companies apply to the Office for admittance into the program in advance of commencing production. Production companies can apply for a refund of sales taxes on qualifying spending in the County within three years of the date of admittance. Production companies' County corporate income tax liabilities also are reduced by the amount of qualifying spending, up to 100 percent of the taxes owed.
  - The Department of Economic Assistance administers three tax abatement programs: the Economic Assistance Initiative (EAI), the High-Tech Investment Program (HTIP), and the Competitive County Credit (3C). The agreements entered into by the Department include clawback provisions should the recipient of the tax abatement fail to fully meet its commitments, such as employment levels and timelines for relocation.
    - EAI offers individual incentive packages to attract new business to the County. Abatements may be granted to any company agreeing to relocate to the County or to establish a new business in the County. The Department abates up to 75 percent of the property tax bills through a reduction in the assessed value of the facilities that the new or relocating businesses construct or purchase. The Department also arranges for the County to construct certain infrastructure features that are ancillary to newly constructed facilities. One agreement involving the construction of a new office building for the central headquarters of a major corporation included a substantial commitment from the County to construct a new exit on County Highway 84 and connecting roadways and ancillary features between the highway and the building.
    - HTIP offers reductions in business income taxes to attract businesses in technology industries to move to the County High-Tech Industry Park (CHIP). Abatements may be granted to any technology company agreeing to move into CHIP. The abatement is administered as a credit on a company's

County income tax return and equals 25 percent of the company's corporate income tax liability. The abatement begins in the year when the company begins its relocation to CHIP.

  - 3C offers reductions in business income taxes to attract and retain jobs. Abatements may be granted to any business agreeing to remain in the County or to relocate to the County. The abatement is a credit on a company's County income tax return and is effective beginning in the year of the agreement (for job retention) or the year when the business begins its relocation to the County (for job attraction). The amount of the abatement is based on the number of jobs retained or attracted.

- The Environmental Conservation Department administers the Renewable Energy Incentive to encourage businesses to invest in solar, wind, and other sources of clean, efficient energy. The program also covers investments in energy-efficient vehicles such as hybrid, electric, and alternative-fuel cars and ancillary facilities, such as charging stations. These abatements are provided under the authority of the State of Example's Environmental Protection Division. After their application and acceptance into the program, companies can file for two types of tax abatements: a refund of sales taxes on spending related to renewable energy and a credit against their County corporate income tax liability for eligible spending, up to a maximum of $100,000.

Tax Abatement Program	Amount of Taxes Abated (in thousands)
Residential Improvement Program	$ 32,912
Film and Television Production Incentives	
Sales tax	13,435
Corporate income tax	12,479
Economic Assistance Initiative	18,566
High-Tech Investment Program	9,578
Competitive County Credit	11,159
Renewable Energy Incentive	
Sales tax	8,157
Corporate income tax	4,619

State of Sample Tax Abatements

County property tax revenues were reduced by $28,346,000 under agreements entered into by the State of Sample. Under the State's biennial budget for fiscal years 2016–2017, the State reimburses the County for one-third of the reduction in tax revenues. The County received $9,449,000 in County fiscal year 2017.

Figure 46 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

First and foremost, the disclosures can help you to *understand the amount of taxes that were abated during the year*. This note disclosure also tells you why a government is abating taxes and what it expects to accomplish by doing so. Because a government reports both its own tax abatements and those of

other governments that reduce its taxes, you can distinguish between the impacts of the government's policy choices and those that are imposed upon it.

The information in the note will not answer the questions, "Are the government's tax abatements a good deal? How is the government benefiting from these agreements?" It will, however, give you a jumping off point to seek more information from the government to explore those issues further.

SUPPORTING INFORMATION

WHAT'S AHEAD?

- WHAT DOES IT COST TO PROVIDE SERVICES AND OPERATE A GOVERNMENT?
- WHERE DOES THE REVENUE COME FROM TO FINANCE THOSE COSTS?
- ARE SUFFICIENT REVENUES BEING RAISED TO COVER COSTS, OR IS A GOVERNMENT RUNNING DEFICITS?

Trends in Revenues and Expenses

A government's statistical section includes an SI schedule that shows information about the government's revenues, expenses, and other factors that changed net position over the past 10 fiscal years. This information comes from the government-wide statement of activities and carries forward the separation of information for governmental activities and BTAs. A government has some leeway in deciding how to format this schedule—for instance, it might choose to show revenues and expenses in the same schedule (as in Figure 47) or in separate schedules. No matter how it is arranged, the schedule includes the following information:

- Expenses by function, program, or identifiable activity
- Program revenues by category—charges for services, operating grants and contributions, and capital grants and contributions
- Total net (expense) revenue
- General revenues and other changes in net position, and
- Total change in net position.

Although the grants and contributions amounts are shown in the aggregate, the schedule presents a government's largest charges for services individually and identified by function, program, or identifiable activity.

What can you do with trends in revenues and expenses?

This information tells you, in broad strokes, where a government gets its resources from and what it uses those resources for. You can track the various revenue sources and expenses over time using percentage change ratios. Have certain revenues grown faster than others, or even shrunk? Are the

costs of particular functions or programs rising more rapidly than others, or even falling? How has the mix of revenues and expenses changed? These questions can be assessed by calculating percentage distribution ratios over time or percentage change ratios for the period as a whole.

The net (expense) revenue information for the BTAs can be examined over time to determine whether they raise sufficient resources to cover their own costs, or whether taxes are needed to support them. The net expense amount for governmental activities can be monitored to determine whether these functions are more or less reliant on general revenue financing. For each year, you can divide the net expense amount by total expenses; for example, using culture and recreation in Figure 42:

$$(\text{net expense} \div \text{expenses}) \times 100 =$$

$$(\$5{,}087{,}151 \div 11{,}532{,}350) \times 100 = 44.11 \text{ percent}$$

In other words, 44 percent of the cost of culture and recreation services is financed with taxes and other general revenues. The larger this ratio, the more dependent governmental activities are on general revenues (and, therefore, the less self-reliant they are). Conversely, 56 percent of the cost of culture and recreation services is financed using those activities' own revenues from charges and grants. Dividing a *net revenue* by total expenses shows the degree to which a function produces surplus resources that can *supplement* general revenues.

In general, comparing revenues and expenses over time tells you whether the government has raised sufficient resources each year to cover its costs. Has the government needed during the past 10 years to rely on unusual methods to achieve balance?

WHAT'S AHEAD?

- HOW VIABLE IS A GOVERNMENT'S BIGGEST OWN-SOURCE REVENUE OVER TIME?
- HOW HAVE TAX RATES CHANGED OVER TIME?
- WHAT OTHER JURISDICTIONS ARE TAXING THE SAME REVENUE BASE AS A GOVERNMENT?
- HOW GOOD A JOB IS A GOVERNMENT DOING COLLECTING ITS PROPERTY TAXES?

Revenue Capacity

A government's statistical section includes either three or four SI schedules about its most significant OWN-SOURCE REVENUES—revenues that the government generates itself through tax levies or charges for services, as opposed to monies it receives from other governments. For many governments, especially school districts and local governments such as cities and towns, the property tax is the most significant own-source revenue. Together, these schedules help you to understand and assess the government's capacity to raise additional revenue from this source if the need arises.

Revenue base

The first SI schedule presents information about the economic base or activity that is taxed or charged to produce the revenue for the last 10 years. (See Figure 48.) For an income tax, the revenue base might be personal income; for a sales tax, taxable retail sales; for water charges, total water consumption. The revenue base is presented by major component, if applicable, such as types of property, classes of rate payers, or kinds of retail sales transactions. The schedule also includes the TOTAL DIRECT RATE that is applied by the government to the revenue base.

If a government reports a property tax as its most significant own-source revenue, its schedule contains the ASSESSED VALUE of taxable property, organized by type of property—for example, residential, commercial, utility, and so on. Assessed value usually is not equal to the actual market value of property if it were sold. Sometimes this happens because property values are not assessed every year and, therefore, the value assigned to a property does not change as market values change. Sometimes it is a result of the methodology a government employs to value property—it may assign particular values to certain features of property but not take into account the sales value of the property as a whole. Sometimes governments assign an assessed value that is a percentage of market value. For those reasons, the schedule also includes the estimated actual value of property.

Figure 47. Statistical Section Schedule of Changes in Net Assets/Position

City of Chronological
① Changes in Net Assets/Position, Last 10 Fiscal Years
(accrual basis of accounting)

	Fiscal Year									
	20X0	20X1	20X2	20X3	20X4	20X5 [a]	20X6	20X7	20X8	20X9
Expenses										
Governmental activities:										
General government	$ 7,861,321	$ 8,021,756	$ 8,182,192	$ 8,345,835	$ 8,512,752	$ 8,683,007	$ 8,856,667	$ 9,033,801	$ 9,214,477	$ 9,398,766
Police	19,010,700	18,398,684	18,766,658	19,141,991	19,524,831	19,915,327	20,313,634	20,719,906	21,134,305	21,556,991
Fire	11,607,694	11,344,586	11,571,478	11,802,907	12,038,965	12,279,745	12,525,340	12,775,846	13,031,363	13,291,991
Refuse collection	5,089,538	5,193,406	5,297,274	5,403,220	5,511,284	5,621,510	5,733,940	5,848,619	5,965,591	6,084,903
Other public works	13,139,232	13,007,037	13,267,178	13,532,521	13,803,172	14,079,235	14,360,820	14,648,036	14,940,997	15,239,817
Redevelopment	9,783,295	9,682,265	9,875,910	10,073,429	10,274,897	10,480,395	10,690,003	10,903,803	11,121,879	11,344,317
Parks and recreation	8,747,423	8,925,942	9,104,461	9,286,550	9,472,281	9,661,727	9,854,961	10,052,061	10,253,102	10,458,164
Library	2,034,699	2,076,224	2,117,748	2,160,103	2,203,305	2,247,371	2,292,319	2,338,165	2,384,928	2,432,627
Interest on long-term debt	12,760,549	13,020,968	13,281,388	13,547,015	13,817,956	14,094,315	14,376,201	14,663,725	14,957,000	15,256,140
Total governmental activities expenses	90,034,451	89,670,868	91,464,287	93,293,571	95,159,443	97,062,632	99,003,885	100,983,962	103,003,642	105,063,716
Business-type activities:										
Water	21,108,839	20,539,651	20,950,444	21,369,453	21,796,842	22,232,779	22,677,434	23,130,983	23,593,603	24,065,475
Wastewater	10,958,734	10,982,382	11,202,030	11,426,070	11,654,592	11,887,683	12,125,437	12,367,946	12,615,305	12,867,611
Transit	783,168	799,151	815,135	831,437	848,066	865,027	882,328	899,974	917,974	936,333
Total business-type activities expenses	32,850,741	32,321,184	32,967,609	33,626,960	34,299,500	34,985,489	35,685,199	36,398,903	37,126,882	37,869,419
Total primary government expenses	$ 122,885,192	$ 121,992,052	$ 124,431,896	$ 126,920,531	$ 129,458,943	$ 132,048,121	$ 134,689,084	$ 137,382,865	$ 140,130,524	$ 142,933,135
Program Revenues										
Governmental activities:										
Charges for services:										
Refuse collection	$ 4,478,165	$ 4,865,556	$ 4,962,867	$ 5,062,124	$ 5,163,367	$ 5,266,634	$ 5,371,967	$ 5,479,406	$ 5,588,994	$ 5,700,774
Other public works	8,143,696	8,706,894	8,881,032	9,058,653	9,239,826	9,424,622	9,613,115	9,805,377	10,001,484	10,201,514
Parks and recreation	1,561,549	1,993,417	2,033,285	2,073,951	2,115,430	2,157,739	2,200,893	2,244,911	2,289,810	2,335,606
Other activities	1,735,735	1,771,158	1,806,581	1,842,712	1,879,567	1,917,158	1,955,501	1,994,611	2,034,503	2,075,193
Operating grants and contributions	6,041,058	6,497,667	6,627,620	6,760,173	6,895,376	7,033,284	7,173,949	7,317,428	7,463,777	7,613,052
Capital grants and contributions	3,140,265	3,704,352	3,778,439	3,854,008	3,931,088	4,009,710	4,089,904	4,171,702	4,255,136	4,340,239
Total governmental activities program revenues	25,100,468	27,539,044	28,089,824	28,651,621	29,224,654	29,809,147	30,405,329	31,013,436	31,633,705	32,266,379
Business-type activities:										
Charges for services:										
Water	18,261,330	19,634,010	20,026,690	20,427,224	20,835,768	21,252,484	21,677,534	22,111,084	22,553,306	23,004,372
Wastewater	3,967,097	4,448,059	4,537,020	4,627,761	4,720,316	4,814,722	4,911,017	5,009,237	5,109,422	5,211,610
Transit	156,634	159,704	162,898	166,156	169,479	172,869	176,326	179,853	183,450	187,119
Operating grants and contributions	10,389,269	10,901,295	11,119,321	11,341,707	11,568,541	11,799,912	12,035,911	12,276,629	12,522,161	12,772,605
Capital grants and contributions	560,668	804,110	820,192	836,596	853,328	870,395	887,802	905,558	923,670	942,143
Total business-type activities program revenues	33,334,998	35,947,178	36,666,121	37,399,444	38,147,432	38,910,382	39,688,590	40,482,361	41,292,009	42,117,849
Total primary government program revenues	$ 58,435,466	$ 63,486,222	$ 64,755,945	$ 66,051,065	$ 67,372,086	$ 68,719,529	$ 70,093,919	$ 71,495,796	$ 72,925,713	$ 74,384,227

Figure 47 (continued)

Net (Expense)/Revenue										
Governmental activities	$(64,933,983)	$ (62,131,825)	$ (63,374,461)	$ (64,641,951)	$ (65,934,790)	$ (67,253,485)	$ (68,598,555)	$(69,970,526)	$ (71,369,937)	$ (72,797,336)
Business-type activities	484,257	3,625,994	3,698,513	3,772,484	3,847,933	3,924,892	4,003,390	4,083,458	4,165,127	4,248,429
Total primary government net expense	$(64,449,729)	$ (58,505,831)	$ (59,675,948)	$ (60,869,467)	$ (62,086,857)	$ (63,328,594)	$ (64,595,165)	$(65,887,068)	$ (67,204,810)	$ (68,548,907)
General Revenues and Other Changes in Net Assets/Positio										
Governmental activities:										
Taxes										
Property taxes	$ 18,993,540	$ 19,381,163	$ 19,768,786	$ 20,164,162	$ 20,567,445	$ 20,978,794	$ 21,398,370	$ 21,826,338	$ 22,262,864	$ 22,708,122
Franchise taxes	8,164,634	8,331,259	8,897,884	9,175,842	9,459,359	9,848,546	10,245,517	10,650,427	11,063,436	11,584,705
Sales taxes	17,148,354	17,498,320	17,928,927	18,287,506	18,653,256	19,026,321	19,406,847	19,794,984	20,190,884	20,594,701
Other taxes	2,781,964	2,838,739	2,902,513	3,060,563	3,221,774	3,486,209	3,755,933	4,031,052	4,311,673	4,597,906
Unrestricted grants and contributions	5,413,160	5,923,632	6,042,978	6,263,838	6,489,115	6,718,897	7,053,275	7,394,341	7,742,228	7,997,703
Payments in lieu of taxes	9,058,559	9,643,428	9,836,297	10,133,022	10,435,682	10,644,396	10,857,050	11,074,191	11,295,675	11,618,618
Investment earnings	6,517,801	6,950,817	7,089,833	7,331,630	7,578,322	7,829,888	7,986,486	8,177,547	8,406,898	8,576,913
Miscellaneous	4,905,579	5,505,693	5,615,807	5,742,123	5,897,965	5,985,294	6,105,000	6,227,100	6,350,401	6,477,409
Transfers	1,008,741	1,029,327	1,049,914	1,071,136	1,092,789	1,115,053	1,137,354	1,160,101	1,183,303	1,206,969
Total governmental activities	73,992,332	77,102,378	79,132,939	81,229,822	83,395,707	85,633,398	87,945,832	90,336,081	92,807,362	95,363,046
Business-type activities:										
Investment earnings	2,584,242	3,236,982	3,492,083	3,762,305	4,048,477	4,351,475	4,672,218	4,965,662	5,314,978	5,651,278
Transfers	(1,008,741)	(1,029,327)	(1,049,914)	(1,070,912)	(1,092,331)	(1,114,177)	(1,136,461)	(1,113,175)	(1,126,479)	(1,106,417)
Total business-type activities	1,575,501	2,207,655	2,442,169	2,691,393	2,956,146	3,237,298	3,535,757	3,852,487	4,188,499	4,544,861
Total primary government	$ 75,567,833	$ 79,310,033	$ 81,575,108	$ 83,921,215	$ 86,351,853	$ 88,870,696	$ 91,481,589	$ 94,188,568	$ 96,995,861	$ 99,907,907
Change in Net Assets/Position										
Governmental activities	$ 9,058,346	$ 14,970,553	$ 15,758,478	$ 16,587,871	$ 17,460,917	$ 18,379,912	$ 19,347,277	$ 20,365,554	$ 21,437,425	$ 22,565,711
Business-type activities	2,059,759	5,833,648	6,140,682	6,463,876	6,804,080	7,162,190	7,539,147	7,935,945	8,353,626	8,793,290
Total primary government	$ 11,118,105	$ 20,804,201	$ 21,899,160	$ 23,051,747	$ 24,264,997	$ 25,542,102	$ 26,886,424	$ 28,301,499	$ 29,791,051	$ 31,359,001

[a] Beginning in 20X5, the City began reporting net position rather than net assets, in accordance with GASB Statement 63.

Figure 47 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Figure 48. Statistical Section Schedule of Revenue Base Information

City of Mathematical
Assessed Value and Estimated Actual Value of Taxable Property ①
Last 10 Fiscal Years
(in thousands of dollars)

Fiscal Year Ended June 30	Residential Property	Commercial Property	Industrial Property	Less: Tax Exempt Property	Total Taxable Assessed Value	② Total Direct Tax Rate	Estimated Actual Taxable Value	③ Assessed Value[a] as a Percentage of
20X0	$2,593,519	$ 1,815,464	$1,556,112	$ 778,056	$5,187,039	$4.05	$14,902,445	40.028%
20X1	2,697,275	1,888,093	1,618,365	809,183	5,394,551	3.62	15,498,630	40.028
20X2	2,648,721	1,854,105	1,589,233	794,616	5,297,442	3.33	15,219,635	40.028
20X3	2,688,372	1,881,861	1,613,023	806,512	5,376,745	3.20	15,447,473	40.028
20X4	2,710,909	1,897,637	1,626,546	813,273	5,421,819	3.22	15,576,971	40.028
20X5	2,857,171	2,000,020	1,714,303	857,151	5,714,343	3.11	16,417,397	40.028
20X6	3,118,397	2,182,878	1,871,038	935,519	6,236,794	2.96	17,918,409	40.028
20X7	3,426,648	2,398,654	2,055,989	1,027,994	6,853,297	2.95	19,689,630	40.028
20X8	3,912,429	2,738,700	2,347,457	1,173,729	7,824,858	2.85	22,480,942	40.028
20X9	4,374,719	3,062,304	2,624,832	1,312,416	8,749,439	2.98	25,137,277	40.028

Source: Gerrard County Board of Equalization and Assessment.

Note: Property in Gerrard County is reassessed once every five years on average. The County assesses property at approximately 45 percent of actual value for commercial and industrial property and 35 percent for residential property. Estimated actual value is calculated by dividing assessed value by those percentages. Tax rates are per $1,000 of assessed value. ④

[a] Includes tax-exempt property.

Figure 48 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② The total direct rate often is either an aggregate of individual levy rates (for instance, one rate applied to all property for debt service plus a second rate applied to all property for general operating support) or a weighted-average of different rates applied to different types of property.

③ This percentage is a weighted average of separate assessment rates applied to residential property and other property, as described in the note to the schedule.

④ Governments briefly describe how property is assessed.

Figure 49 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② If there are limitations on a government's ability to raise its most significant own-source revenue, it is disclosed in this schedule.

Figure 50 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② At first blush, the requirement to present information for the current year and the period nine years prior may seem counterintuitive. However, you should notice that the 2 years reported here are the same as the first and last years of the 10-year trends reported in the other revenue capacity schedules.

Figure 49. Statistical Section Schedule of Direct and Overlapping Rates

City of Mathematical
① Direct and Overlapping Property Tax Rates
Last 10 Fiscal Years
(rate per $1,000 of assessed value)

	City Direct Rates					Overlapping Rates [a]		
Fiscal Year	Basic Rate	General Obligation Debt Service	Redevelopment Debt Service	Redevelopment Program	Total Direct	Anfield School District	Shankly Flood Control District	Owen County
20X0	$ 1.89	$ 0.17	$ 1.76	$ 0.23	$ 4.05	$ 2.10	$ 0.11	$ 4.32
20X1	1.75	0.17	1.47	0.23	3.62	2.25	0.11	4.36
20X2	1.66	0.17	1.26	0.23	3.33	2.31	0.11	4.42
20X3	1.66	0.17	1.15	0.23	3.20	2.33	0.11	4.48
20X4	1.66	0.21	1.12	0.23	3.22	2.35	0.11	4.56
20X5	1.66	0.24	0.97	0.23	3.11	2.35	0.13	4.61
20X6	1.66	0.20	0.87	0.23	2.96	2.39	0.13	4.65
20X7	1.66	0.18	0.88	0.23	2.95	2.37	0.13	4.60
20X8	1.66	0.16	0.80	0.23	2.85	2.45	0.13	4.52
20X9	1.66	0.14	0.95	0.23	2.98	2.45	0.13	4.23

Source: Owen County Board of Equalization and Assessment.

Note: The City's basic property tax rate may be increased only by a majority vote of the City's residents. Rates for debt service are set based on each year's requirements.

[a] Overlapping rates are those of local and county governments that apply to property owners within the City of Mathematical. Not all overlapping rates apply to all Mathematical property owners; for example, although the County property tax rates apply to all City property owners, the Flood Control District rates apply only to the approximately one-third of city property owners whose property is located within that District's geographic boundaries. ②

Figure 50. Statistical Section Schedule of Principal Revenue Payers

City of Mathematical
Principal Property Tax Payers
Current Year and Nine Years Ago ②

①

	20X9			20X0		
Taxpayer	**Taxable Assessed Value**	**Rank**	**Percentage of Total City Taxable Assessed Value**	**Taxable Assessed Value**	**Rank**	**Percentage of Total City Taxable Assessed**
Tofu Farmers of America, Inc.	$ 120,316,033	1	1.38%	$ 80,545,475	1	1.53%
Kenwood Health Plan, Inc.	85,616,816	2	0.98	32,696,104	4	0.60
Oak Energy Partners Ltd.	82,521,151	3	0.94	—		—
Reanimator Laboratories	69,373,517	4	0.79	46,738,407	3	0.86
Pine Scent Car Fresheners	18,686,454	5	0.21	8,594,292	7	0.16
Jamie Q. Public	18,320,000	6	0.21	—		—
Willow Container Corp.	17,504,162	7	0.20	—		—
Deanland Properties	15,455,204	8	0.18	11,400,269	6	0.21
Kramerica, Inc.	14,666,419	9	0.17	—		—
Vandelay Industries	13,298,369	10	0.15	—		—
Acorn Energy Partners Ltd.	—		—	50,167,988	2	0.93
Shrub Plaza Company	—		—	19,692,339	5	0.36
Wooden Acres Ltd.	—		—	7,913,882	8	0.15
Balsawood Farms	—		—	4,703,927	9	0.09
Fern Foundries	—		—	3,767,223	10	0.07
Total	$ 455,758,125		5.21%	$ 266,219,906		4.96%

Source: County Board of Equalization and Assessment.

Revenue rates

The two basic factors that largely determine a government's revenues are (1) the base or activity that is being taxed or charged and (2) the rates or fees that are applied to them. In addition to information about the base or activity, a government presents SI about the tax rates or charges related to its most significant own-source revenue. (See Figure 49.)

Figures 48 and 49: The total direct property tax rate dropped from $4.05 to $2.98 between 20X0 and 20X9.

Although a government may apply a single tax rate or fee, it is equally common to apply a variety of rates to different components of the revenue base or multiple fees to different types of customers. A utility might set different rates for residential and commercial customers, for instance. Multiple property tax rates often are levied for different types of property. A government also may have separate taxes on the same revenue base for separate purposes. For example, the government might levy a basic tax on property for the general support of the government, in addition to a separate property tax that is used for repaying debt or financing some other specific activity. Each of the individual rates that the government levied for the past 10 years for its most significant own-source revenue is reported in this schedule, as well as the same total direct rate reported in the revenue base schedule. That should help you to crosswalk the two schedules.

It may be the case that more than one government is levying a tax or charging a fee against a particular revenue base. This is very common for property taxes—a village, town, school district, other special districts, and county government all might be levying taxes on the same property. In order to get a sense of the total tax burden on the revenue base of interest, the schedule also includes the tax rates of overlapping governments. As with the overlapping debt schedule (see Part Six), overlapping governments are those that coincide geographically, at least in part, with the government. The illustrative city government in Figure 49 overlaps with three governments that also levy a property tax—a school district, a flood control district, and a county.

Figure 51. Statistical Section Schedule of Principal Revenue Payers for a Government Reporting a Personal Income Tax

State of Calculation

① **Personal Income Tax Filers and Liability by Income Level**

Current Year and Nine Years Ago

(income tax liability amounts are in thousands)

②

20X9

Income Level	Number of Filers	Percentage of Total	Personal Income Tax Liability	Percentage of Total
$100,001 and higher	16,666	6.05%	$ 1,212,121	51.67%
$75,001–$100,000	9,999	3.63	222,333	9.48
$50,001–$75,000	22,222	8.06	333,444	14.22
$25,001–$50,000	75,555	27.42	444,555	18.95
$10,001–$25,000	79,999	29.03	111,222	4.74
$10,000 and lower	71,111	25.81	22,003	0.94
Total	275,552	100.00%	$ 2,345,678	100.00%

20X0

Income Level	Number of Filers	Percentage of Total	Personal Income Tax Liability	Percentage of Total
$100,001 and higher	14,666	6.01%	$ 818,818	46.38%
$75,001–$100,000	8,555	3.50	161,161	9.13
$50,001–$75,000	18,888	7.73	292,292	16.53
$25,001–$50,000	67,777	27.75	353,353	20.02
$10,001–$25,000	70,999	29.07	121,121	6.86
$10,000 and lower	63,333	25.93	18,687	1.06
Total	244,218	100.00%	$ 1,765,432	100.00%

Source: State Department of Treasury.

Figure 51 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② For certain revenues, such as a personal income tax, a government may be legally prohibited from disclosing individual payers. In such circumstances, governments present alternative information that informs the issue of concentrations of sources from which the own-source revenue is derived. This is an illustration of one type of information that a government might present instead for a personal income tax.

The capacity to raise revenues is not simply a matter of how high a government's rates are in comparison with other governments or how much those rates have changed over time, though these are important considerations. Just as a government's power to issue long-term debt may be legally limited, so too may be its power to raise tax rates or user fees. For example, a government may be able to increase tax rates only if approved by the voters. If a government's ability to change the rates of its most significant own-source revenue is legally restricted in any way, it explains the nature of the restriction in a note to this schedule.

Principal revenue payers

The third revenue capacity SI schedule lists, for the current year and the period nine years before, the most significant payers of the own-source revenue. (See Figure 50.) The purpose of this information is to help you assess how dependent a government is on the largest payers of its own-source revenue. In addition to identifying the payers, the schedule shows the amount of the revenue base related to each payer *or* the actual taxes levied or fees charged to each. Finally, for each payer, the amount of revenue base they represent or the actual taxes (or fees) they were levied is divided by the total revenue base or total taxes (or fees), respectively, to produce the percentage they account for. Governments generally include the 10 largest payers, but they may include fewer if less than 10 payers account for half or more of the total revenue base or total taxes levied.

Figure 50: Tofu Farmers of America, Inc. was the largest property taxpayer in both 20X0 and 20X9, but its share of total taxable assessed value decreased from 1.53% to 1.38%.

Some governments may not be able to identify individual payers. For example, governments generally are prohibited from identifying individual income tax payers. If this is the case, a government presents other information that will help you to assess whether significant amounts of its own-source revenue come from specific types of payers. Figure 51 is an illustration of how a government reporting an income tax might comply with this requirement. The schedule divides the income tax liability among 6 income levels and reveals that the highest level—$100,001 and higher—represents just 6 percent of the taxpayers but accounts for more than half of the income taxes.

Figure 52. Statistical Section Schedule of Property Tax Levies and Collections

City of Mathematical
① Property Tax Levies and Collections
Last 10 Fiscal Years

Fiscal Year Ended June 30	Taxes Levied for the Fiscal Year	Collected within the Fiscal Year of the Levy		Collections in Subsequent Years	Total Collections to Date	
		Amount	Percentage of Levy		Amount	Percentage of Levy
20X0	$ 21,012,190	$ 18,343,800	87.30%	$ 2,508,286	$ 20,852,086	99.24%
20X1	19,520,892	17,595,149	90.13	1,771,684	19,366,833	99.21
20X2	17,616,968	15,456,835	87.74	1,944,119	17,400,955	98.77
20X3	17,225,167	15,124,061	87.80	1,933,017	17,057,079	99.02
20X4	17,473,003	15,486,912	88.63	1,787,482	17,274,394	98.86
20X5	17,746,808	15,501,805	87.35	1,908,253	17,410,058	98.10
20X6	18,462,001	16,346,494	88.54	1,586,631	17,933,124	97.14
20X7	20,242,938	18,359,297	90.69	1,255,761	19,615,057	96.90
20X8	22,326,307	20,581,542	92.19	872,383	21,453,924	96.09
20X9	26,083,673	24,158,911	92.62	—	24,158,911	92.62
			②		③	④

Sources: Owen County Board of Equalization and Assessment and Owen County Department of Finance.

Totals may not add due to rounding.

Figure 52 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② This column equals the amount collected within the fiscal year of the levy divided by the taxes levied.

③ This column equals collections within the fiscal year of the levy plus collections in subsequent years.

④ This column equals total collections to date divided by taxes levied.

Property tax levies and collections

If a government reports a property tax as its most significant own-source revenue, it presents a fourth SI schedule. For each of the past 10 tax periods, this schedule presents the following information (see Figure 52):

1. The amount of property tax levied
2. The amount of that levy that was collected prior to the end of the period
3. The amount collected divided by the total levy (2 ÷ 1)
4. The amount of that levy collected after the end of the period
5. The total amount of that levy collected (2 + 4), and
6. The total amount collected to date divided by the total levy (5 ÷ 1).

What can you do with revenue capacity information?

The information in the revenue capacity schedules is intended to help you understand and assess the factors that affect a government's ability to raise its most significant own-source revenue. The revenue base schedule informs you about how the economic base or activity underlying the revenue has changed over the last decade. Is it growing or declining? Are particular parts of the base—such as residential property versus commercial, or certain kinds of retail sales—growing faster or slower than the total revenue base? What effects are these changes likely to have on the revenue the government obtains? Can the government potentially broaden its tax or fee to apply to other parts of the revenue base? For instance, are there retail activities to which a county's sales tax currently is not applied?

With the exception of broadening the activities on which a tax or fee can be levied, the revenue base largely is beyond the control of the government. The government likely has more control over the rates it levies or sets. (Though, as mentioned above, there may be legal limitations on its rate-setting abilities.) Has the government been raising rates (or lowering them) over the past 10 years? Have certain rates increased at a different pace from others? The number of rate increases and their magnitude would certainly bear on your judgments about the government's ability to raise rates further. Comparisons with other governments' rates also might be meaningful, though you should be

certain that the rates apply to the same kind of base, measured in the same way. (See **Keep in mind…comparing assessed property values and tax rates in multiple jurisdictions.**)

The schedule of principal payers helps to answer the following questions: Who are the biggest taxpayers for the government? How much of the revenue do they provide? In other words, how dependent is the government on those payers, and what could potentially happen if one of them went out of business or moved away?

The information about property tax levies and collections is useful in at least two ways. First, it may be an indicator of the financial management capabilities of the government. How good a job does it do in collecting its taxes? Has its ability to collect what it levies improved or declined over time? Second, it may be an early warning sign of economic problems on the horizon. A declining collection rate in the fiscal year of the levy could be an indication that some property owners are having financial difficulties, which ultimately could reduce other revenue sources or increase certain government spending needs.

the TOTAL DIRECT RATE generally is the sum of the individual rates a government applies to a revenue base, such as a general property tax rate and special property tax rate for debt service added together, or a weighted average of rates applied to different categories of revenue base, such as residential, industrial, and commercial property

By the numbers…revenue and expense policies

The SSAP contains several revenue- and expense-related descriptions and disclosures:

- The government's policy for allocating indirect expenses such as overhead (if it does so) among the functions and programs in the statement of activities (indicated with a ③ in Figure E-2)
- A description of the types of transactions included in program revenues ③
- An explanation of what constitutes the operating and nonoperating revenues of its proprietary funds ④
- Under the modified accrual basis of accounting used in the governmental funds, revenue is recorded if it is collected during the year or soon enough in the following year that it is *available* to pay for current-year liabilities. Accounting standards specify that the time after the end of the fiscal year in which collections can be considered revenue (the "period of availability") is 60 days for property taxes but do not specify the period for any other type of revenue; a government identifies in the SSAP the length of time it uses to define *available* for its other revenue sources, ⑥ and
- Interest expenses generally are reported in a separate line on the statement of activities; however, the government discloses any interest expense that is included in the direct expenses reported by function, program, or identifiable activity.

Keep in mind…an abatement by any other name

The labels that are used to describe the various types of tax expenditures often are interchangeable from government to government. Consequently, there are some transactions that are called abatements but that do not meet the definition of a tax abatement that should be disclosed by a government. On the other hand, there are transactions with other names—credits, refunds, exemptions, tax increment financings, and so on—that *may* meet the definition of a tax abatement. When they do, they should be included in a government's note disclosure. The point is to focus on whether the substance of the transaction meets the definition rather than on how a government titles the transaction.

By the numbers…reporting of revenues and expenses by BTAs and fiduciary activities

The kinds of information about changes in net position that are reported by governments that are engaged solely in BTAs or solely in fiduciary activities are somewhat different. BTAs present revenues by major source and distinguish between operating and nonoperating revenues and expenses.

Governments conducting only fiduciary activities report additions by source and deductions by type. Deductions related to benefit payments and refunds are shown in further detail by type of benefit (such as age and service pension, disability pension, health insurance coverage, and so on) and type of refund. These governments report this information separately for each of their individual pension or OPEB plans.

By the numbers…overlapping rates—who's in and who's out?

Not all governments are required to include the OVERLAPPING RATES in their revenue rate schedule, and not all overlapping governments' rates are included in the schedule. State government rates are not included in the schedules prepared by localities and other sub-state-level governments, and states are not required to include overlapping rates in their schedules. Regional governments (for example, counties encompassing a large number of local governments) are encouraged to present this schedule but are not required to do so.

Keep in mind…actual property value

When the schedule of revenue base information is prepared for a property tax, it includes both assessed value and actual value. Most of the time, the actual value amounts are estimated, often by simply dividing the assessed value amounts by an assumed percentage. Although the actual value amounts sometimes are the product of sophisticated surveys of actual property sales, even these amounts may be estimated based on an application of actual sales experience from a small fraction of properties to the majority of properties that have not been sold recently. Whatever method the government uses, it describes it in a note to the schedule.

Keep in mind…comparing assessed property values and tax rates in multiple jurisdictions

Assessed value usually is a fraction of market value and a product of a government's particular system for assessing property values. Care must be taken to be certain that the assessed value information for the governments you are comparing actually is equivalent and comparable. Otherwise, the tax rates may not be comparable. Consider, for example, two governments that apply the same tax rate to assessed value; but, one government assesses property at full market value, while the other assesses at just 25 percent of market value. Without knowing anything about their assessment policies, you might think their rates were comparable. However, despite having the same tax rate, the tax burden actually is four times greater in the government that assesses at full value.

PART NINE

GOVERNMENTAL FUNDS

The governmental funds generally track the financial activity of a government's basic services—such as regular education, special education, and busing for school districts; police, fire, and parks for a local government; or income support, higher education, and prisons for state governments. These services are considered the staples of government and basically are the same as those included in the governmental activities of the government-wide statements.

By the numbers…comparing governmental activities and governmental funds

There are three key differences between the governmental funds and governmental activities—the scope of a government they cover, the kinds of resources they include, and the types of financial activities they report.

	Governmental Activities	**Governmental Funds**
Scope	• Typically the basic services of a government (no BTAs or fiduciary activities) • Contain the activities of governmental funds • Typically include internal service funds	• Typically the basic services of a government (those not included in proprietary and fiduciary funds) • Internal service funds are included among the proprietary funds (discussed in Part Ten)
Types of Resources	Economic resources—all assets and liabilities, both financial and capital	• Current financial resources—financial assets (generally, cash and assets that will become cash in the next year) and current liabilities that current assets generally will be used to pay off • No capital assets or long-term liabilities
Types of Financial Activities	All transactions and other events regardless of whether cash changed hands	Transactions and other events in which (a) cash was received during the year or soon thereafter, (b) goods or services were received and payment was normally due, or (c) resources flowed between the governmental and other funds

Two financial statements report the finances of the governmental funds—the balance sheet and the statement of revenues, expenditures, and changes in fund balances. As explained in Part Two, the governmental funds statements employ a current financial resources measurement focus and modified accrual basis of accounting, producing very different information from the government-wide financial statements.

Government-wide financial statements aggregate a government's financial information into two categories—governmental activities and BTAs (and sometimes component units). The fund financial statements provide some of the detail behind those highly aggregated numbers.

By the numbers…types of governmental funds

	Fund Types	**Examples**
Governmental Funds track the basic activities of a government	The *general fund* accounts for the most basic, tax-supported activities of a local government (technically, the resources not required to be in another fund).	Every general purpose government has a general fund or primary operating fund, in which it typically accounts for police, fire, parks, education, and similar activities.
	Special revenue funds track revenue sources restricted or committed to specific uses.	State mental health aid received and used by a county is tracked in the county's mental health fund.
	Capital projects funds follow the resources used to build, acquire, and renovate major general capital assets.	A city issues long-term bonds and uses the proceeds to upgrade its recreational facilities; this activity is accounted for in the capital improvements fund.
	Debt service funds account for resources used to repay general long-term debt.	A county has separate funds for repaying general obligation debt and tax-backed bonds.
	Permanent funds report resources legally restricted	A scholarship fund tracks investments donated by a resident who stipulates that only the earnings of the

	so that only the earnings they generate—and not the resources themselves—may be used.	investments be used to provide college scholarships to needy students.

In the governmental funds financial statements, governments show their **MAJOR FUNDS** individually. The remaining **NONMAJOR FUNDS** are combined in a column on the right-hand side of the statement. Displaying major funds separately provides information that is useful for tracking the financial activity of specific programs and revenue sources. There are three circumstances under which a fund is considered major and is displayed in its own column in the financial statements:

1. The main operating fund (usually the general fund) always is considered major.
2. An individual governmental or enterprise fund's assets (plus deferred outflows), liabilities (plus deferred inflows), revenues, OR expenditures/expenses are at least:
   a. 10 percent of the total for all governmental OR enterprise funds, respectively, AND
   b. 5 percent of the total for all governmental AND enterprise funds *combined*.
3. A government may report as major any other governmental or enterprise fund it believes is important to the users of its financial statements.

This last clause suggests that if there is fund information that users of financial statements consider important and want to see included individually on the statements, a government has the ability to comply (though it is not required to). Governments also may choose to include certain funds to meet state or federal reporting requirements.

Figure E-4 in Appendix E presents the calculations for the funds listed in Local City's governmental funds statements (Figures 53 and 54). The general fund qualifies automatically, though it also is large enough to qualify under liabilities/deferred inflows, revenues, and expenditures. The HUD Programs fund qualifies by liabilities/deferred inflows, and the Community Redevelopment fund by assets/deferred outflows. The inclusion of the Route 7 Construction fund is done at the government's discretion, though it should be noted that the fund is close to qualifying by both assets/deferred outflows and expenditures.

BALANCE SHEET

In form and function, the balance sheet is very similar to the statement of net position. Both contain assets, deferred outflows, liabilities, and deferred inflows, though the balance sheet contains primarily *current* assets and liabilities. Instead of net position, the balance sheet ends with fund balance. The arrangement of the balance sheet is slightly different—*assets plus deferred outflows equal liabilities plus*

deferred inflows plus fund balances, rather than assets plus deferred outflows minus liabilities minus deferred inflows equals net position—but this is more a function of emphasis than a substantive difference.

As you can see in Figure 53 (and Figures B-3 and C-3), the types of assets and liabilities are listed on the left-hand side, just as in the statement of net position. The columns, however, primarily represent individual major governmental funds. The general fund always is included and is listed first. Any individual special revenue, capital projects, debt service, and permanent funds that qualify as major are listed subsequently. The remaining nonmajor funds are aggregated in a single column, second from the right. The nonmajor funds may be shown individually in combining financial statements included in a government's CAFR. (This is discussed on page 226 with the supporting information.) Finally, all of the governmental funds are totaled in the right-hand column.

Fund Balance

The fund balances listed at the bottom of the statement are divided among five categories:

- Nonspendable
- Restricted
- Committed
- Assigned, and
- Unassigned.

These categories of fund balance are based on the degree to which a government is bound to honor the constraints placed on how the fund balance can be used—ranging from nonspendable as the most stringent constraint to unassigned as the least (actually, no constraint at all).

NONSPENDABLE FUND BALANCE represents resources that cannot be spent, either because they are not in spendable form (such as inventory) or are required by an external individual or organization to be maintained intact (such as an amount donated to the government with the stipulation that it be invested and only the earnings be spent, which would be reported in a permanent fund).

RESTRICTED FUND BALANCE is constrained in the same ways as the resources represented by restricted net position—for instance, a federal program requirement or a provision in the state constitution.

Figure 53: Fund balance restricted to debt service in the nonmajor funds was $3,832,062.

Figure 53. Governmental Funds Balance Sheet

Local City
Balance Sheet
① Governmental Funds
As of December 31, 2017

	General	HUD Programs	③ Community Redevelopment	Route 7 Construction	④ Other Governmental Funds	Total Governmental Funds	
ASSETS ②							
Cash and cash equivalents	$ 3,418,485	$ 1,236,523	$ —	$ —	$ 5,606,792	$ 10,261,800	
Investments	—	—	13,262,695	10,467,037	3,485,252	27,214,984	
Receivables, net	3,644,561	2,953,438	353,340	11,000	10,221	6,972,560	
Due from other funds	1,370,757	—	—	—	—	1,370,757	
Receivables from other governments	—	119,059	—	—	1,596,038	1,715,097	
Liens receivable	791,926	3,195,745	—	—	—	3,987,671	
Inventories	182,821	—	—	—	—	182,821	
Total assets	$ 9,408,550	$ 7,504,765	$ 13,616,035	$ 10,478,037	$ 10,698,303	$ 51,705,690	=
LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND FUND BALANCES							
Liabilities:							
Accounts payable	$ 3,408,680	$ 129,975	$ 190,548	$ 1,104,632	$ 1,074,831	$ 5,908,666	
Due to other funds	—	25,369	—	—	—	25,369	
Payable to other governments	94,074	—	—	—	—	94,074	
Advances on grants	—	1,435,599	—	—	—	1,435,599	
Total liabilities (Note 2)	3,502,754	1,590,943	190,548	1,104,632	1,074,831	7,463,708	+
Deferred inflows of resources:							
Unavailable revenue—taxes	4,250,430	—	—	—	—	4,250,430	
Unavailable revenue—grants	—	4,837,446	250,000	11,000	—	5,098,446	
Total deferred inflows of resources	4,250,430	4,837,446	250,000	11,000	—	9,348,876	+
Fund balances: ⑤							
Nonspendable							
Inventories	182,821	—	—	—	—	182,821	
Nonexpendable corpus	—	—	—	—	1,405,300	1,405,300	
Restricted for:							
Community development	—	576,376	2,119,314	—	—	2,695,690	
Debt service	—	—	—	—	3,832,062	3,832,062	
Capital projects	—	—	—	5,792,587	675,404	6,467,991	
Other purposes	310,027	—	—	—	—	310,027	
Committed to:							
Community development	—	500,000	11,056,173	—	—	11,556,173	
Capital projects	—	—	—	2,569,818	—	2,569,818	
Other purposes	40,292	—	—	—	1,138,718	1,179,010	
Assigned to:							
Parks and recreation	100,000	—	—	—	1,007,077	1,107,077	
Capital projects	—	3,195,745	—	1,000,000	1,241,270	5,437,015	
Other purposes	—	—	—	—	323,641	323,641	
Unassigned ⑥	1,022,226	—	—	—	—	1,022,226	
Total fund balances	1,655,366	4,272,121	13,175,487	9,362,405	9,623,472	38,088,851	+
Total liabilities, deferred inflows of resources, and fund balances	$ 9,408,550	$ 10,700,510	$ 13,616,035	$ 10,478,037	$ 10,698,303		

⑦ Amounts reported for *governmental activities* in the statement of net position are different because (see Note 4, also):

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	161,082,708
Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the funds.	9,348,876
Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the statement of net position.	2,994,691
Deferred outflows of resources and deferred inflows of resources related to pension and retiree health insurance liabilities and derivatives are not reported in the funds.	9,782,596
Certain accounts payable are not due and payable in the current period and, therefore, are not reported in the funds.	(469,534)
Long-term liabilities, including bonds payable and retirement benefits, are not due and payable in the current period and, therefore, are not reported in the funds.	(185,056,759)
Net position of governmental activities	$ 35,771,429

Figure 53 Notes

① Three items generally appear at the top of each statement: name of the government, name of the statement, and date of or period covered by the statement. The fund financial statements also identify the category of funds covered by the statement (governmental, proprietary, or fiduciary).

② No distinction is made between current and noncurrent because governmental funds mostly present current financial resources; there are no capital assets or long-term liabilities.

③ The governmental funds statements present a government's *major* funds individually. The criteria defining major can be found on page 195.

④ The funds that are not major are aggregated in a single column; some governments report them individually in a combining statement with their supplemental information.

⑤ A government does not have to show this level of detail for fund balance on the balance sheet. It may show as little as just the aggregate amounts for each of the five categories (see page 213), as long as it presents the detail for each category in the notes to financial statements.

⑥ Unassigned should be a positive number only in the general fund. If a negative number (in parentheses) is shown on the assigned fund balance line in one of the other governmental funds, it means that fund spent more for a particular purpose than it had available for that purpose.

⑦ The reconciliation of total governmental fund balance to the net position of governmental activities that you find may not be this detailed. Some governments provide greater detail in the notes (see Figures 58 and 59) if the descriptions here are broad or if there are important adjustments that cannot be identified within the larger categories. Some governments may place the reconciliation on a separate page from the statement (see Figure 55, for example).

COMMITTED FUND BALANCE is constrained by a government itself, using its highest level of decision-making authority (perhaps a statute passed by a state legislature or resolution passed by a city council; the exact action may differ from government to government). Committed fund balance is different from restricted in that a government does not have to obtain the agreement of another government or get a constitutional provision changed in order to use the resources for another purpose. Nonetheless, committed fund balance cannot be used for any purpose other than the use for which it was committed unless a government again uses its highest level of decision-making authority to change or remove the purpose limitation.

Figure 53: Fund balance committed to community redevelopment was $11,556,173 for all governmental funds combined.

By contrast, **ASSIGNED FUND BALANCE** represents resources a government *intends* to use for a particular purpose. Ultimately, a government may use these resources for some other purpose without taking any further action to change the assignment. Fund balances outside of the general fund (for instance, in a special revenue fund) are at least assigned, and often are committed or restricted. This means that when you see resources in another governmental fund, you know that the government at a minimum *intends* to use those resources for the purpose associated with the fund (such as repaying long-term debt or constructing roads).

Figure 53: Fund balance assigned to parks and recreation in the general fund was $100,000.

The final category is **UNASSIGNED FUND BALANCE.** Unassigned fund balance contains the resources not required to be reported in one of the other categories. In other words, these resources are not constrained in any way, not even by intent, and can be used for any purpose. The only place that you will see a positive unassigned fund balance is in the general fund. If a number appears on the unassigned line in another governmental fund, it will be a negative number (either presented in parentheses or preceded by a minus sign). That indicates that the government spent more for a particular purpose than was available in that fund.

Figure 53: Local City had $1,022,226 in unassigned fund balance.

Reconciliation

Both of the governmental funds statements contain a **RECONCILIATION** that explains how they differ from the governmental activities in the government-wide financial statements. Reconciliations are useful because they can help explain how the shorter term financial information in the governmental funds statements differs from the more comprehensive financial information in the government-wide statements. The reconciliation in the balance sheet explains the differences between *total fund balance* for the governmental funds and *total net position* for governmental activities at the government-wide level.

The reconciliation may appear in the lower right corner of the balance sheet, below the total fund balance for the governmental funds, although a government has the option to put it in an accompanying schedule on the page following the balance sheet. (See Figure B-4, for instance.) In either case, a government may provide less detail with the balance sheet but then offer sufficient additional explanation in a note to the financial statements. A sample illustration of this note (Figure 58) is presented on page 217.

- The first item and the last two items in the reconciliation in Figure 53 reflect the difference between the governmental funds' emphasis on current resources and the comprehensive focus of the governmental activities. The governmental funds do not include capital assets or long-term liabilities, so they must be added to total fund balances to reach governmental activities net position.
- The second item results from the requirement that revenues be "available" to pay for current expenditures in order to be recorded as revenues and be included in the governmental fund balances. The portion of revenues that did not meet that criterion and were deferred in the governmental funds must be added in.

- Certain deferred outflows and deferred inflows, such as those related to pensions and OPEB, are not related to flows of current financial resources and need to be added to governmental fund balance.
- Finally, the net position of the internal service funds must be added to the governmental fund balance. Internal service funds are shown with the proprietary funds because they operate in a business-like manner. However, they almost always are governmental in purpose and, therefore, are included among the governmental activities in the government-wide statements, rather than among the BTAs.

What Can You Do with Balance Sheet Information?

The potential uses of the information in the balance sheet are similar to those of the statement of net position information. However, while many of the analyses are the same, the analyses tell you different things about the government because the information in the two statements is inherently different.

You can analyze the nature of current financial resources

Percentage distributions and percentage changes can tell you what kinds of (mostly short-term) financial resources and short-term liabilities the government has, and how their balances have changed over time.

You can assess short-term financing needs and a government's capacity to meet them

The short-term financial information contained in the governmental funds statements makes them particularly well-suited for assessing the near-term financial issues of a government's basic public services. Liquidity can be assessed in a very straightforward fashion. The balance sheet information is essential for this purpose if the statement of net position does not present current and noncurrent assets and liabilities separately and you cannot separate them on your own.

You can understand the relationships between government-wide and governmental funds statements and their respective accounting methods

The reconciliation is an extremely valuable tool for learning about these differences. It is informative both about differences in the scope of the activities that each encompasses and about how the accounting assumptions of the two kinds of statements differ. For instance, the list of adjustments to fund balance tells you the effect that the accounting methods used in governmental funds statements have in comparison to the government-wide statements.

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES

The inflows and outflows measured in the governmental funds are different from the more comprehensive changes in net position in the statement of activities; this statement focuses primarily on cash and other current financial resources that come into and flow out of a government. Consistent with the fund focus of these statements, the difference between revenues (and OTHER FINANCING SOURCES) and expenditures (and OTHER FINANCING USES) is CHANGE IN FUND BALANCE rather than change in net position.

This statement contains the same major funds in columns as the balance sheet, with "other governmental funds" and "total governmental funds" columns on the right. (See Figures 54, B-5, and C-4.) Governments categorize revenues by nature or type: various taxes, fees, and earnings; intergovernmental aid; and so on. Expenditures are listed by function. Expenditures for debt service and capital outlays (for building or buying capital assets) are listed separately from the functional operating expenditures.

Figure 54: General government expenditures in the Community Redevelopment fund were $417,814.

Figure 54. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances

Local City
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
for the Year Ended December 31, 2017

	General	② HUD Programs	Community Redevelopment	③ Route 7 Construction	④ Other Governmental Funds	Total Governmental Funds	
REVENUES ①							
Property taxes	$ 51,173,436	$ —	$ —	$ —	$ 4,680,192	$ 55,853,628	
Franchise taxes	4,055,505	—	—	—	—	4,055,505	
Public service taxes	8,969,887	—	—	—	—	8,969,887	
Fees and fines	606,946	—	—	—	—	606,946	
Licenses and permits	2,287,794	—	—	—	—	2,287,794	
Intergovernmental	6,119,938	2,578,191	—	—	2,830,916	11,529,045	
Charges for services	11,374,460	—	—	—	30,708	11,405,168	
Investment earnings	552,325	87,106	549,489	270,161	364,330	1,823,411	
Miscellaneous	881,874	66,176	—	2,939	94	951,083	
Total revenues	86,022,165	2,731,473	549,489	273,100	7,906,240	97,482,467	+
EXPENDITURES ⑤							
Current:							
General government	8,630,835	—	417,814	16,700	121,052	9,186,401	
Public safety	33,729,623	—	—	—	—	33,729,623	
Public works	4,975,775	—	—	—	3,721,542	8,697,317	
Engineering services	1,299,645	—	—	—	—	1,299,645	
Health and sanitation	6,070,032	—	—	—	—	6,070,032	
Cemetery	706,305	—	—	—	—	706,305	
Culture and recreation	11,411,685	—	—	—	—	11,411,685	
Community development	—	2,954,389	—	—	—	2,954,389	
Education—payment to school district	21,893,273	—	—	—	—	21,893,273	
Debt service:							
Principal ⑥	—	—	—	—	3,450,000	3,450,000	
Interest and other charges	—	—	—	—	5,215,151	5,215,151	
Capital outlay	—	—	2,246,671	11,281,769	3,190,209	16,718,649	
Total expenditures	88,717,173	2,954,389	2,664,485	11,298,469	15,697,954	121,332,470	−
Excess (deficiency) of revenues over expenditures ⑦	(2,695,008)	(222,916)	(2,114,996)	(11,025,369)	(7,791,714)	(23,850,003)	= +
OTHER FINANCING SOURCES (USES)							
Proceeds of long-term capital-related debt	—	—	17,529,560	—	2,060,856	19,590,416	
Transfers in	129,323	—	—	—	5,551,187	5,680,510	
Transfers out	(2,163,759)	(348,046)	(2,273,187)	—	(219,076)	(5,004,068)	
Total other financing sources and uses	(2,034,436)	(348,046)	15,256,373	—	7,392,967	20,266,858	+
SPECIAL ITEM ⑧							
Proceeds from sale of park land	3,476,488	—	—	—	—	3,476,488	+
Net change in fund balances	(1,252,956)	(570,962)	13,141,377	(11,025,369)	(398,747)	(106,657)	=
Fund balances—beginning	2,908,322	1,647,338	34,110	20,387,774	10,022,219	34,999,763	
Fund balances—ending ⑨	$ 1,655,366	$ 1,076,376	$ 13,175,487	$ 9,362,405	$ 9,623,472	$ 34,893,106	

⑩

Figure 54 Notes

① In the governmental funds, revenues are included only if the transaction occurs and cash is received during the year or soon enough thereafter to be used to pay current costs. They are shown by major source.

② This is a special revenue fund established to report on federal aid received from the Department of Housing and Urban Development (HUD).

③ These are capital projects funds.

④ No debt service or permanent funds qualified as major. They are included in this column.

⑤ Expenditures generally are recorded when a government has received a good or service and payment is normally due. They are listed by major functional category.

⑥ Debt service and capital outlay demonstrate basic differences in the kinds of information contained in the governmental funds and government-wide statements. The government-wide statements report only interest on debt; repayment of principal reduces an outstanding liability, not net position. In the governmental funds statements, the entire cost of capital assets is recorded as an expenditure right away, rather than depreciated over the assets' useful lives.

⑦ Every governmental fund had a deficit—expenditures were greater than revenues. The deficits in the two capital projects funds, however, arise in part because the related inflows—typically proceeds from bonds—are considered *other financing sources* instead of revenues.

⑧ When the differences between revenues and expenditures and between other financing sources and uses are added together, there is a general fund shortfall of $4,729,444 [(2,695,008) + (2,034,436)]. Were it not for the capital asset sale, the beginning fund balance of $2.9 million would have been reduced to a *deficit* of $1.8 million [2,908,322 + (4,729,444)].

⑨ These are the fund balances that appear in the balance sheet (see Figure 53).

⑩ The reconciliation for this statement is presented on a separate page (see Figure 55). It also could be displayed here, as in the balance sheet (see Figure 53).

This distinction from the government-wide statement of activities is a prime example of the differences between the kinds of information the two statements report. As previously described, the cost of purchasing, building, or renovating capital assets is spread over the useful lives of the assets through depreciation in the statement of activities. However, the entire cost is reported as expenditures in the year it is incurred in this governmental funds statement because capital outlays are outflows of current financial resources. Similarly, the governmental funds report *both* interest on long-term debt *and* repayment of debt principal (because both are outflows of current financial resources), whereas the statement of activities includes just the interest expenses (because repayment of principal reduces a liability, debt payable, *not* net position).

Surpluses and Deficits

The difference between revenues and expenditures is labeled as **EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES**, or surplus (deficit). You can see in Figure 54 that each of Local City's major

governmental funds had a deficit—expenditures exceeded revenues—in 2017. After adding in other financing sources (uses) and any extraordinary or special items, the statement presents the total changes in fund balance for the year for each fund. They are added to the fund balances as of the beginning of the year to obtain the ending fund balances that appear in the balance sheet. Local City's general fund and HUD Programs special revenue fund had decreases in fund balance and its Community Redevelopment capital projects fund had a very large increase in fund balance.

What do these results say about Local City's ability to manage its finances? Is it doing a good job or a bad job? It can be difficult to draw conclusions based on a fund's bottom line in a single year, because not all decreases in fund balances (or increases, for that matter) are created equal. Some examples should help explain this distinction.

- Example 1: A capital projects fund shows a sizable decrease in fund balance in a given year. Upon further inspection, you see that the expenditures were financed with the proceeds of long-term bonds that were sold the previous year. This drop in fund balance is the product of the timing of resource flows—the financing source was recorded in one year and the expenditures in the next year. Consequently, you probably should not be too concerned about this deficit. Nor should you have been too elated about the large surplus that fund showed the year before, when the proceeds of the bonds were recorded without any offsetting expenditures.
- Example 2: A general fund shows a sizable decrease in fund balance in a given year. As in the previous example, the decrease may be the product of timing. Alternatively, a school district may have been saving surplus resources from prior years in order to purchase a building or to install state-of-the-art wiring in older school buildings to support computers and Internet access—it reports the expenditures this year but all of the inflows of resources were reported in prior years. However, what if the fund had a decrease in fund balance despite selling some major capital assets (potentially a special item) and borrowing resources from other funds? You might conclude that the government was having trouble making ends meet.

The moral of this story is that surpluses and deficits (and increases and decreases in fund balances) are flags that alert you to potentially favorable and unfavorable situations; you need to ask additional questions to better understand the reasons behind them and their positive and negative connotations. They should be viewed objectively: a deficit in a governmental fund is not automatically bad, nor is a surplus always good.

Other Changes in Fund Balances

As just mentioned, a government shows changes in fund balances that are not revenues or expenditures (or, at least, not typical ones) separately at the bottom of the statement. The purpose is basically the same as in the statement of activities: to allow a direct comparison of the resource flows from a government's activities to ascertain (1) whether the government is raising enough resources (in this case, short-term financial resources) to finance its expenditures and (2) how normal operations

are affecting fund balances. Including other items unrelated to normal operations that change fund balance (such as special and extraordinary items) would distort that picture.

The other financing sources and uses section lists resource flows related to the proceeds from issuing long-term debt, and transfers among funds. Most of the financial activity here is related to Local City's issuance of debt. Much of the transfer activity took place in the general and community redevelopment funds. One can surmise from the nonmajor funds column and the supplemental combining statement for the nonmajor funds (see Figure 64) that these transfers primarily went to Local City's debt service funds.

Reconciliation

Like the balance sheet, this governmental funds financial statement includes a reconciliation—explaining the differences between net change in fund balances for the governmental funds statement and change in net position for governmental activities in the government-wide statement. Figure 53 demonstrates the option a government has to show a reconciliation on the same page as a statement. Figure 54 does not show the reconciliation on the face of the statement; rather, Figure 55 shows how the reconciliation might be displayed on the page following the statement. (The separate-page format also is shown in Figures B-4, B-6, and C-5.) A government provides a note disclosure if additional explanation is necessary, or if the categories in the reconciliation do not present important individual differences. (See the note disclosures discussion beginning on page 215.)

The sample reconciliation in Figure 55 runs through the major explanations of how net change in fund balances differs from change in net position:

- The net change in fund balances is the remainder when expenditures and other outflows of current financial resources are subtracted from revenues and other inflows of current financial resources. Included among expenditures, however, are outflows of current financial resources for capital construction and purchases, which are not included as expenses for governmental activities. (Recall that the construction or purchase price—historical cost—is depreciated over the years of usefulness of the capital asset.) These outflows are removed in the reconciliation.
- When assets are sold, the governmental funds reflect all of the proceeds from the sale, but the government-wide statements count only the portion that represents the gain (or loss) on the sale, not the original purchase price. The original purchase price is removed in the reconciliation.
- The government-wide statements generally report a broader, longer term set of inflows and outflows than the governmental funds. The additional revenues and expenses are added individually (as in Figure 55) or a net amount (revenues minus expenses) is added.
- The resources provided by bond sales and other long-term obligations, and their related liabilities, are treated differently in the two types of financial statements. In the governmental funds they are other sources of financing and increase fund balances; in the government-wide statements they

increase assets but are offset by a liability and have no net effect on net position. Therefore, they do not appear on the statement of activities. Those resources are removed in the reconciliation.

- Internal service funds are included with the proprietary funds, not the governmental funds. However, because they typically are considered a part of the governmental activities in the government-wide statements, they need to be added in.

What Can You Do with Information from the Statement of Revenues, Expenditures, and Changes in Fund Balances?

This statement is not organized to supply the net cost information you can get in the statement of activities. However, it does serve many of the other purposes of that statement, but with a narrower focus on short-term resources and how they are used. You can *describe the nature of the inflows and outflows of current financial resources and how they have changed over time* using percentage change and percentage distribution. Comparisons may be made with other governments, though care must be shown to avoid comparing apples to oranges. The structures and definitions of funds are idiosyncratic, designed primarily to serve the purposes of a government's particular interests and budget; consequently, they may differ greatly from one local government to the next. Furthermore, as noted in Part Seven regarding expenses, the definitions of functional expenditure categories may be different.

Figure 55. Reconciliation of Net Changes in Fund Balances to Change in Net Position (Separate-Page Format)

Local City
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances
of Governmental Funds to the Statement of Activities
for the Year Ended December 31, 2017

Net change in fund balances—total governmental funds	①	$ (106,657)
Amounts reported for *governmental activities* in the statement of activities are different because:	②	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.		13,231,649
In the statement of activities, only the *gain* on the sale of the park land is reported, whereas in the governmental funds, the proceeds from the sale increase financial resources. Thus, the change in the net position differs from the change in the fund balance by the cost of the land sold.		(823,000)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.		1,920,630
Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net position. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position. This is the amount by which proceeds exceeded repayments.		(16,140,416)
Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.		(437,684)
Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The change in net position of the internal service funds is reported with governmental activities.	③	(758,808)
④ Change in net position of governmental activities	⑤	$ (3,114,286)

Figure 55 Notes

① This amount comes from the governmental funds statement of revenues, expenditures, and changes in fund balances (Figure 54).

② A government provides a note disclosure if further clarification is needed because of the abbreviated language and aggregation of the reconciliation. This note is illustrated in Figure 59.

③ The internal service funds are reported in the proprietary funds statements (see Figures 68–70) and not the governmental funds because they try to charge a price for goods and services high enough to recoup their costs. However, the nature of the activity (essentially providing support and administrative services to other parts of a government) merits their inclusion with the governmental activities.

④ The reconciliation also could be presented on the face of the statement, as it is for the illustrative balance sheet in Figure 53.

⑤ This is the amount you will find in the government-wide statement of activities (Figure 42).

You also can compare inflows and outflows to determine whether a government is raising sufficient resources to meet its short-term financing needs. In other words, did the government's fund balances increase or decrease?

Once again, the reconciliation proves to be a valuable instructional tool from which you can learn about the differences between full accrual and modified accrual information and how the governmental funds statements and the government-wide statements relate to one another.

Will a government be able to finance services in the future?

Recall that the statement of net position provides information useful for determining a government's ability to finance its long-run liabilities. This information is used to assess the extent to which a government's assets are *leveraged* by debt. Information from the fund statements and the government-wide statement of activities can inform the issue of *coverage*.

To assess a government's ability to "cover" future repayment of its outstanding debt, you can compare cash flows generated by operations to either its interest payments on debt or its entire debt repayments, both interest *and* principal. (See COVERAGE RATIOS in Part Fourteen.) In general, the larger the cash flows are relative to the pertinent payments, the better a government's ability to repay long-term debt. Conversely, the smaller the cash flows relative to the payments, the more questions may arise about a government's ability to pay off long-term debt. Again, it is up to you to determine what is "large enough" or "too small" or "just right" for a government's coverage ratios. You can do so with trend comparisons and cross-government comparisons, by looking further into the circumstances surrounding a government's outstanding debts, and by seeking out the rules of thumb of regular observers of government debt.

Particular advantages of governmental funds information

While the information in the statement of revenues, expenditures, and changes in fund balances may be used for similar purposes as the statement of activities information, the former may be better suited than the latter to informing budgetary analysis and decision making. Because the governmental funds often are structured like a government's budget, or vice versa, the financial statement information from past years may be comparable to current and future budget numbers. Consequently, you may be able to *use your analysis of past trends to assist in making or assessing present-day budget choices*.

The similarities between budget and fund structure and the display of information for major individual funds also should make the funds statements more useful than the government-wide statements for *judging compliance with budgetary and legal restrictions*. Tracking the collection and use of the revenue from a tax restricted to a particular purpose is easier when the fund that accounts for that tax is visible on the statement, rather than aggregated within a larger category.

NOTE DISCLOSURES RELATED TO THE GOVERNMENTAL FUNDS

Three note disclosures are specifically relevant to the governmental funds balance sheet: interfund balances, fund balance, and reconciliation to the statement of net position. Another four note disclosures relate to the statement of revenues, expenditures, and changes in fund balances: special revenue funds, property taxes, interfund transfers, and reconciliation to the statement of activities.

WHAT'S AHEAD?

- WHAT FINANCIAL ACTIVITY TAKES PLACE AMONG A GOVERNMENT'S FUNDS?
- HOW MUCH DO A GOVERNMENT'S FUNDS OWE TO OTHER FUNDS?
- WERE THERE ANY UNUSUAL TRANSACTIONS AMONG THE FUNDS?

Interfund Balances and Transfers

During the course of a normal year, resources often are moved from one fund to another. For instance, revenues collected in the general fund may be transferred to a debt service fund to be used to repay debt or to a capital projects fund to finance construction. Likewise, amounts left over in one fund after debt has been repaid or a capital project has been completed may be transferred back to the general fund to finance other activities, if allowable. At the end of the fiscal year, some funds may owe resources to other funds. It is difficult to conceive of the volume and nature of these "interfund" activities, however, because they generally are added together and shown in two lines in each of the fund financial statements ("due from other funds" and "due to other funds" in Figure 53, and "transfers in" and "transfers out" in Figure 54).

In order to help you understand this financial activity, governments present note disclosures regarding **INTERFUND TRANSFERS** during the fiscal year and **INTERFUND BALANCES** as of the end of the fiscal year. The latter disclosure shows the amounts *due from* each of the columns in the fund financial statements (except for the total columns) to each of the other columns. (See Figure 56.) These columns include the following (if applicable):

- Each major governmental and enterprise fund individually
- Nonmajor governmental funds in the aggregate
- Nonmajor enterprise funds in the aggregate
- Internal service funds in the aggregate, and
- Each class of fiduciary fund.

The note also discloses the purposes for the interfund balances and identifies any that are not expected to be repaid within a year.

Figure 56: The general fund owed the internal service funds $5,000,000.

The interfund transfers note shows the amounts transferred between those fund columns during the fiscal year. (See Figure 57.) The note also describes the general reasons why a government makes those transfers. A government pays particular attention to the intended purpose and amount of a significant transfer if it meets one or both of these conditions:

- It is a transfer that does not occur on a routine basis
- It is inconsistent with the activities of the fund making the transfer.

What can you do with information about interfund balances and transfers?

The additional detail provided by these disclosures is valuable for helping you to understand how a government's funds interact and the nature of the financial activity that occurs among them. You should be able to obtain a basic appreciation for how resources flow from one fund to another and the reasons they move. Furthermore, if financial activity that is out of the ordinary occurs between funds, you should be able to tell from these notes.

Figure 57: $3,500,000 was transferred from the water and sewer fund to the general fund.

Figure 56. Interfund Balances Note Disclosure

Interfund balances at September 30, 2017, consisted of the following (amounts in thousands):

①

		Due from					
		General Fund	Highway	Redevelopment Agency	Internal Service	All Others	Total
Due to	General fund	$ —	$ 6,000	$ 6,145	$ 8,815	$ 1,777	$ 22,737
	Nonmajor governmental	7,181	—	2,867	—	—	10,048
	Internal service	5,000	7,415	3,834	32	1,104	17,385
	All others	311	—	—	1,113	—	1,424
	Total	$ 12,492	$ 13,415	$ 12,846	$ 9,960	$ 2,881	$ 51,594

The balance of $8,815,000 due to the general fund from the internal service funds resulted from loans made to establish working capital when each internal service fund was first created; $7,285,000 of the balance is not scheduled to be collected in the subsequent year.

All remaining balances resulted from the time lag between the dates that (1) interfund goods and services were provided or reimbursable expenditures occurred, (2) transactions were recorded in the accounting system, and (3) payments between funds were made.

Figure 56 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Figure 57. Interfund Transfers Note Disclosure

Interfund transfers for the year ended December 31, 2017, consisted of the following (amounts in thousands):

①

		Transfer from					
		General Fund	Community Development	Nonmajor Governmental	Water and Sewer	All Others	Total
Transfer to	General fund	$ —	$ —	$ 15,942	$ 3,500	$ 1,933	$ 21,375
	Nonmajor governmental	41,203	4,227	—	—	—	45,430
	Water and sewer	—	—	4,836	—	—	4,836
	All others	2,105	—	9,800	—	—	11,905
	Total	$ 43,308	$ 4,227	$ 30,578	$ 3,500	$ 1,933	$ 83,546

Transfers are used to (1) move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them, (2) move receipts restricted to debt service from the funds collecting them to the debt service fund as debt service payments become due, and (3) use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

The City made two one-time transfers: (1) $3,500 from the water and sewer fund to the general fund to subsidize, in part, the City's share of the Hayley Valley Regional Fire Protection District's capital program and (2) the residual equity of $4,227 of the community development fund to the debt service fund.

Figure 57 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Fund Balance

Several disclosures regarding fund balance may appear in the notes, including the required detail below each fund balance category, stabilization arrangements and minimum fund balance policies, and policy for spending order.

Category details

As described previously, governments present their fund balance in five categories: nonspendable, restricted, committed, assigned, and unassigned. Accounting standards require that governments offer additional detail beneath each category:

- Nonspendable fund balance is distinguished between the portion not in a spendable form (such as inventory) and the portion required to be maintained intact (such as permanent fund principal), at a minimum. Some governments may identify specific items within those two groups, but they are not required to.
- Restricted fund balance is shown by the major purposes to which resources are devoted.
- Committed and assigned fund balance are shown in sufficient detail for the reader to identify the major commitments and assignments.

This detail does not have to be shown on the face of the balance sheet, however. A government may show as little as just the aggregate amounts for each category in the balance sheet, if it presents the required detail in a note disclosure.

Stabilization arrangements

It is common practice for governments to put aside resources to be used in a financial emergency. By turns called **RAINY-DAY FUNDS**, *stabilization funds, emergency funds, contingency funds,* and so on, these funds all are intended to provide needed monies should a government find itself facing unexpected financial problems.

These amounts may not always be evident on the face of the balance sheet. Rainy-day funds generally cannot be reported in a separate special revenue fund because they usually are not supplied by a specific revenue source. Rather, most rainy-day funds are stocked with surplus resources available at the end of the fiscal year. Furthermore, rainy-day resources usually cannot be reported as restricted or committed fund balance because the circumstances under which the resources can be used are not specific enough or, if they are specific, the circumstances occur routinely (and thus do not describe an emergency or "rainy day"). Consequently, rainy-day resources may be included within unassigned fund balance in the general fund because, in reality, those resources are available to be spent for any purpose, even if the government's intention is to hold onto them until an emergency arises.

Because it may be difficult, if not impossible, to identify rainy-day resources in the balance sheet when they do not qualify to be reported as restricted or committed fund balance, governments with such arrangements disclose them in the notes. Specifically, governments disclose:

- The authority for establishing STABILIZATION ARRANGEMENTS (for example, by statute or ordinance)
- The requirements for additions to the stabilization amount
- The conditions under which stabilization amounts may be spent, and
- The stabilization balance, if not apparent on the face of the financial statements.

A government also may have a MINIMUM FUND BALANCE POLICY that requires it to maintain a certain level of fund balance at the end of each fiscal year. For instance, a government may have adopted a policy to end each year with unassigned fund balance equal to at least 5 percent of total noncapital expenditures for the year. Such a policy effectively is the same thing as a rainy-day fund. If a government has a minimum fund balance policy, it describes the policy in the notes.

It should be pointed out that this disclosure requirement applies only to minimum fund balance policies adopted by a government itself. Some states require certain local governments and school districts to maintain a minimum level of fund balance. Such a situation might require disclosure of instances in which a local government did not comply with the state requirement, but it would not be disclosed as a minimum fund balance *policy*.

Spending order

If a government has resources from more than one fund balance category that it can spend on a particular purpose, it discloses in the SSAP its policy regarding which resources it would spend first. A similar disclosure requirement for restricted and unrestricted net position was described earlier. (See page 122.) Because these resources probably are held in the same bank account and, therefore, are indistinguishable from each other, the order-of-spending policy actually is an *assumption* about which resources are spent first. This is needed for determining which category of fund balance the remaining resources should be reported in.

What can you do with fund balance disclosures?

It is important to know not just that a certain amount of fund balance is restricted, committed, or assigned, but also the *purposes* for which the resources are constrained. If you wish to assess the potential that restricted or committed resources could become available for other purposes, it is essential to know what uses they currently are devoted to.

If you are interested in a government's ability to withstand unforeseen financial difficulties, information about the availability of rainy-day resources is important to have. How much money has been set aside? Under what circumstances can it be used? What is the outlook for the rainy-day amount growing or shrinking in the future?

The existence of stabilization arrangements and minimum fund balance policies are not only relevant to assessments of future fiscal health. They also may be considered by some to be an indication of the quality of financial management of a government. Many analysts view saving against a rainy day as a mark of prudent financial planning and control.

Detailed Reconciliations

The governmental funds financial statements contain reconciliations to the information in the government-wide financial statements. The balance sheet reconciliation explains why the amount of fund balance differs from the net position of the governmental activities. The reconciliation in the statement of revenues, expenditures, and changes in fund balances explains why the amount of net change in fund balances is different from the change in net position of governmental activities.

Because of the inherent space limitations of including the reconciliation on the statement itself, the various adjustments are categorized and aggregated. Aggregation combines individual adjustments within a broader category. Further, the use of succinct language may result in descriptions that are insufficiently specific. Consequently, you will find notes to these financial statements if they are necessary to clearly explain the differences between the governmental funds and governmental activities. (See Figures 58 and 59.) If a government presents its reconciliation on the page following the statement, it has more room for detail and, consequently, may not need to present this note.

Governments have leeway in deciding how to structure and present the detailed note regarding the reconciliations, as long as the note succeeds in adequately explaining the nature of the adjustments made in the reconciliations. Figures 58 and 59 present two possible formats for the notes. Figure 58 arranges the reconciliation of the balance sheet and the statement of net position in columns; it looks similar to the illustrative balance sheet in Figure 53. (Annotations have been added to the sample note in Figure 58 to help you understand how it works.) The format in Figure 59 essentially expands on the arrangement of the reconciliation in Figure 55 by looking more closely at how the individual changes in fund balance and net position (revenues, expenses/expenditures) differ, rather than contrasting the aggregate change.

What can you do with reconciliation disclosures?

The reconciliation is an extremely valuable tool for learning about the relationship—both quantitative and qualitative—between the government-wide and governmental funds financial statements and their respective accounting methods. It is informative both about differences in the scope of activities that each encompasses and about how the accounting assumptions of the two kinds of statements differ. For instance, in addition to the activities of the governmental funds, governmental activities also include the internal service fund activities. Due to space considerations, the reconciliations presented

in the notes can explain the differences much more fully than the reconciliations that accompany the statements.

Figure 58. Note Disclosure Reconciling the Governmental Funds Balance Sheet to the Government-Wide Statement of Net Position

Explanation of Differences between Governmental Funds Balance Sheet and the Statement of Net Position

"Total fund balances" of the City's governmental funds ($34,893,106) differs from "net position" of governmental activities ($123,558,874) reported in the statement of net position. This difference primarily results from the long-term economic focus of the statement of net position versus the current financial resources focus of the governmental fund balance sheet.

Balance Sheet/Statement of Net Position

①	Total Governmental Funds	② Long-Term Assets, Liabilities [a]	③ Internal Service Funds [b]	④ Reclassifications and Eliminations ⑤	⑥ Statement of Net Position Totals
ASSETS					
Cash and cash equivalents	$ 10,261,800	$ —	$ 3,336,099	$ —	$ 13,597,899
Investments	27,214,984	—	150,237	—	27,365,221
Receivables, net	6,972,560	—	326,864	3,818,611	11,118,035
Due from other funds	1,370,757	—	—	1,195,757	2,566,514
Due from other governments	1,715,097	—	—	—	1,715,097
Liens receivable	3,987,671	—	—	(3,987,671)	—
Inventories	182,821	—	139,328	—	322,149
Capital assets	—	161,082,708	8,940,052	—	170,022,760
Total assets	$ 51,705,690	$ 161,082,708	$ 12,892,580	$ 1,026,697	$ 226,707,675
DEFERRED OUTFLOWS OF RESOURCES					
Pensions	$ —	$ 8,365,521	$ —	$ —	$ 8,365,521
Retiree health insurance	—	6,686,417	—	—	6,686,417
Hedging derivatives	—	1,754,896	—	—	1,754,896
Total deferred outflows of resources	$ —	$ 16,806,834	$ —	$ —	$ 16,806,834
LIABILITIES					
Accounts payable	$ 5,908,666	$ 319,297	$ 780,570	$ 94,074	$ 7,102,607
Due to other funds	25,369	—	1,170,388	(1,195,757)	—
Due to other governments	94,074	—	—	(94,074)	—
Matured bonds and interest payable	—	—	—	—	—
Advances on grants	1,435,599	—	—	—	1,435,599
Long-term liabilities	—	185,056,759	7,777,871	—	192,834,630
Total liabilities	$ 7,463,708	$ 185,376,056	$ 9,728,829	$ (1,195,757)	$ 201,372,836
DEFERRED INFLOWS OF RESOURCES					
Unavailable revenue—taxes	$ 4,250,430	$ —	$ —	$ (4,250,430)	$ —
Unavailable revenue—grants	5,098,446	—	—	(5,098,446)	—
Pensions	—	3,903,910	—	—	3,903,910
Retiree health insurance	—	3,120,328	—	—	3,120,328
Total deferred inflows of resources	$ 9,348,876	$ 7,024,238	$ —	$ (9,348,876)	$ 7,024,238
FUND BALANCES/NET POSITION					
Net investment in capital assets	$ —	$ 95,020,640	$ 8,690,746	$ —	$ 103,711,386
Restricted	14,711,070	8,040,847	—	—	22,751,917
Unrestricted	20,182,036	(108,223,363)	(5,696,055)	—	(93,737,382)
Total fund balances/net position	$ 34,893,106	$ (5,161,876)	$ 2,994,691	$ —	$ 32,725,921

[a] The costs of building and acquiring capital assets (land, infrastructure, buildings, equipment) financed from the governmental funds are reported as expenditures in the year they are incurred, and the assets do not appear on the balance sheet. However, the statement of net position includes those capital assets among the assets of the City as a whole, and their original costs are expensed annually over their useful lives.

Original cost of capital assets	$ 199,336,115
Accumulated depreciation	(38,253,407)
	$ 161,082,708

Because the governmental funds focus on short-term financing, some assets will not be available to pay for current-period expenditures. Those assets (for example, receivables) are offset by a deferred inflow of resources in the governmental funds and, thus, are not included in fund balance. They are, however, included in the net position of the governmental activities.

Adjustment of deferred revenue	$ 9,348,876

Long-term liabilities are reported in the statement of net position but not in the governmental funds because they are not due and payable in the current period. Balances at December 31, 2017, were:

Bonds and notes payable	$ 82,139,924
Less deferred interest from refunding	(3,068,230)
Net pension liability	55,720,140
Net OPEB liability	44,576,112
Compensated absences	5,104,433
Litigation settlement—general fund	584,380
Subtotal, long-term liabilities	$ 185,056,759

[b] Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds of the government. The assets and liabilities of the internal service funds, which are reported in the proprietary funds rather than the governmental funds, are included in governmental activities in the statement of net position.

Figure 58 Notes

① The first column is taken almost as is from the right-hand total column of the balance sheet (Figure 53).

② Governmental funds do not contain capital assets or long-term liabilities, so they must be added in.

③ Internal service funds are proprietary, not governmental, and must be added in.

④ Reclassifications involve shifting activities from governmental funds to BTAs and from proprietary funds to governmental activities.

⑤ Eliminations are made to avoid double-counting of transfers and certain other financial activity among the funds.

⑥ This column is the governmental activities information found in the statement of net position (Figure 1).

Figure 59 Notes

① Comparison of Figures 54 and 42.

② Information from Figure 54.

③ Subtract the expenditures amount from the revenues to get the governmental funds change in fund balances of ($106,657).

④ See Figures 69 and 76 for more information about internal service funds.

⑤ Information from Figure 42.

⑥ The information on the left provides a proof for the adjustments in the column above—both add up to the total below.

⑦ Subtract the expenses amount from the revenues amount to get the statement of activities' change in net position of ($3,114,286).

Special Revenue Funds

The accounting standards allow governments to use special revenue funds to report specific revenue sources that are restricted or committed to being used for specified purposes. However, governments are not *required* to report special revenue funds. To help you understand why it is reporting special revenue funds, a government discloses the purpose of each major special revenue fund and identifies the revenue sources and other resources reported in them. (See Figure E-2.)

Property Taxes

If a government has a property tax, it discloses the details of its property tax calendar, such as when taxes are levied, when payments are due, when payments are considered overdue, and so on.

Figure 59. Note Disclosure Reconciling the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances to the Government-Wide Statement of Activities

Explanation of Differences between Governmental Fund Operating Statements and the Statement of Activities ①

Total revenues and other financing sources ($121,225,813) in the governmental funds differs from total governmental activities revenues and transfers ($102,692,727) in the statement of activities. The differences result primarily from the long-term economic focus of the statement of activities versus the current financial resources focus of the governmental funds. The main components of the difference are described below.

Total revenues, other financing sources, and special item of the governmental funds consist of: ②

Revenues	$ 97,482,467
Proceeds of long-term capital debt	19,590,416
Proceeds from sale of park land	3,476,488
Transfers in (net)	676,442
Total revenues and other sources—governmental funds ③	121,225,813

Because some property taxes ($566,189) will not be collected for several months after the City's fiscal year ends, they are not considered "available" revenues in the governmental funds. Similarly, certain license and permit revenues ($1,354,441) are not currently available at year-end and are not reported as revenue in the governmental funds. 1,920,630

The proceeds from the sale of land ($3,476,488) are reported as revenue (as a special item) in the governmental funds. However, the cost of the land sold ($823,000) is removed from the capital assets account in the statement of net position and is offset against the sale proceeds, resulting in a "gain on sale of land" in the statement of activities. Thus, the revenue reported in the governmental funds is greater than the gain in the statement of activities. (823,000)

Internal service funds are used by management to charge the costs of certain activities, such as insurance and telecommunications, to individual funds. The investment earnings ($134,733) of the internal service funds and the net interfund transfers (–$175,033) are reported with governmental activities. ④ (40,300)

Bond proceeds are reported as financing sources in governmental funds and thus contribute to the change in fund balances. In the government-wide statements, however, issuing debt increases long-term liabilities in the statement of net position and does not affect the statement of activities. Total proceeds were $19,590,416. (19,590,416)

Total revenues of governmental activities in the statement of activities consist of: ⑤

Charges for services	$ 15,720,525	⑥
Operating grants and contributions	5,176,310	
Capital grants and contributions	4,894,915	
General revenues, special items, and transfers	76,900,977	
Total revenues of governmental activities		⑦ $ 102,692,727

Total expenditures ($121,332,470) of the governmental funds differ from total expenses ($105,807,013) of governmental activities reported in the statement of activities. The difference is attributable primarily to the economic resources focus of governmental activities versus the current financial resources focus of governmental funds. The main components of the differences are described below. ③ $ 121,332,470

Some expenses reported in the statement of activities do not require the use of current financial resources ($437,684) and, therefore, are not reported as expenditures in governmental funds. 437,684

When the purchase or construction of capital assets is financed through the governmental funds, the resources expended for those assets are reported as expenditures in the years they are incurred. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital expenditures (capital outlay of $16,718,649 plus $718,508 included in current expenditures) exceeded depreciation ($2,679,128) in the current period. (12,513,141)

Internal service funds are "closed" by charging additional amounts to participating governmental activities to completely cover the internal service funds' costs for the year. (See the revenue adjustment [$40,300], above.)

Repayment of bond principal is reported as an expenditure in governmental funds. For the City as a whole, however, the principal payments reduce the liabilities in the statement of net position and do not result in an expense in the statement of activities. The City's bonded debt was reduced by principal payments made to bond holders ($3,450,000). (3,450,000)

Total expenses of governmental activities ⑦ $ 105,807,013

SUPPORTING INFORMATION RELATED TO THE GOVERNMENTAL FUNDS

The supporting information related to the governmental funds financial statements includes budgetary comparisons, combining statements of nonmajor funds and individual funds, and schedules of trends in fund balances and revenues and expenditures.

WHAT'S AHEAD?

- HOW DID A GOVERNMENT'S BUDGET CHANGE DURING THE YEAR?
- HOW DID BUDGETED REVENUES AND EXPENDITURES COMPARE WITH THE ACTUAL RESULTS FOR THE YEAR?

Budgets

A government prepares a budgetary comparison for the general fund and each major special revenue fund for which it legally adopts an annual budget. Accounting standards *encourage* governments to present their budgetary comparisons as RSI. However, a government has the option to present them as basic financial statements instead.

The left-hand side of the schedule lists categories of resource inflows (such as taxes and grants) and outflows (engineering services, for instance). (See Figures 60 and 61.) At a minimum, you will see three columns in the schedule: original budget, final budget, and actual amounts.

The amounts in the **ORIGINAL BUDGET** column come from the budget originally adopted for the year. The original budget numbers in this schedule also may reflect legally authorized adjustments a government made to its adopted budget subsequent to adoption but prior to the beginning of the fiscal year (such as reserves, transfers, allocations, and supplemental appropriations). If a government is required by law to carry over **APPROPRIATIONS** from one year to the next, these amounts also are included within the original budget numbers.

Budgets are revised over the course of a year to take into account *external factors* (such as differences between actual economic performance and the assumptions made in the adopted budget) and *changes in policy* (such as a decision to hire more police officers). The **FINAL BUDGET** reflects the sum of all legal adjustments made to the budget by a government since the start of the fiscal year. (Some changes may even have been made after the *end* of the year.)

Figure 60. Budgetary Comparison Schedule

Local City
Budgetary Comparison Schedule for the General Fund
for the Year Ended December 31, 2017

①	② Budgeted Amounts		Actual Amounts—	③ Variances—Positive (Negative)		Budget-	④ Actual Amounts—
	Original	Final	Budgetary Basis	Original to Final	Final to Actual	to-GAAP Reconciliation	GAAP Basis
REVENUES							
Property taxes	$ 52,017,833	$ 51,853,018	$ 51,173,436	$ (164,815)	$ (679,582)	$ —	$ 51,173,436
Other taxes—franchise and public service	12,841,209	12,836,024	13,025,392	(5,185)	189,368	—	13,025,392
Fees and fines	718,800	718,800	606,946	—	(111,854)	—	606,946
Licenses and permits	2,126,600	2,126,600	2,287,794	—	161,194	—	2,287,794
Intergovernmental	6,905,898	6,571,360	6,119,938	(334,538)	(451,422)	—	6,119,938
Charges for services	12,392,972	11,202,150	11,374,460	(1,190,822)	172,310	—	11,374,460
Interest	1,015,945	550,000	552,325	(465,945)	2,325	—	552,325
Miscellaneous	3,024,292	1,220,991	881,874	(1,803,301)	(339,117)	—	881,874
Total revenues	91,043,549	87,078,943	86,022,165	(3,964,606)	(1,056,778)	—	86,022,165
EXPENDITURES							
Current:							
General government (including contingencies and miscellaneous)	11,837,534	9,468,155	8,621,500	2,369,379	846,655	9,335	8,630,835
Public safety	33,050,966	33,983,706	33,799,709	(932,740)	183,997	(70,086)	33,729,623
Public works	5,215,630	5,025,848	4,993,187	189,782	32,661	(17,412)	4,975,775
Engineering services	1,296,275	1,296,990	1,296,990	(715)	—	2,655	1,299,645
Health and sanitation	5,756,250	6,174,653	6,174,653	(418,403)	—	(104,621)	6,070,032
Cemetery	724,500	724,500	706,305	—	18,195	—	706,305
Culture and recreation	11,059,140	11,368,070	11,289,146	(308,930)	78,924	122,539	11,411,685
Education—payment to school district	22,000,000	22,000,000	21,893,273	—	106,727	—	21,893,273
Total expenditures	90,940,295	90,041,922	88,774,763	898,373	1,267,159	(57,590)	88,717,173
Excess (deficiency) of revenues over expenditures	103,254	(2,962,979)	(2,752,598)	(3,066,233)	210,381	57,590	(2,695,008)
OTHER FINANCING SOURCES (USES)							
Transfers in	939,525	130,000	129,323	(809,525)	(677)	—	129,323
Transfers out	(2,970,256)	(2,163,759)	(2,163,759)	806,497	—	—	(2,163,759)
Total other financing sources and uses	(2,030,731)	(2,033,759)	(2,034,436)	(3,028)	(677)	—	(2,034,436)
SPECIAL ITEM							
Proceeds from sale of park land	1,355,250	3,500,000	3,476,488	2,144,750	(23,512)	—	3,476,488
Total other financing sources (uses) and special items							
Net change in fund balance	(572,227)	(1,496,738)	(1,310,546)	(924,511)	186,192	57,590	(1,252,956)
Fund balances—beginning	3,528,750	2,742,799	2,742,799	(785,951)	—	165,523	2,908,322
Fund balances—ending	$ 2,956,523	$ 1,246,061	$ 1,432,253	$ (1,710,462)	$ 186,192	$ 223,113	$ 1,655,366

Explanation of differences:

(1) The City budgets for claims and compensated absences only to the extent expected to be paid, rather than on the modified accrual basis. ⑤ ⑥ $ (129,100)

Encumbrances for goods and services ordered but not received are reported as expenditures in the year the orders are placed for budgetary purposes but are reported in the year the goods and services are received for GAAP purposes. 186,690

Net increase in fund balance—budget to GAAP $ 57,590 ⑦

(2) The amount reported as "fund balance" on the budgetary basis of accounting derives from the basis of accounting used in preparing the City's budget. (See the financial statement notes for a description of the City's budgetary accounting method.) This amount differs from the fund balance reported in the statement of revenues, expenditures, and changes in fund balances because of the cumulative effect of transactions such as those described above.

Figure 60 Notes

① Local City presents its schedule using the format, terminology, and classifications of the statement of revenues, expenditures, and changes in fund balances. Alternatively, a government may use those of its own budget document.

② Budgeted amounts include the originally adopted budget (including legal adjustments made prior to the start of the year) and the final budget (with all changes made to the budget subsequent to the start of the year).

③ Some governments refer to this as *favorable (unfavorable)*.

④ This is the reconciliation of the government's budgetary basis with the modified accrual basis of the general fund. Adjustments appear in the column below and explanations are at the bottom of the schedule.

⑤ Variance columns are encouraged but not required; governments may include one, both, or neither.

⑥ If expenditures exceeded *appropriations* in any individual fund, a government should disclose it in a note to the schedule.

⑦ Governments have some leeway to decide how best to present the reconciliation, just as they do for the reconciliations in the governmental funds statements. Figure 62 contains a fairly detailed reconciliation that would be presented on the page following the comparison schedule. Some governments present a more succinct reconciliation than that, while others like Local City place the reconciling adjustments in columns on the face of the schedule.

Figure 61. Budgetary Comparison Schedule for a Major Special Revenue Fund

Local City
① **Budgetary Comparison Schedule for the HUD Programs Fund** ②
for the Year Ended December 31, 2017

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note A) ③	Variance with Final Budget—Positive (Negative) ④
	Original	Final		
Budgetary fund balances, January 1	$ 1,600,000	$ 1,618,441	$ 1,618,441	$ —
Resources (inflows):				
Federal grants	2,000,000	2,000,000	1,963,526	(36,474)
State grants	—	600,000	614,665	14,665
Interest on investments	85,000	85,000	87,106	2,106
Miscellaneous	50,000	50,000	66,176	16,176
Amounts available for appropriation	3,735,000	4,353,441	4,349,914	(3,527)
Charges to appropriations (outflows):				
Community development:				
Ombudsman office	1,725,000	1,725,000	1,687,422	37,578
Weatherization program	700,000	1,300,000	1,279,104	20,896
Transfers to other funds	350,000	350,000	348,046	1,954
Total	2,775,000	3,375,000	3,314,572	60,428
Budgetary fund balances, December 31	$ 960,000	$ 978,441	$ 1,035,342	$ 56,901

⑤

Figure 61 Notes

① A government will prepare a budgetary comparison for its main operating fund (usually the general fund) and every major special revenue fund for which it has a legally adopted budget.

② A government has the option to present this as a part of the basic financial statements instead of a schedule in RSI.

③ The government's explanation of the difference between the numbers shown here and those in the governmental funds balance sheet is contained in the note illustrated in Figure 62.

④ Variance columns are encouraged but not required: a government may include an original-to-final and/or a final-to-actual column, or neither.

⑤ See Figures 60 and 62 for other options a government has for presenting the reconciliation of the budgetary basis to GAAP.

The third column contains the amounts that *actually* flowed in and out during the year (as opposed to the budget numbers, which are estimates or predictions). The amounts are stated on the same basis as the budget figures. (This basis often is *cash* inflows and outflows.)

Figure 60: Actual property tax revenues were $844,397 less than originally budgeted [original-to-final variance of ($164,815) plus final-to-actual variance of ($679,582)].

The variance columns shown in Figures 60 and 61 are encouraged but not required. A government may include them, and many do, but if it does not, they can be created with some simple math. To obtain original-budget-to-final-budget variances, subtract the original budget amounts from the final budget amounts. To obtain final-budget-to-actual variances, subtract the final budget amounts from the amounts in the actual column.

When *actual inflow amounts fall below budgeted inflows,* the number in the variance column is shown in parentheses; the same is true when *actual outflows exceed budgeted outflows.* It works the same way for the column comparing the final and original budgets. If final budget revenues are lower than the original budget or if expenditures are higher, the variances are placed in parentheses.

Variance figures in parentheses are sometimes called *negative* variances or *unfavorable* variances. They are not necessarily negative in the sense that they are *bad* but, rather, that they indicate an adverse impact on the bottom line—the difference between inflows and outflows. Higher-than-expected spending and lower-than-expected revenues can lead to a deficit. However, the extra spending might have been the result of meeting additional, unexpected needs, which could be considered a good thing to do.

By the same token, *positive* or *favorable* variances (actual revenues higher than budgeted or actual expenditures lower than budgeted) are not necessarily desirable. For instance, lower-than-expected spending could be the result of not delivering necessary services. *The variance column is most valuable as a*

red flag to potential problems; variances should be investigated further for explanation. The discussion in MD&A of significant budget variances may be your starting point for this line of inquiry.

The budgetary comparison schedule also reconciles the actual budget results to the amounts in the governmental funds statement of revenues, expenditures, and changes in fund balances. If the numbers in the budgetary comparison and the governmental funds statement differ, it is mainly because the governmental funds financial statements are prepared following GAAP, while most governments do not use those accounting principles as their basis for budgeting. Many governments budget on a cash or near-cash basis, or include ENCUMBRANCES and other items that would not be

Figure 62. Budgetary Comparison Reconciliation

Note A: Explanation of Differences between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures

①	General Fund	HUD Programs Fund
Sources/inflows of resources		
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule	$ 92,370,775	$ 4,349,914
Differences—budget to GAAP:		
The fund balance at the beginning of the year is a budgetary resource but is not a current-year revenue for financial reporting purposes.	(2,742,799)	(1,618,441)
Transfers from other funds are inflows of budgetary resources but are not *revenues* for financial reporting purposes.	(129,323)	—
The proceeds from the sale of the park land are budgetary resources but are regarded as a *special item,* rather than revenue, for financial reporting purposes.	(3,476,488)	—
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances—governmental funds.	$ 86,022,165	$ 2,731,473
Uses/outflows of resources		
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule.	$ 90,938,522	$ 3,314,572
Differences—budget to GAAP:		
The City budgets for claims and compensated absences only to the extent expected to be paid, rather than on the modified accrual basis.	129,100	3,900
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but are reported in the year the supplies are received for financial reporting purposes.	(186,690)	(16,037)
Transfers to other funds are outflows of budgetary resources but are not *expenditures* for financial reporting purposes.	(2,163,759)	(348,046)
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances—governmental funds	$ 88,717,173	$ 2,954,389

Figure 62 Note

① If the budgetary comparisons were presented as basic financial statements instead of RSI, this reconciliation would be either a schedule to a basic financial statement or a note to financial statements.

considered revenues or expenditures in the financial statement. A government has some leeway to decide how best to present the reconciliation. Figure 62 shows a fairly detailed reconciliation that would be presented on the page following the budgetary comparison schedule. Some governments present a more succinct reconciliation than that, while others place the reconciling adjustments in columns on the schedule itself (as in Figure 60).

What can you do with budgetary comparison information?

The budgetary comparison schedule is a vital tool for achieving an important goal of financial reporting—*judging a government's compliance with its budget*. But, as just mentioned, it is only a first step in that process. It can be likened to a radar system—it identifies potential "situations" but nonetheless requires that you look for yourself to determine how much of a problem the situation may be, if a problem at all. The column showing variances between the actual and final budget amounts is your radar. The explanations of budget variances in MD&A should help you to *understand what caused the budget variances* you observe in this schedule, although you still may want to delve deeper.

There almost always are variances between the original and final budgets. Governments rarely are exactly on the mark when predicting inflow and outflow amounts before a fiscal year begins. There are many underlying assumptions involved in budgeting and thus many opportunities for actual experience to differ from expectations. Taking into account what you have learned from MD&A about changes in the economy and a government's policies, the variance between the original and final budgets may give you a sense of *the government's capacity to budget accurately* in the first place and *its ability to enforce the budget and control finances* during the course of the year. Variances identified in the schedule could be investigated further to determine their causes—perhaps faulty estimates, policy changes, or unforeseen economic shifts.

The budget-to-GAAP reconciliation (especially the more detailed version in Figure 62) could be very valuable to legislative staff, agency officials, advocacy organizations, or anyone who deals primarily with budget numbers. The reconciliation may help you connect recent and current budget figures to the 10-year trends you can find in the statistical section. (See Figure 66.)

Funds

As noted earlier, major governmental funds are shown individually and nonmajor governmental funds are aggregated into a single column in the governmental funds financial statements. If a government prepares a CAFR, the financial section will include (as SI) combining statements and possibly individual fund statements that offer more detail about the information aggregated in the fund financial statements.

Nonmajor funds

Combining statements are presented for the nonmajor governmental funds, showing them individually in their own columns and typically organized by fund type—special revenue, debt service, capital projects, and permanent. For each governmental fund type, the following combining statements are prepared:

- Combining balance sheet (Figure 63)
- Combining statement of revenues, expenditures, and changes in fund balances (Figure 64).

Individual Funds

Financial statements for single funds basically are the same as the combining statements, with the exception that they show only one fund and may show greater detail than fund statements. A government may use individual fund statements in order to demonstrate its compliance with a finance-related legal or contractual provision. If a fund reports activities for which long-term debt has been issued, the bond covenants governing that borrowing may require that individual financial information for that fund be prepared. If this legal requirement is not met through major fund reporting, the government could present individual statements for that fund instead.

Another use of individual fund statements is to make comparisons between the current and prior years. If it wanted to do so, a government could prepare a complete set of financial statements for that fund for the current year and a separate set for the prior year. Alternatively, a government could prepare a single set of comparative financial statements that included the information for both years in separate columns.

What can you do with this information?

The inclusion of combining and individual fund statements in the CAFR complements the information reported in the basic financial statements. A fund may not be considered major in accounting terminology, but it may be very important to *your* interests. Although a government has the ability to report a fund as major even if it does not meet the numerical requirements, it may not be feasible to do so for many funds that otherwise would be nonmajor without cluttering the financial statements. If you are interested in the financial activity related to a specific fund that is not reported

in its own column in the basic financial statements, and the government prepares a CAFR or chooses to present combining and individual fund statements, you will be able to find the information you need.

Figure 63. Combining Balance Sheet, Nonmajor Governmental Funds

Local City
Combining Balance Sheet for Nonmajor Governmental Funds
As of December 31, 2017

① ②

	Special Revenue Funds				Debt Service Funds			Capital Projects Fund	Permanent Fund	Total Nonmajor Governmental Funds
	Parks	Tax Surcharge	Historic District	Total	Central City Development	Community Redevelopment	Total	Bridge	Cemetery Care	
ASSETS										
Cash and cash equivalents	$ 371,413	$1,999,819	$ 189,880	$ 2,561,112	$ 677,143	$ 164,861	$ 842,004	$1,141,648	$1,062,028	$ 5,606,792
Investments	—	—	—	—	941,510	2,200,470	3,141,980	—	343,272	3,485,252
Receivables, net	—	10,221	—	10,221	—	—	—	—	—	10,221
Receivable from other governments	—	129,883	4,836	134,719	—	—	—	1,461,319	—	1,596,038
Total assets	$ 371,413	$2,139,923	$ 194,716	$ 2,706,052	$ 1,618,653	$ 2,365,331	$ 3,983,984	$2,602,967	$1,405,300	$ 10,698,303
LIABILITIES AND FUND BALANCES										
Liabilities:										
Accounts payable	$ 61,165	$ 170,615	$ 4,836	$ 236,616	$ 151,922	$ —	$ 151,922	$ 686,293	$ —	$ 1,074,831
Total liabilities	61,165	170,615	4,836	236,616	151,922	—	151,922	686,293	—	1,074,831
Fund balances:										
Nonspendable	—	—	—	—	—	—	—	—	1,405,300	1,405,300
Restricted for:										
Capital projects	—	—	—	—	—	—	—	675,404	—	675,404
Debt service	—	—	—	—	1,466,731	2,365,331	3,832,062	—	—	3,832,062
Committed to:										
Playground equipment	176,487	—	—	176,487	—	—	—	—	—	176,487
Recreation programs	—	962,231	—	962,231	—	—	—	—	—	962,231
Assigned to:										
Capital projects	—	—	—	—	—	—	—	1,241,270	—	1,241,270
Recreation programs	—	1,007,077	—	1,007,077	—	—	—	—	—	1,007,077
Other purposes	133,761	—	189,880	323,641	—	—	—	—	—	323,641
Total fund balances	310,248	1,969,308	189,880	2,469,436	1,466,731	2,365,331	3,832,062	1,916,674	1,405,300	9,623,472
Total liabilities and fund balances	$ 371,413	$2,139,923	$ 194,716	$ 2,706,052	$ 1,618,653	$ 2,365,331	$ 3,983,984	$2,602,967	$1,405,300	$ 10,698,303

Figure 64. Combining Statement of Revenues, Expenditures, and Changes in Fund Balances, Nonmajor Governmental Funds

Local City
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances
Nonmajor Governmental Funds
for the Year Ended December 31, 2017

① ②

	Special Revenue Funds				Debt Service Funds			Capital Projects Fund	Permanent Fund	Total Nonmajor Governmental Funds
	Parks	Tax Surcharge	Historic District	Total	Central City Development	Community Redevelopment	Total	Bridge	Cemetery Care	
REVENUES										
Property taxes	$ —	$ —	$ —	$ —	$ 4,680,192	$ —	$ 4,680,192	$ —	$ —	$ 4,680,192
Intergovernmental	—	1,312,670	60,426	1,373,096	—	—	—	1,457,820	—	2,830,916
Charges for services	30,708	—	—	30,708	—	—	—	—	—	30,708
Investment earnings	4,543	123,329	226	128,098	103,631	42,973	146,604	16,939	72,689	364,330
Miscellaneous	—	94	—	94	—	—	—	—	—	94
Total revenues	35,251	1,436,093	60,652	1,531,996	4,783,823	42,973	4,826,796	1,474,759	72,689	7,906,240
EXPENDITURES										
Current:										
General government	50,000	3,622	—	53,622	8,920	2,900	11,820	55,610	—	121,052
Public works	705,487	2,968,283	47,772	3,721,542	—	—	—	—	—	3,721,542
Debt service:										
Principal	—	—	—	—	2,910,000	540,000	3,450,000	—	—	3,450,000
Interest and other charges	—	—	—	—	3,885,191	1,329,960	5,215,151	—	—	5,215,151
Capital outlay	—	—	—	—	—	—	—	3,190,209	—	3,190,209
Total expenditures	755,487	2,971,905	47,772	3,775,164	6,804,111	1,872,860	8,676,971	3,245,819	—	15,697,954
Excess (deficiency) of revenues over expenditures	(720,236)	(1,535,812)	12,880	(2,243,168)	(2,020,288)	(1,829,887)	(3,850,175)	(1,771,060)	72,689	(7,791,714)
OTHER FINANCING SOURCES (USES)										
Proceeds of long-term debt	—	—	—	—	760,856	—	38,045,000	1,300,000	—	39,345,000
Transfers in	—	—	177,000	177,000	1,604,149	2,387,149	3,991,298	1,382,889	—	5,551,187
Transfers out	—	(42,500)	—	(42,500)	—	—	—	(113,167)	(63,409)	(219,076)
Total other financing sources and uses	—	(42,500)	177,000	134,500	2,365,005	2,387,149	4,752,154	2,569,722	(63,409)	7,392,967
Net change in fund balances	(720,236)	(1,578,312)	189,880	(2,108,668)	344,717	557,262	901,979	798,662	9,280	(398,747)
Fund balances—beginning	1,030,484	3,547,620	—	4,578,104	1,122,014	1,808,069	2,930,083	1,118,012	1,396,020	10,022,219
Fund balances—ending	$ 310,248	$ 1,969,308	$ 189,880	$ 2,469,436	$ 1,466,731	$ 2,365,331	$ 3,832,062	$ 1,916,674	$ 1,405,300	$ 9,623,472

Figures 63 and 64 Notes

① These illustrations show all nonmajor governmental funds in a single statement but grouped (including subtotals) by fund type. A government may opt instead for separate combining statements for each fund type if it has numerous nonmajor funds.

② The totals in this column feed into the nonmajor funds column in the balance sheet (Figure 53) and the statement of revenues, expenditures, and changes in fund balances (Figure 54).

Trends in Fund Balances

If a government reports governmental funds in its basic financial statements, its statistical section includes an SI schedule of fund balances for the last 10 years. (See Figure 65.) The schedule reports the five categories of fund balance for the general fund and for the sum of the other governmental funds. These trends can be examined to determine whether available resources have grown over time or diminished. The mix between categories also can be analyzed. Are more of the resources generally available for any purpose (unassigned) or only for specific uses?

Trends in Revenues and Expenditures

If a government reports governmental funds in its financial statements, it also presents a statistical section schedule with revenues, expenditures, and other changes in fund balances for the past 10 fiscal years. (See Figure 66.) At a minimum, a government presents the following information for *total governmental funds* at the same level of detail you find in the statement of revenues, expenditures, and changes in fund balances:

- Revenues by source
- Expenditures by function
- Other financing sources, other financing uses, and other changes in fund balance by type, and
- Total change in fund balances.

Figure 66: The City of Statistical had a negative net change in fund balance (a decrease) in 20X0–20X2 and 20X6.

A government may provide more detail for any of this information than it presents in the financial statement, either in this schedule or in a separate schedule. For example, a government might aggregate tax revenues in the statement and in this schedule but also present a separate SI schedule with more specific information about individual taxes. (See Figure 67.) A government also presents debt service expenditures in separate principal and interest components and calculates a ratio of debt service divided by noncapital expenditures. (Refer to page 142 in Part Six.)

What can you do with this trend information?

A comprehensive review of a government's finances should consider both its long-term prospects and its short-term outlook. After all, if it does not make it through the short term, a government has no long run. This information is amenable to the same analyses as the schedule of trends in government-wide revenues and expenses (Figure 47)—such as percentage change and percentage distribution—but the story to be told is the *short-run* financial experience of the government. You also can compare revenues and expenditures over time to ascertain whether the government is covering its outflows from year to year or using resources accumulated in the past or pushing payments off to the future.

Figure 65. Statistical Section Schedule of Fund Balances

City of Statistical ①
Fund Balances, Governmental Funds
Last 10 Fiscal Years
(modified accrual basis of accounting)

	Fiscal Year									
	20X0	20X1	20X2	20X3	20X4 [a]	20X5	20X6	20X7	20X8	20X9
General fund										
Reserved	$ 6,722,872	$ 6,797,299	$ 7,549,349	$ 7,162,493						
Unreserved	39,546,951	34,566,111	31,125,648	30,000,154						
Nonspendable					$ 1,112,323	$ 1,115,864	$ 1,176,583	$ 1,240,606	$ 1,308,113	$ 1,236,933
Restricted					2,458,952	2,466,780	2,601,009	5,344,261	5,377,624	2,111,898
Committed					956,241	959,285	1,011,484	1,066,524	1,124,558	1,063,366
Assigned					3,424,886	3,435,789	3,622,746	3,819,875	4,027,732	3,808,565
Unassigned					31,526,911	31,269,874	28,113,555	30,030,046	30,220,537	31,605,673
Total general fund	$ 46,269,823	$ 41,363,410	$ 38,674,997	$ 37,162,647	$ 39,479,313	$ 39,247,592	$ 36,525,377	$ 41,501,312	$ 42,058,564	$ 39,826,435
All other governmental funds										
Reserved	$ 18,989,132	$ 20,377,901	$ 19,953,298	$ 22,400,477						
Unreserved, reported in:										
Special revenue funds	8,323,089	8,060,677	7,958,184	8,018,536						
Capital projects funds	3,851,886	3,781,238	2,963,047	3,402,455						
Debt service funds	4,287,652	4,152,470	4,099,671	4,130,761						
Nonspendable					$ 2,358,974	$ 2,378,463	$ 2,385,190	$ 2,726,275	$ 3,168,375	$ 3,052,737
Restricted					18,745,214	18,900,078	18,953,532	21,663,915	25,176,993	24,258,094
Committed					11,623,985	11,720,017	11,753,164	13,433,884	15,612,358	15,042,545
Assigned					7,461,221	7,522,862	7,544,138	8,622,961	10,021,284	9,655,531
Total all other governmental funds	$ 35,451,759	$ 36,372,286	$ 34,974,200	$ 37,952,229	$ 40,189,394	$ 40,521,420	$ 40,636,024	$ 46,447,035	$ 53,979,010	$ 52,008,907

[a] Beginning in 20X4, the City began reporting fund balance in accordance with GASB Statement 54, which changed how fund balance is classified.

Figures 65 and 66 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Figure 66. Statistical Section Schedule of Changes in Fund Balances

City of Statistical ①
Changes in Fund Balances, Governmental Funds
Last 10 Fiscal Years
(modified accrual basis of accounting)

	Fiscal Year									
	20X0	**20X1**	**20X2**	**20X3**	**20X4**	**20X5**	**20X6**	**20X7**	**20X8**	**20X9**
Revenues										
Taxes	$ 26,267,700	$ 26,495,252	$ 26,284,710	$ 28,954,785	$ 29,977,720	$ 30,442,344	$ 32,617,140	$ 39,650,001	$ 43,743,092	$ 49,435,320
Licenses, fees, and permits	3,532,841	3,008,722	4,410,897	7,673,948	9,813,411	11,202,863	9,454,323	13,385,329	9,884,567	11,224,714
Fines and penalties	326,598	308,157	351,353	374,252	392,650	436,051	488,500	860,126	1,562,990	1,105,048
Charges for services	6,151,778	5,387,557	5,872,279	7,462,332	7,991,102	7,343,190	8,962,504	10,806,778	11,187,411	11,634,689
Special assessments	11,365,205	10,188,591	8,515,168	8,764,388	8,811,251	8,377,823	8,382,471	8,787,785	9,175,512	8,488,067
Intergovernmental	15,540,752	13,495,919	12,742,002	9,505,719	12,193,773	11,270,410	11,780,262	13,395,868	18,182,327	17,242,467
Investment earnings	11,986,002	8,980,865	9,028,427	7,899,789	9,695,941	12,056,372	9,512,799	10,040,487	6,654,778	10,604,860
Other revenues	6,460,513	3,400,996	3,626,147	8,735,815	12,322,491	14,576,981	12,510,453	14,620,720	15,986,776	15,163,499
Total revenues	81,631,389	71,266,059	70,830,983	79,371,028	91,198,339	95,706,034	93,708,452	111,547,094	116,377,453	124,898,664
Expenditures										
General government	8,247,588	7,528,601	6,815,338	7,293,992	7,714,023	8,459,006	9,405,687	11,049,809	10,988,887	12,547,645
Police [a]	13,597,361	13,129,512	12,526,731	13,529,493	15,174,847	16,272,905	16,790,906	18,142,355	19,790,239	22,639,931
Fire	8,456,568	8,165,601	7,790,715	8,414,359	9,437,650	10,120,563	10,442,721	11,283,224	12,308,088	11,692,537
Refuse collection	4,080,124	4,142,258	4,205,338	4,269,379	4,334,395	4,400,401	4,467,412	4,535,443	4,604,511	4,823,462
Other public works	13,480,900	9,168,715	6,153,569	12,359,844	9,730,625	9,428,474	8,936,241	9,089,559	8,212,694	8,516,466
Parks and recreation	3,851,886	3,781,238	2,963,047	3,402,454	3,616,722	4,268,916	4,256,346	4,672,020	7,586,387	11,132,786

Capital outlay	38,793,881	35,122,208	61,112,259	22,270,493	29,804,719	20,728,911	26,558,157	30,478,506	30,328,142	33,820,224
Debt service										
Interest	11,053,542	13,502,322	14,300,337	11,350,341	10,191,242	11,389,970	10,826,408	11,552,128	12,239,270	14,360,876
Principal	5,983,565	7,309,153	7,741,138	6,144,230	5,516,780	6,165,683	5,860,611	6,561,088	6,374,046	6,956,210
Total expenditures	108,924,775	103,114,216	124,738,686	90,287,584	96,850,398	92,723,649	99,191,262	109,112,282	114,594,150	128,814,024
Excess of revenues over (under) expenditures	(27,293,386)	(31,848,157)	(53,907,703)	(10,916,556)	(5,652,059)	2,982,385	(5,482,810)	2,434,812	1,783,303	(3,915,360)
Other Financing Sources (Uses)										
Proceeds from borrowing	—	—	47,050,000	—	9,345,000	—	—	—	—	7,915,000
Proceeds from refunding	—	—	—	—	—	—	—	33,000,000	—	15,625,000
Payments to escrow agent								(33,000,000)		(15,625,000)
Transfers in	30,456,987	31,848,016	7,113,443	21,802,896	10,767,445	6,254,973	8,999,786	14,810,024	13,132,580	7,670,544
Transfers out	(7,458,618)	(3,985,746)	(4,342,239)	(9,420,661)	(9,906,555)	(9,137,053)	(6,124,587)	(6,457,890)	(6,826,657)	(5,766,396)
Total other financing sources (uses)	22,998,369	27,862,270	49,821,204	12,382,235	10,205,890	(2,882,080)	2,875,199	8,352,134	6,305,923	9,819,148
Net change in fund balances	$ (4,295,017)	$ (3,985,887)	$ (4,086,499)	$ 1,465,679	$ 4,553,831	$ 100,305	$ (2,607,611)	$ 10,786,946	$ 8,089,226	$ 5,903,788
Debt service as a percentage of noncapital expenditures	24.3%	30.6%	34.6%	25.7%	23.4%	24.4%	23.0%	23.0%	22.1%	22.4%

[a] Starting in 20X7, the City implemented a program to hire 50 additional police officers over 3 years to fill community policing positions.

Figure 67. Statistical Section Schedule of Detailed Tax Revenues

City of Statistical
① Tax Revenues by Source, Governmental Funds ②
Last 10 Fiscal Years
(modified accrual basis of accounting)

Fiscal Year	Property [a]	Sales and Use [b]	Occupancy	Franchise	Property Transfer	Other	Total
20X0	$ 15,995,182	$ 8,781,849	$ 327,593	$ 723,490	$ 225,826	$ 213,760	$ 26,267,700
20X1	16,105,883	8,758,174	304,454	780,474	201,637	344,630	26,495,252
20X2	15,138,090	9,713,005	279,320	755,944	224,205	174,146	26,284,710
20X3	16,437,018	11,000,767	331,103	842,422	252,089	91,386	28,954,785
20X4	16,242,615	12,100,400	349,578	894,130	304,647	86,350	29,977,720
20X5	15,880,677	12,746,984	383,534	954,799	372,934	103,416	30,442,344
20X6	15,905,680	14,286,678	468,626	1,366,863	476,515	112,778	32,617,140
20X7	18,641,088	18,230,041	584,248	1,542,614	545,644	106,366	39,650,001
20X8	21,345,165	19,271,523	717,374	1,635,455	657,544	116,031	43,743,092
20X9	24,153,481	21,856,323	816,813	1,870,141	627,824	110,738	49,435,320
Change							
20X0–20X9	51.0%	148.9%	149.3%	158.5%	178.0%	(48.2)%	88.2%

Notes: ③

[a] The City was able to keep its property tax rates fairly stable during the last three years of this schedule because of substantial growth in property values (see Schedule 5). The City also has received more resources because of improvements in collection rates (see Schedule 8).

[b] Sales and use tax revenues increased 149 percent in the past 10 years due to a combination of rate increases (see Schedule 6A), growth in taxable retail sales (see Schedule 5A), and several legislative measures to broaden the sales tax base.

Figure 67 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② This is not a required schedule. It is an example of how a government might report aggregated amounts in one schedule but provide more detail in another. (See Figure 66.) A government can use a variety of formatting approaches as long as it presents the required information in the schedules.

③ These notes connect the information in this schedule with that in the other statistical section schedules.

MAJOR FUNDS are funds that exceed specific size criteria or that a government considers important to report

NONSPENDABLE FUND BALANCE comprises resources that cannot be spent

RESTRICTED FUND BALANCE is resources legally constrained by organizations or persons external to a government

COMMITTED FUND BALANCE is resources legally constrained by a government itself using its highest level of decision-making authority

ASSIGNED FUND BALANCE represents resources a government intends to use for a particular purpose

UNASSIGNED FUND BALANCE is available for any purpose

OTHER FINANCING SOURCES are inflows of current financial resources other than revenues

OTHER FINANCING USES are outflows of current financial resources other than expenditures

EXPENDITURES are outflows of cash or a promise to pay when goods or services are received and payment is normally due

By the numbers…reclassified short-term debt

Under certain circumstances, if a government has decided after the end of the fiscal year (but before the financial report is issued) to refinance BANs, TANs, or RANs by issuing long-term debt to repay them, it may report them as noncurrent (long-term) liabilities instead of current liabilities (those expected to be paid off within a year). Consequently, such debt would not appear in the governmental funds balance sheet, which reports only current financial resources. A government discloses such circumstances in the notes to financial statements.

By the numbers…reserved and unreserved

Fund balance was not always reported in these five categories. Prior to June 30, 2011, governments were required to report their fund balance as either *reserved* or *unreserved.* Reserved fund balance represented resources that were legally limited to a purpose more specific than the purpose of the fund they were reported in, and unreserved fund balance equaled the resources available for any purpose *of the fund in which it was reported.* Frequently, however, unreserved was mistakenly interpreted to mean available for *any* purpose. For example, unreserved fund balance in a capital projects fund was available for any capital projects, but not available for purposes other than capital projects. The five fund balance categories were intended to be more intuitive by applying to constrained resources regardless of what fund they are reported in and to result in more comparable reporting among governments.

Some governments also divided unreserved fund balance between *designated* and *undesignated*. Designated unreserved fund balance represented resources that a government *intended* to use for a particular purpose, similar to assigned fund balance. However, whereas the current accounting standards identify how a government expresses intent that results in assigned fund balance and *require* that it be reported when present, the actions necessary to establish designations previously were not identified and reporting designations was *optional*.

PART TEN

PROPRIETARY AND FIDUCIARY FUNDS

Proprietary funds report the activities for which a government charges a fee to the users or direct beneficiaries of the service. That fee usually is set high enough to cover most or all of the costs of providing the service, though this is not universally true. (See **Upon further review…mass transit** on page 161 for a common example of an exception to this rule.) There are two kinds of proprietary funds. *Enterprise funds* account for activities (perhaps water and sewer service) directed toward those outside the government structure. *Internal service funds* normally record the services provided to other parts of a government; examples in some governments include central automobile pools and personnel administration.

A government's fiduciary funds account for the activities in which it acts solely as a *fiduciary* for someone else. In other words, a government is acting as the trustee or agent for resources it does not own. The principal example of such an arrangement is an employee pension plan. A government may be responsible for providing resources to the plan, possibly for investing and maintaining those resources, and actually may operate the benefits distribution aspect of the plan, but the resources in the plan are not available to the government. This is the reason fiduciary activities are not included in the government-wide financial statements; to include resources that do not belong to the government could be misleading if you are trying to determine a government's financial standing. Another example of a fiduciary relationship might be a state that collects sales taxes imposed by county and local governments within its jurisdiction on behalf of those governments. The collection of the taxes and subsequent distribution to the governments would be accounted for in an agency fund, but at no time would any of those resources be legally available to the state government except its own portion of the tax (which is accounted for in the *governmental* funds).

PROPRIETARY FUNDS FINANCIAL STATEMENTS

The proprietary funds statements are the:

- Statement of net position (Figures 68, B-7, and C-6)
- Statement of revenues, expenses, and changes in fund net position (Figures 69, B-8, and C-7)—some governments use the title "changes in fund equity" instead—and
- Statement of cash flows (Figures 70, B-9, and C-8).

Figure 68: Accounts payable for the parking facilities were $304,003.

The first two statements use the same accounting methods as the government-wide financial statements—economic resources measurement focus and accrual basis of accounting—and serve

basically the same purposes. The proprietary funds financial statements typically provide greater detail than is available for BTAs in the government-wide statements. Furthermore, changes in the net position of BTAs are presented in a more traditional operating statement format in the fund statements. (Some of the other unique features of proprietary funds statements are explained in the notes to Figures 68–70.)

Figure 69: Charges for services for the internal service funds were $15,256,164.

By the numbers…types of proprietary funds

	Fund Types	**Examples**
Proprietary Funds report activities generally financed by charging a fee to customers.	*Enterprise funds* may be used to account for *any* activity that charges a fee to users; they are *required* to be used for any activity that does one or more of the following: • Is financed with debt that is repaid only with the activity's own user revenues • Is legally required to cover its costs (including depreciation or debt service) with fees and charges rather than taxes and similar revenues • Sets its fees and charges in order to recover all of its operating and capital costs (including depreciation or debt service).	A county has a public utility to provide electricity to residents and businesses.
	Internal service funds report activities that provide goods or services to other funds of the government, or to other governments, in return for a fee to reimburse costs.	A municipal garage fuels and services a city's fleet of road maintenance vehicles, garbage trucks, and patrol cars.

Figure 68. Proprietary Funds Statement of Net Position

Local City
Statement of Net Position
Proprietary Funds
As of December 31, 2017

	① Business-Type Activities—Enterprise Funds			② Governmental Activities—Internal Service Funds (See Note H.)
	Water and Sewer	Parking Facilities	Total	
ASSETS				③
Current assets:				
Cash and cash equivalents	$ 8,416,653	$ 1,804,767	$10,221,420	$ 3,336,099
Investments	47,596,245	—	47,596,245	150,237
Receivables, net	3,564,586	3,535	3,568,121	157,804
Due from other governments	41,494	—	41,494	—
Inventories	126,674	—	126,674	139,328
Total current assets	59,745,652	1,808,302	61,553,954	3,783,468
Noncurrent assets:				
Restricted cash and cash equivalents ④	—	1,493,322	1,493,322	—
Capital assets:				
Land	813,513	3,021,637	3,835,150	—
Distribution and collection systems	39,504,183	—	39,504,183	—
Buildings and equipment	106,135,666	23,029,166	129,164,832	⑤ 14,721,786
Less accumulated depreciation	(15,328,911)	(5,786,503)	(21,115,414)	(5,781,734)
Total capital assets	131,124,451	20,264,300	151,388,751	8,940,052
Total noncurrent assets	131,124,451	21,757,622	152,882,073	8,940,052
Total assets	190,870,103	23,565,924	214,436,027	12,723,520 → +
DEFERRED OUTFLOWS OF RESOURCES				
Pensions	4,849,872	149,996	4,999,868	—
Retiree health insurance	2,909,967	89,999	2,999,966	—
Total deferred outflows of resources	$ 7,759,839	$ 239,995	$ 7,999,835	$ — → +
LIABILITIES				
Current liabilities:				
Accounts payable	$ 447,427	$ 304,003	$ 751,430	$ 780,570
Due to other funds	175,000	—	175,000	1,170,388
Compensated absences	112,850	8,827	121,677	237,690
Claims and judgments	—	—	—	1,687,975
Bonds, notes, and loans payable	3,944,109	360,000	4,304,109	249,306
Total current liabilities	4,679,386	672,830	5,352,216	4,125,929
Noncurrent liabilities:				
Compensated absences	451,399	35,806	487,205	—
Claims and judgments	—	—	—	⑥ 5,602,900
Net pension liability	32,332,482	999,974	33,332,456	—
Net OPEB liability	19,399,781	599,993	19,999,774	—
Bonds, notes, and loans payable	54,452,049	19,544,019	73,996,068	—
Total noncurrent liabilities	106,635,711	21,179,792	127,815,503	5,602,900
Total liabilities	111,315,097	21,852,622	133,167,719	9,728,829 → −
DEFERRED INFLOWS OF RESOURCES				
Pensions	2,263,274	69,998	2,333,272	—
Retiree health insurance	1,357,985	42,000	1,399,984	—
Service concession arrangement proceeds	—	1,435,599	1,435,599	—
Total deferred inflows of resources	3,621,258	1,547,597	5,168,855	— → −
NET POSITION				
Net investment in capital assets	72,728,293	360,281	73,088,574	8,690,746
Restricted for debt service	—	1,451,996	1,451,996	⑦ —
Unrestricted	10,965,294	(1,406,577)	9,558,717	(5,696,055)
Total net position	$ 83,693,587	$ 405,700	$84,099,287	$ 2,994,691 ← =
			⑧	⑨

Figure 68 Notes

① The water and sewer system has two identifiable *segments*—water services and sewer services—for which additional information is provided in the notes (Figure 71).

② Internal service funds are aggregated in a single column; governments may present them individually in combining statements with the supplementary information (Figures 75–77).

③ This refers to the note explaining the reconciliation of governmental fund balance to governmental activities net position (Figure 58).

④ A government is legally or contractually prohibited from using *restricted assets* for operating purposes. Sources of this restriction may be laws, regulations of oversight bodies, or agreements connected with outstanding debt.

⑤ These capital asset amounts, along with additional details, can be found in the capital assets note (Figure 12).

⑥ The long-term liabilities note provides detailed information on these obligations (Figure 16). The notes combine the current and noncurrent parts shown here but also show the current portions in a separate column.

⑦ Internal service funds are included with the governmental activities in the government-wide statements.

⑧ This total is the same as found for the BTAs in the government-wide statement of net position (Figure 1). It also is shown as the ending net position in the statement of activities (Figure 42) and statement of revenues, expenses, and changes in fund net position (Figure 69). (However, the numbers will be different if there are activities in the enterprise funds that are classified as governmental activities instead of BTAs. See the next note.)

⑨ Enterprise funds and BTAs generally are synonymous. If, however, a government has an enterprise fund that is categorized as a governmental activity in the government-wide statements, it will provide—at the bottom of this statement—a reconciliation of total enterprise funds net position to total BTA net position.

Statement of Cash Flows

The purpose of a statement of cash flows is to identify where cash comes from and how it is used. Why track the flow of cash when there already is a statement that tracks revenues and expenses? Because it is possible that a government can have sufficient resources to cover expenses but not have enough cash to actually pay its bills. It may be equally plausible that, despite having a deficit, a government has plenty of cash available. This is the case because not all revenues and expenses involve cash. When a school district provides a continuing education course to adults, it is entitled to payment in return and records a revenue in the amount of the tuition, even if the students do not pay right away. The example in **Upon further review…a cash flow problem** should illuminate the potential problem of a cash shortfall masked by a revenue surplus.

Figure 69. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position

Local City
Statement of Revenues, Expenses, and Changes in Fund Net Position
Proprietary Funds
for the Year Ending December 31, 2017

	Business-Type Activities—Enterprise Funds			Governmental Activities—Internal Service Funds (See Note I.)
	Water and Sewer	Parking Facilities	Total	
Operating revenues:				
Charges for services	$ 11,329,883	$ 1,340,261	$ 12,670,144	$ 15,256,164
Miscellaneous	—	3,826	3,826	1,066,761
Total operating revenues	11,329,883	1,344,087	12,673,970	16,322,925
Operating expenses:				
Personal services	3,400,559	762,348	4,162,907	4,157,156
Contractual services	344,422	96,032	440,454	584,396
Utilities	754,107	100,726	854,833	214,812
Repairs and maintenance	747,315	64,617	811,932	1,960,490
Other supplies and expenses	498,213	17,119	515,332	234,445
Insurance claims and expenses	—	—	—	8,004,286
Depreciation	1,163,140	542,049	1,705,189	1,707,872
Total operating expenses	6,907,756	1,582,891	8,490,647	16,863,457
Operating income (loss)	4,422,127	(238,804)	4,183,323	(540,532)
Nonoperating revenues (expenses):				
Interest and investment revenue	454,793	146,556	601,349	134,733
Miscellaneous revenue	—	104,925	104,925	20,855
Interest expense	(1,600,830)	(1,166,546)	(2,767,376)	(41,616)
Miscellaneous expense	—	(46,846)	(46,846)	(176,003)
Total nonoperating revenue (expenses)	(1,146,037)	(961,911)	(2,107,948)	(62,031)
Income (loss) before contributions and transfers	3,276,090	(1,200,715)	2,075,375	(602,563)
Capital contributions	1,645,919	—	1,645,919	18,788
Transfers out	(290,000)	(211,409)	(501,409)	(175,033)
Change in net position	4,632,009	(1,412,124)	3,219,885	(758,808)
Total net position—beginning	79,061,578	1,817,824	80,879,402	3,753,499
Total net position—ending	$ 83,693,587	$ 405,700	$ 84,099,287	$ 2,994,691

Figure 69 Notes

① The definition of what does and does not constitute operating revenues and expenses is determined by each government based on guidance in accounting standards. Typically, it is based on the definition of operating cash flows in the statement of cash flows. **OPERATING REVENUES** generally are fees and charges produced by the activity's provision of goods or services to customers, and **OPERATING EXPENSES** are the costs of that provision and of collecting payment from customers.

② If Local City had nonmajor enterprise funds, they would be aggregated in a single column (just as in the governmental funds statements) just before the totals column in each of the proprietary funds statements. If a government has nonmajor enterprise funds, it may present them individually in supplementary combining statements in its CAFR (see Figures 72–74).

③ This refers to the note reconciling governmental funds change in fund balances to governmental activities change in net position (See Figure 59).

④ Operating income (loss) is calculated by subtracting operating expenses from operating revenues.

⑤ You can use this line to judge the financial sustainability of the activities. A loss indicates that an activity is not supporting itself and must use resources accumulated from the past or push costs off to the future, or utilize some other financing method to cover costs.

⑥ Capital contributions are amounts received for purchasing or building capital assets (or the receipt of an actual capital asset); both increase net position but should not be considered with the usual, annual inflows and outflows of the activities. That is why contributions are presented below the income (loss) amount. Similar reasoning leads to the presentation of transfers, special and extraordinary items, and additions to endowment principal.

⑦ This total transfers-out amount can be found in the statement of activities (see Figure 42); the transfer is made to the governmental activities.

⑧ Note the presence of these total net position amounts in the proprietary funds statement of net position (Figure 68) and in both government-wide statements (Figures 1 and 42).

⑨ Enterprise funds and BTAs generally are synonymous. If, however, a government has an enterprise fund that is categorized as a governmental activity in the government-wide statements, it will provide with this statement a reconciliation of change in enterprise funds net position to change in BTA net position.

Types of cash flows

The cash flows statement helps you determine *whether* a government's BTAs met their cash needs during the year and *how* they met them. For these purposes, the statement divides cash flows into four categories:

- **OPERATING CASH FLOWS** are generated by and used for basic operating purposes—the provision of services and the production and sale of goods. Examples include cash received for goods and services and cash payments to employees and suppliers. Here you discover whether the operations of the BTAs were self-sufficient on a cash basis—whether they raised enough cash to make their payments. If they did not, the cash they needed to pay the bills came from one of the other three categories. Both the enterprise and internal service funds of Local City had positive operating cash flows. (For a contrasting example, see Figure C-8. Neither of the

enterprise funds of the school district had positive operating cash flows; the cash they received from user charges financed only a small portion of the cash payments made for operations.)

Figure 70: Net cash provided by the operating activities of Local City's enterprise funds was $1,921,872.

- **NONCAPITAL FINANCING CASH FLOWS** generally relate to (1) certain grants and subsidies to or from other governments and (2) borrowing money for purposes other than buying or constructing capital assets. General grant support that governments receive from other governments would be listed in this section of the statement. Borrowing for noncapital purposes typically involves the sale of short-term notes (examples of which are listed on page 80) to even out cash flows over the year. These types of notes usually are repaid within the year, so the net cash flow for the year (absent the grants and subsidies) should be close to zero. If you notice that the net cash provided by short-term borrowing is growing by a larger percentage than revenues, it may suggest that a government is having trouble raising via operations the cash it needs to pay bills. This is an alert to look more deeply and ask more questions. Alternatively, it may reflect a change in the timing of when a government receives payments on bills or grants, or when it must make payments of its own.

Figure 70: Net cash used by the noncapital financing activities of Local City's enterprise funds was ($501,409).

- **CAPITAL AND RELATED FINANCING CASH FLOWS** are the product of borrowing and repaying funds for the purposes of purchasing, building, or reconstructing capital assets. They also include cash receipts from selling a capital asset and aid received from other levels of government to finance capital assets.

Figure 70: Net cash used by the capital and related financing activities of Local City's enterprise funds was ($3,691,303).

- **INVESTING CASH FLOWS** relate to the acquisition and sale of investments that are not cash equivalents, and the loaning of money and collection on loans by a government. Virtually all of the cash flows in this category for Local City were the receipt of interest and dividends from its investments; there is only a small amount, $15,684, in the internal service funds related to the sale of investments. In the State of Seabury cash flows statement, both the Lottery and Unemployment Compensation funds had cash outflows for the purchase of investments—$64,007 and $363,719, respectively. (See Figure B-9.)

Figure 70: Net cash provided by the investing activities of Local City's enterprise funds was $598,540.

The net cash flows for each of the four categories are totaled near the bottom of the statement to determine the overall net increase or decrease in cash. In the case of Local City, there were overall net

decreases in cash in both types of proprietary funds and in the internal service funds. The same is true for the state government proprietary funds, but both school district funds had positive overall cash flows. In the manner of the statement of activities, the statement of cash flows adds the net change in cash to the beginning cash balance to produce the ending cash balance.

Figure 70. Proprietary Funds Statement of Cash Flows

Local City
Statement of Cash Flows
Proprietary Funds
for the Year Ended December 31, 2017

	Business-Type Activities—Enterprise Funds			Governmental Activities—Internal Service Funds
	Water and Sewer	Parking Facilities	Total	
CASH FLOWS FROM OPERATING ACTIVITIES ①				
Receipts from customers	$ 11,400,200	$ 1,345,292	$ 12,745,492	$ 15,326,343
Payments to suppliers	(2,725,349)	(365,137)	(3,090,486)	(2,812,238)
Payments to employees	(3,360,055)	(750,828)	(4,110,883)	(4,209,688)
Internal activity—payments to other funds	(1,296,768)	—	(1,296,768)	—
Claims paid	—	—	—	(8,482,451)
Other receipts (payments)	(2,325,483)	—	(2,325,483)	1,061,118
Net cash provided by operating activities	1,692,545	229,327	1,921,872	883,084 → +
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES ②				
Operating subsidies and transfers to other funds	(290,000)	(211,409)	(501,409)	(175,033) → +
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES ③				
Proceeds from capital debt	4,041,322	8,660,778	12,702,100	—
Capital contributions	1,645,919	—	1,645,919	—
Purchases of capital assets	(4,194,035)	(144,716)	(4,338,751)	(400,086)
Principal paid on capital debt	(2,178,491)	(8,895,000)	(11,073,491)	(954,137)
Interest paid on capital debt	(1,479,708)	(1,166,546)	(2,646,254)	41,616
Other receipts (payments)	—	19,174	19,174	48,184
Net cash (used) by capital and related financing activities	(2,164,993)	(1,526,310)	(3,691,303)	(1,264,423) → +
CASH FLOWS FROM INVESTING ACTIVITIES ④				
Proceeds from sales and maturities of investments	—	—	—	15,684
Interest and dividends	454,793	143,747	598,540	129,550
Net cash provided by investing activities	454,793	143,747	598,540	145,234 → +
Net (decrease) in cash and cash equivalents	(307,655)	(1,364,645)	(1,672,300)	(411,138) ← =
Balances—beginning of the year	8,724,308	4,662,734	13,387,042	3,747,237
Balances—end of the year ⑤	$ 8,416,653	$ 3,298,089	$ 11,714,742	$ 3,336,099
Reconciliation of operating income (loss) to net cash provided (used) by operating activities: ⑥				
Operating income (loss)	$ 4,422,127	$ (238,804)	$ 4,183,323	$ (540,532)
Adjustments to reconcile operating income to net cash provided (used) by operating activities: ⑦				
Cash flows reported in other categories:				
Depreciation expense	1,163,140	542,049	1,705,189	1,707,872
Change in assets and liabilities:				
Receivables, net	653,264	1,205	654,469	31,941
Inventories	2,829	—	2,829	39,790
Accounts and other payables	(297,446)	(86,643)	(384,089)	475,212
Accrued expenses	(4,251,369)	11,520	(4,239,849)	(831,199)
Net cash provided by operating activities ⑧	$ 1,692,545	$ 229,327	$ 1,921,872	$ 883,084

Figure 70 Notes

① Operating cash flows are related to the provision of services and the production and sale of goods.

② Noncapital financing cash flows are related to general grants made to or received from other governments, as well as borrowing money for purposes other than buying or building capital assets. The amounts shown here are transfers from the BTAs to the governmental activities.

③ Capital and related financing cash flows are related to borrowing and repaying debt for purchasing and constructing capital assets, as well as the sale of capital assets.

④ Investing cash flows predominantly are related to investment earnings and the sale and purchase of investments.

⑤ This is the amount shown as the combination of unrestricted and restricted cash in the BTAs on both the government-wide and proprietary funds statements of net position, though for some governments it also may include some items classified as investments. (See Figures 1 and 68.)

⑥ The reconciliation explains the differences between the operating flows of cash and the operating income (loss) reported on an accrual basis in the proprietary funds statement of revenues, expenses, and changes in fund net position (Figure 69).

⑦ These adjustments remove revenues and expenses that did not involve an exchange of cash.

⑧ If a government engaged in any investing, capital, or financing activities that affected assets and liabilities but did not involve cash, it would explain them either on the face of the statement or in a separate schedule. A capital lease is the most prevalent example. This disclosure is not illustrated because Local City had no such activities.

Reconciliation of cash and accrual

The last section of the statement is a reconciliation of the net cash provided (used) by operating activities to the operating income (loss) amounts in the statement of revenues, expenses, and changes in fund net position. (See Figure 69.) Alternatively, a government may present the reconciliation in an accompanying schedule. The function of this reconciliation is similar to those in the governmental funds statements. In this case, it is intended to explain how the accrual-based results of operations for a government's BTAs differ from their annual cash flows. It also may help you understand how the information in the three proprietary funds statements are related to each other.

As noted earlier, not all revenues and expenses involve cash. Depreciation, for example, is a noncash expense; the reported value of capital assets, rather than cash, is reduced on the statement of net position. There are other expenses, such as the using up of inventory, that similarly do not involve cash changing hands. On the inflow side, cash is not the only resource that flows into a government and is considered revenue. Recall the example in **Upon further review…a cash flow problem** on page 238 of the water utility billing customers; a revenue is recorded, but rather than cash flowing in, a receivable is created and appears on the statement of net position.

What can you do with statement of cash flows information?

Four closely related potential uses for cash flows statement information have been touched upon:

- *You can assess whether and how cash requirements were met.* The division of cash flows into categories allows you to readily see whether the operations of BTAs generated enough cash on their own to support their needs, or whether other means of raising cash were employed to pay for operations.
- *You can identify sources and uses of cash.* You can use percentage distributions and percentage changes to track where a government's BTAs get their cash and how they use it, and make comparisons over time and with other BTAs. For example, you might examine the BTAs' use of external financing to balance cash flows, how that has changed during the past decade, and how it compares with similar BTAs' use of external financing.
- *You can get a sense of future cash needs and the ability of a government's BTAs to pay bills as they come due.* Your consideration of the first two issues should give you a good sense of where BTAs are headed. Is cash harder to come by through operations, or is it easier? Are BTAs becoming less reliant or more dependent on borrowing and asset sales? Your answers to these questions may provide insight into the government's future finances.
- *You can learn about the differences between cash and income.* In the same way that the governmental funds reconciliations were instructive about the differences between the accrual-based change in net position and the modified accrual-based change in fund balances, the reconciliation in the cash flows statement identifies the differences between financial activities measured on an accrual basis versus a cash basis.

Your assessment of these issues will be informative to judgments about the ability of a government to manage its BTA cash flows, as well as assist in evaluating the government's overall financial management. You also might use such analyses as part of a determination of whether and how the BTAs' methods for meeting cash flow requirements should change. Should they engage in more or less short-term borrowing? Do bill collection deadlines or the timing of major cash outlays need to be altered?

NOTE DISCLOSURES ON PROPRIETARY FUNDS SEGMENTS

If a government has enterprise funds, it discloses information in its notes about individual **SEGMENTS** within its BTAs. For instance, a government's utility system might have two segments that operate water and sewer services. When a segment exists, a government provides a note disclosure that (1) describes what the segment does and (2) presents a set of **CONDENSED FINANCIAL STATEMENTS.** These statements, which are illustrated in Figure 71, include:

- Condensed statement of net position
- Condensed statement of revenues, expenses, and changes in fund net position
- Condensed statement of cash flows.

A government also may present a statement of activities for its segments with the supplemental information in the CAFR, but it is not required to do so.

Figure 71: Noncurrent liabilities of the sewer department were $49,426,828.

What Can You Do with Segment Disclosures?

The fund financial statements are valuable in part because they provide more detail than you can find in the government-wide statements. Rather than a single column for BTAs, the proprietary funds statements show the major enterprise funds individually, allowing you to examine the finances of the various business-type functions a government engages in. Even these funds, though, may encompass more than a single activity. The segment note disclosures help you to identify the activities that have their own revenue sources and for which long-term debt has been issued and will be repaid from those sources. If you are interested in evaluating a government's ability to raise the necessary resources to repay that debt, you need financial information specifically related to the relevant activity.

SUPPORTING INFORMATION RELATED TO PROPRIETARY FUNDS

Supporting information that is relevant to the proprietary funds financial statements can be found in combining financial statements and fund-type and individual fund statements.

Nonmajor Enterprise Funds

In the proprietary funds financial statements, major enterprise funds are each shown individually and nonmajor enterprise funds are aggregated into a single column. If a government prepares a CAFR, the financial section will include as SI combining statements that offer more detail about the information aggregated in the fund financial statements. The following combining statements show the nonmajor enterprise funds individually in their own columns:

- Combining statement of net position (Figure 72)
- Combining statement of revenues, expenses, and changes in fund net position (Figure 73)
- Combining statement of cash flows (Figure 74).

Figure 71 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Figure 71. Condensed Statements, Segments

The town issues separate revenue bonds to finance its water and sewer activities. The two activities are accounted for together, but investors in those bonds rely solely on the revenue generated by the individual activities for repayment. Summary financial information for each activity is presented below. The water activity relates to the water supply system. The sewer activity relates to the sewage treatment plant, sewage pumping stations, and collection systems.

	Water	Sewer
CONDENSED STATEMENT OF NET POSITION		
Assets		
Current assets	$ 5,229,593	$ 6,919,814
Capital assets	38,952,991	92,171,460
Total assets	44,182,584	99,091,274
Deferred outflows of resources	1,476,352	2,908,734
Liabilities		
Interfund payables	—	175,000
Other current liabilities	1,520,672	2,984,214
Noncurrent liabilities	5,476,120	49,426,828
Total liabilities	6,996,792	52,586,042
Deferred inflows of resources	1,099,888	2,134,445
Net position		
Net investment in capital assets	32,772,337	39,955,956
Unrestricted	4,789,919	7,323,565
Total net position	$ 37,562,256	$ 47,279,521
CONDENSED STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION		
Operating revenues	$ 4,159,350	$ 7,170,533
Depreciation expense	(549,987)	(613,153)
Other operating expenses	(2,642,774)	(3,101,842)
Operating income	966,589	3,455,538
Nonoperating revenues (expenses):		
Investment income	217,378	237,415
Interest expense	(402,972)	(1,197,858)
Capital contributions	1,159,909	486,010
Transfers out	—	(290,000)
Change in net position	1,940,904	2,691,105
Beginning net position	35,621,352	44,588,416
Ending net position	$ 37,562,256	$ 47,279,521
CONDENSED STATEMENT OF CASH FLOWS		
Net cash provided (used) by:		
Operating activities	$ 841,902	$ 850,643
Noncapital financing activities	—	(290,000)
Capital and related financing activities	(523,876)	(1,641,117)
Investing activities	217,378	237,415
Net increase (decrease)	535,404	(843,059)
Beginning cash and cash equivalents	3,089,534	5,634,774
Ending cash and cash equivalents	$ 3,624,938	$ 4,791,715

By the numbers…supplemental statements in the CAFR

Category	Statements
Component units (typically aggregated in a single column on the government-wide statements, although multiple component units may be shown individually)	Combining statement of net position and combining statement of activities; OR condensed statements of net position and activities in the notes (the component unit statements appear between the funds statements and the notes, whereas the other statements below would be found after the notes and RSI); see Figures 91–93
Nonmajor governmental funds (aggregated in a single column on the governmental funds statements)	Combining balance sheet; combining statement of revenues, expenditures, and changes in fund balances; see Figures 63 and 64
Nonmajor enterprise funds (aggregated in a single column on the proprietary funds statements)	Combining statement of net position; combining statement of revenues, expenses, and changes in fund net position; combining statement of cash flows; see Figures 72–74
Internal service funds (aggregated in a single column on the proprietary funds statements)	Combining statement of net position; combining statement of revenues, expenses, and changes in fund net position; combining statement of cash flows; see Figures 75–77
Fiduciary funds (aggregated by fund type on the fiduciary funds statements)	Combining statement of fiduciary net position; combining statement of changes in fiduciary net position; see Figures 80 and 81 For agency funds: combining statement of assets and liabilities; combining statement of changes in assets and liabilities; see Figure 82
Individual governmental funds	Balance sheet and statement of revenues, expenditures, and changes in fund balances; OR separate balance sheets and statements of revenues, expenditures, and changes in fund balances for the current and previous year; OR a single comparative balance sheet and comparative statement of revenues, expenditures, and changes in fund balances containing both years

Individual proprietary funds	Statement of net position, statement of revenues, expenses, and changes in fund net position, and statement of cash flows; OR separate statements of net position, statements of revenues, expenses, and changes in fund net position, and statements of cash flows for the current and previous year; OR a single comparative statement of net position, statement of revenues, expenses, and changes in fund net position, and statement of cash flows containing both years
Individual fiduciary funds	Statement of fiduciary net position and statement of changes in fiduciary net position; OR separate statements of fiduciary net position and statements of changes in fiduciary net position; OR a single comparative statement of fiduciary net position and statement of changes in fiduciary net position containing both years

Figure 72. Combining Statement of Net Position, Nonmajor Enterprise Funds

City of Finden
Combining Statement of Net Position ①
Nonmajor Enterprise Funds
As of June 30, 2017

	Storm Sewer Fund	Recreation Fund	Solid Waste Fund	Street Lighting Fund	② Total Nonmajor Proprietary Funds
ASSETS					
Current assets:					
Cash and cash equivalents	$ 1,791,622	$ 318,147	$ 370,372	$ —	$ 2,408,141
Accounts receivable (net of allowance for doubtful accounts)	171,353	—	244,834	29,050	445,237
Restricted cash:					
Capital improvement projects	—	1,009,131	—	—	1,009,131
Total current assets	1,962,975	1,327,278	615,206	29,050	3,934,509
Capital assets:					
Land	280,748	39,822	—	—	320,570
Buildings and systems	25,883	3,989,563	—	—	4,015,446
Improvements other than buildings	473,085	—	—	—	473,085
Machinery and equipment	793,681	215,053	35,688	3,564	1,047,986
Infrastructure	3,184,484	—	—	—	3,184,484
Construction in progress	718,688	546,011	4,025	324,137	1,592,861
Less accumulated depreciation	(800,769)	(3,942,962)	(33,378)	(2,970)	(4,780,079)
Total capital assets (net of accumulated depreciation)	4,675,800	847,487	6,335	324,731	5,854,353
Total assets	6,638,775	2,174,765	621,541	353,781	9,788,862
LIABILITIES					
Accounts payable	56,478	113,007	194,005	168	363,658
Accrued liabilities—short term	26,502	53,011	—	5,732	85,245
Due to other funds	—	—	—	316,515	316,515
Total liabilities	82,980	166,018	194,005	322,415	765,418
DEFERRED INFLOWS OF RESOURCES					
Grants received in advance	—	165,727	—	—	165,727
NET POSITION					
Net investment in capital assets	4,675,800	847,487	6,335	324,731	5,854,353
Unrestricted	1,879,995	995,533	421,201	(293,365)	3,003,364
Total net position	$ 6,555,795	$ 1,843,020	$ 427,536	$ 31,366	$ 8,857,717

Figure 72 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements. Local City does not have any nonmajor enterprise funds.

② The totals in this column feed into the nonmajor enterprise funds column in the proprietary funds statement of net position.

Figure 73. Combining Statement of Revenues, Expenses, and Changes in Fund Net Position, Nonmajor Enterprise Funds

City of Finden
Combining Statement of Revenues, Expenses, and Changes in Fund Net Position ①
Nonmajor Enterprise Funds
As of June 30, 2017

	Storm Sewer Fund	Recreation Fund	Solid Waste Fund	Street Lighting Fund	Total Nonmajor Proprietary Funds ②
REVENUES					
Charges for services	$ 2,144,015	$ 1,196,464	$ 2,626,672	$ 305,136	$ 6,272,287
Other revenues	9,713	1,071	—	—	10,784
Total revenues	2,153,728	1,197,535	2,626,672	305,136	6,283,071
EXPENSES					
Personal services	396,881	1,148,263	—	124,933	1,670,077
Supplies and maintenance	124,803	296,259	15,943	2,915	439,920
Administrative fee	252,058	3,228	270,050	—	525,336
Utilities	1,426	166,541	—	2,839	170,806
Contract services	120,565	51,587	2,270,961	485	2,443,598
Equipment lease and rentals	8,271	—	—	691,390	699,661
Insurance	16,627	16,294	—	—	32,921
Depreciation	228,885	173,532	215	1,188	403,820
Miscellaneous	37,575	44,559	—	321	82,455
Total operating expenses	1,187,091	1,900,263	2,557,169	824,071	6,468,594
Operating income (loss)	966,637	(702,728)	69,503	(518,935)	(185,523)
NONOPERATING REVENUES AND EXPENSES					
Interest revenue	17,305	29,314	9,806	(5,081)	51,344
Contributions from developers	152,500	—	—	—	152,500
Donations	—	1,000,000	—	—	1,000,000
Total nonoperating revenues	169,805	1,029,314	9,806	(5,081)	1,203,844
Income (loss) before transfers	1,136,442	326,586	79,309	(524,016)	1,018,321
Transfers in	—	328,562	25,000	480,000	833,562
Transfers out	20,106	(310,009)	—	—	(330,115)
Change in net position	1,116,336	345,139	104,309	(44,016)	1,521,768
Total net position—beginning	5,439,459	1,497,881	323,227	75,382	7,335,949
Total net position—ending	$ 6,555,795	$ 1,843,020	$ 427,536	$ 31,366	$ 8,857,717

Figure 73 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements. Local City does not have any nonmajor enterprise funds.

② The totals in this column feed into the nonmajor enterprise funds column in the proprietary funds statement of revenues, expenses, and changes in fund net position.

Figure 74. Combining Statement of Cash Flows, Nonmajor Enterprise Funds

City of Finden
Combining Statement of Cash Flows
Nonmajor Enterprise Funds ①
As of June 30, 2017

	Storm Sewer Fund	Recreation Fund	Solid Waste Fund	Street Lighting Fund	② Total Nonmajor Proprietary Funds
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from customers and users	$ 2,144,015	$ 1,196,464	$ 2,626,672	$ 305,136	$ 6,272,287
Receipts from interfund services provided	9,713	1,071	—	—	10,784
Payments to suppliers	(263,755)	(456,582)	(2,387,894)	(422,249)	(3,530,480)
Payments to employees	(396,881)	(1,148,263)	—	(124,933)	(1,670,077)
Payments for interfund services used	(252,058)	(3,228)	(270,050)	—	(525,336)
Net cash provided (used) by operating activities	1,241,034	(410,538)	(31,272)	(242,046)	557,178
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Donations	—	1,000,000	—	—	1,000,000
Transfers in	—	328,562	25,000	480,000	833,562
Transfers out	(20,106)	(310,009)	—	—	(330,115)
Net cash provided (used) by noncapital activities	(20,106)	1,018,553	25,000	480,000	1,503,447
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES					
Purchase of capital assets	(1,026,278)	(546,011)	(4,025)	(232,873)	(1,809,187)
Proceeds from sales of capital assets	—	—	—	—	—
Net cash provided (used) by capital and related financing activities	(1,026,278)	(546,011)	(4,025)	(232,873)	(1,809,187)
CASH FLOWS FROM INVESTING ACTIVITIES					
Interest income	17,305	29,314	9,806	(5,081)	51,344
Net cash provided (used) by investing activities	17,305	29,314	9,806	(5,081)	51,344
Net increase (decrease) in cash and cash equivalents	211,955	91,318	(491)	—	302,782
Cash and cash equivalents—beginning of year	1,579,667	1,235,960	370,863	—	3,186,490
Cash and cash equivalents—end of year	$ 1,791,622	$ 1,327,278	$ 370,372	$ —	$ 3,489,272
Reconciliation of operating income to net cash provided (used) by operating activities:					
Operating income (loss)	$ 966,637	$ (702,728)	$ 69,503	$ (518,935)	$ (185,523)
Adjustments to reconcile operating income to net cash provided (used) by operating activities:					
Depreciation expense	228,885	173,532	215	1,188	403,820
(Increase) decrease in receivables	730	—	(11,454)	(16,334)	(27,058)
Increase (decrease) in accounts payable	39,928	82,008	(89,536)	168	32,568
Increase (decrease) in accrued liabilities	4,854	3,631	—	291,867	300,352
Increase (decrease) in deferred revenue	—	33,019	—	—	33,019
Total adjustments	274,397	292,190	(100,775)	276,889	742,701
Net cash provided (used) by operating activities ③	$ 1,241,034	$ (410,538)	$ (31,272)	$ (242,046)	$ 557,178

Figure 74 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements. Local City does not have any nonmajor enterprise funds.

② The totals in this column feed into the nonmajor enterprise funds column in the proprietary funds statement of cash flows.

③ The required reconciliation of change in cash to CHANGE IN FUND NET POSITION is not illustrated here. The note regarding noncash activities likewise is not illustrated.

Internal Service Funds

Internal service funds are aggregated in the proprietary funds financial statements. The internal service funds are shown individually in the following combining statements:

- Combining statement of net position (Figure 75)
- Combining statement of revenues, expenses, and changes in fund net position (Figure 76)
- Combining statement of cash flows (Figure 77).

Individual Funds

If a government has only a single nonmajor enterprise fund or a single internal service fund, it will prepare an individual fund financial statement for that fund rather than a combining statement. A government also may use individual fund statements in order to demonstrate its compliance with a finance-related legal or contractual provision or to present comparisons with the prior reporting period.

What Can You Do with Supporting Information about Proprietary Funds?

Combining and individual fund financial statements for the nonmajor enterprise funds and internal service fund type are amenable to similar analyses and answer similar questions as the statements for the governmental funds. (Refer to Part Nine.) As previously mentioned, a notable difference is that the governmental funds are focused primarily on short-term financial information, whereas the proprietary funds contain accrual and economic resources information, including long-term debt and capital assets.

These combining and individual fund statements provide details that generally are not found in the proprietary funds financial statements. Funds that do not meet the criteria to be automatically reported as major (or which are consolidated by fund type, such as internal service funds) can be examined more closely in these supporting statements.

Figure 75. Combining Statement of Net Position, Internal Service Funds

Local City
Combining Statement of Net Position for Internal Service Funds
As of December 31, 2017

	Casualty Insurance	Fleet Management	Health/Life Insurance	Telecom-munications	Data Processing	① Total
ASSETS						
Current assets:						
Cash and cash equivalents	$ 632,008	$ 1,845,325	$ 428,398	$ 6,645	$ 423,723	$ 3,336,099
Investments	—	—	—	—	150,237	150,237
Receivables, net	9,837	11,363	114,930	203	21,471	157,804
Inventories	—	127,140	—	—	12,188	139,328
Total current assets	641,845	1,983,828	543,328	6,848	607,619	3,783,468
Capital assets:						
Buildings and equipment, net	21,383	2,821,024	—	5,526,642	571,003	8,940,052
Total assets	663,228	4,804,852	543,328	5,533,490	1,178,622	12,723,520
LIABILITIES						
Current liabilities:						
Accounts payable	195,988	77,931	312,622	144,840	49,189	780,570
Due to other funds	—	—	—	970,252	200,136	1,170,388
Compensated absences	11,123	69,714	—	97,449	59,404	237,690
Claims and judgments	1,687,975	—	—	—	—	1,687,975
Bonds, notes, and loans payable	—	—	—	249,306	—	249,306
Total current liabilities	1,895,086	147,645	312,622	1,461,847	308,729	4,125,929
Noncurrent liabilities:						
Claims and judgments	5,602,900	—	—	—	—	5,602,900
Total liabilities	7,497,986	147,645	312,622	1,461,847	308,729	9,728,829
NET POSITION						
Net investment in capital assets	21,383	2,821,024	—	5,277,336	571,003	8,690,746
Unrestricted	(6,856,141)	1,836,183	230,706	(1,205,693)	298,890	(5,696,055)
Total net position	$ (6,834,758)	$ 4,657,207	$ 230,706	$ 4,071,643	$ 869,893	$ 2,994,691

Figure 75 Note

① The totals in this column feed into the internal service funds column in the proprietary funds statement of net position (Figure 68).

Figure 76. Combining Statement of Revenues, Expenses, and Changes in Fund Net Position, Internal Service Funds

Local City
Combining Statement of Revenues, Expenses, and Changes in Fund Net Position for Internal Service Funds
for the Year Ended December 31, 2017

	Casualty Insurance	Fleet Management	Health/Life Insurance	Telecom-munications	Data Processing	① Total
Operating revenues:						
Charges for services	$ 1,886,451	$ 4,096,753	$4,488,619	$ 3,542,116	$ 1,242,225	$ 15,256,164
Miscellaneous	18,907	—	1,047,854	—	—	1,066,761
Total operating revenues	1,905,358	4,096,753	5,536,473	3,542,116	1,242,225	16,322,925
Operating expenses:						
Personal services	169,866	1,248,271	—	1,850,222	888,797	4,157,156
Contractual services	176,486	62,449	24,402	22,843	298,216	584,396
Utilities	—	2,616	—	212,196	—	214,812
Repairs and maintenance	2,497	1,523,774	—	389,132	45,087	1,960,490
Other supplies and expenses	55,041	23,656	—	89,252	66,496	234,445
Insurance claims and expenses	2,085,306	—	5,918,980	—	—	8,004,286
Depreciation	5,541	448,944	—	938,251	315,136	1,707,872
Total operating expenses	2,494,737	3,309,710	5,943,382	3,501,896	1,613,732	16,863,457
Operating income (loss)	(589,379)	787,043	(406,909)	40,220	(371,507)	(540,532)
Nonoperating revenues (expenses):						
Interest and investment revenue	48,570	52,925	10,338	—	22,900	134,733
Miscellaneous revenue	9,544	732	—	10,579	—	20,855
Interest expense	—	—	—	(35,185)	(6,431)	(41,616)
Miscellaneous expense	(14,948)	(39,790)	—	(120,949)	(316)	(176,003)
Total nonoperating revenues (expenses)	43,166	13,867	10,338	(145,555)	16,153	(62,031)
Income (loss) before contributions and transfers	(546,213)	800,910	(396,571)	(105,335)	(355,354)	(602,563)
Capital contributions	—	3,364	—	1,222	14,202	18,788
Transfers in	10,000	—	—	9,008	—	19,008
Transfers out	—	—	(50,319)	—	(143,722)	(194,041)
Change in net position	(536,213)	804,274	(446,890)	(95,105)	(484,874)	(758,808)
Net position—beginning	(6,298,545)	3,852,933	677,596	4,166,748	1,354,767	3,753,499
Net position—ending	$ (6,834,758)	$ 4,657,207	$ 230,706	$ 4,071,643	$ 869,893	$ 2,994,691

Figure 76 Note

① The totals in this column feed into the internal service funds column in the proprietary funds statement of revenues, expenses, and changes in fund net position (Figure 69).

Figure 77. Combining Statement of Cash Flows, Internal Service Funds

Local City
Combining Statement of Cash Flows for Internal Service Funds
for the Year Ended December 31, 2017

	Casualty Insurance	Fleet Management	Health/Life Insurance	Telecom-munications	Data Processing	① Total
CASH FLOWS FROM OPERATING ACTIVITIES						
Receipts from customers	$ 1,905,870	$ 4,098,790	$4,549,558	$ 3,542,157	$1,229,968	$ 15,326,343
Payments to suppliers	(129,409)	(1,671,378)	—	(656,961)	(354,490)	(2,812,238)
Payments to employees	(166,729)	(1,236,855)	—	(1,910,948)	(895,156)	(4,209,688)
Claims paid	(2,863,973)	—	(5,618,478)	—	—	(8,482,451)
Other receipts (payments)	18,907	—	1,023,452	—	18,759	1,061,118
Net cash provided (used) by operating activities	(1,235,334)	1,190,557	(45,468)	974,248	(919)	883,084
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES						
Operating subsidies and transfers to other funds	10,000	—	(50,319)	9,008	(143,722)	(175,033)
RELATED FINANCING ACTIVITIES						
Purchases of capital assets	(13,578)	(237,054)	—	(132,596)	(16,858)	(400,086)
Principal paid on capital debt	—	—	—	(954,137)	—	(954,137)
Interest paid on capital debt	—	—	—	(35,185)	(6,431)	(41,616)
Other receipts (payments)	25,167	(39,058)	—	145,307	—	131,416
Net cash provided (used) by capital and related financing activities	11,589	(276,112)	—	(976,611)	(23,289)	(1,181,191)
CASH FLOWS FROM INVESTING ACTIVITIES						
Proceeds from sales and maturities of investments	—	—	—	—	15,684	15,684
Interest and dividends	48,570	47,742	10,338	—	22,900	129,550
Net cash provided by investing activities	48,570	47,742	10,338	—	38,584	145,234
Net increase (decrease) in cash and cash equivalents	(1,165,175)	962,187	(85,449)	6,645	(129,346)	(411,138)
Balances—beginning of the year	1,797,183	883,138	513,847	—	553,069	3,747,237
Balances—end of the year ②	$ 632,008	$ 1,845,325	$ 428,398	$ 6,645	$ 423,723	$ 3,336,099

Figure 77 Notes

① The totals in this column feed into the internal service funds column in the proprietary funds statement of cash flows (Figure 70).

② The required reconciliation of change in cash to change in fund net position is not illustrated here. See Figure 70 for more details. The note regarding noncash activities likewise is not illustrated.

FIDUCIARY FUNDS FINANCIAL STATEMENTS

There are two required financial statements for the fiduciary funds, and both contain the same kind of comprehensive financial information as the government-wide and proprietary funds financial statements (economic resources and accrual):

- Statement of fiduciary net position (Figures 78, B-10, and C-9), and
- Statement of changes in fiduciary net position (Figures 79, B-11, and C-10).

Figure 78: The fair value of corporate bonds in the fund for the employee retirement plan was $16,320,047.

Information in the fiduciary funds financial statements is aggregated by category of fiduciary fund. In other words, all of the pension and OPEB funds are totaled and presented in a single column, all of the agency funds are combined into a single column, and so on. The net position section of Figure 78 presents the difference between assets, deferred outflows, liabilities, and deferred inflows as *net position held in trust*. (Local City does not have any deferred outflows or deferred inflows in its fiduciary funds at present.) The agency funds do not have net position, however. Because the resources they contain are held temporarily before being passed on to their ultimate recipients, the assets of agency funds exactly equal their liabilities. (See **Upon further review…classifications of fiduciary funds and their financial statements** on page 264.)

Rather than revenues and expenses, Figure 79 reports **ADDITIONS** and **DEDUCTIONS**. Additions generally come from contributions of participating governments and their employees and income from the investments of the funds. Deductions are mostly benefit payments and, to a lesser extent, administrative costs. Agency funds do not appear in the statement of changes in fiduciary net position because, as just mentioned, they do not contain net position.

Figure 79: Refunds of contributions in the fund for the employee retirement plan were $464,691.

What Can You Do with Fiduciary Funds Information?

You may find the fiduciary funds statements useful for beginning to ask questions about the financial status of pensions and trusts. Ultimately, the search for answers to these questions should lead you to the additional disclosures governments make in the notes or RSI (see Parts Five and Six), and from there to the separately issued financial statements, if available, for the entities represented by these funds. This is particularly true for PERS. In this way, the fiduciary funds statements may be a first step toward identifying crucial issues and raising questions that further research can answer.

There are many reasons that you might want to examine the fiduciary funds. For instance, with the data in these statements, as well as the notes and RSI about pensions, you could begin to assess the financial

health of a pension plan. Are the assets growing or declining? Is the government making its necessary contributions as employer? Regarding agency funds, the governments that are the ultimate recipients of the resources collected in those funds might want information about the pace at which the government reporting the agency fund is collecting and disbursing its resources, and whether there are resources in the fund that they can expect to receive soon.

By the numbers…classes of fiduciary funds

	Fund Classifications	Examples
Fiduciary Funds report assets that belong to others and that cannot be used to support a government's own programs.	*Pension (and other employee benefit) trust funds* account for resources held in trust for employees and beneficiaries of pension and retiree healthcare plans.	A state has separate public employee retirement funds for state police, legislators, and other state employees, and separate cost-sharing pension funds for teachers and local government employees.
	Investment trust funds track the portion of a government's investment pools that belongs to other governments.	A county manages a short-term investment pool so localities can earn income from spare cash until it is needed.
	Private-purpose trust funds report all other trust arrangements.	A state has an unclaimed funds account where it holds abandoned bank accounts and other property that are expected to be returned to the original owners or their beneficiaries.
	Agency funds contain resources held on a temporary, purely custodial basis.	As a county collects its own property taxes, it also collects taxes levied by its villages, towns, and school districts and passes along their shares.

Figure 78. Statement of Fiduciary Net Position

Local City
Statement of Fiduciary Net Position
Fiduciary Funds
As of December 31, 2017

	① ② Employee Retirement Plan	Private-Purpose Trust	③ Agency Fund
ASSETS			
Cash and cash equivalents	$ 1,973	$ 1,250	$ 44,889
Receivables:			
Interest and dividends	508,475	760	—
Other receivables	6,826	—	183,161
Total receivables	515,301	760	183,161
Investments, at fair value: ④			
U.S. government obligations	13,056,037	80,000	—
Municipal bonds	6,528,019	—	—
Corporate bonds	16,320,047	—	—
Corporate stocks	26,112,075	—	—
Other investments	3,264,009	—	—
Total investments	65,280,187	80,000	—
Total assets	65,797,461	82,010	$ 228,050 → +
LIABILITIES ⑤			
Accounts payable	—	1,234	$ —
Refunds payable and others	1,358	—	228,050
Total liabilities	1,358	1,234	$ 228,050 → −
NET POSITION ⑥			⑦
Held in trust for pension benefits and other purposes	$ 65,796,103	$ 80,776	=
	⑧ ⑨		

Figure 78 Notes

① This column actually is a single fund rather than an aggregation of multiple funds because Local City has just one pension plan.

② If Local City had any investment trusts, they would be aggregated in a column here.

③ Unlike the governmental and enterprise funds, fiduciary funds are presented by class of fund rather than individual major funds. In the case of Local City, each fund classification is just a single fund. If a government's fiduciary fund classifications contain multiple funds, it may present supplementary combining statements in its CAFR (see Figures 80 and 81).

④ Unlike other assets such as inventories and buildings, most investments are shown in this and other statements at their fair values as of the date of the statement, rather than at their purchase price.

⑤ Local City's fiduciary funds do not have any deferred inflows of resources or deferred outflows of resources. If they did, separate sections would appear in the statement of fiduciary net position to report them, just as in the government-wide statement of net position (Figure 1).

⑥ Net position is not categorized as it is in the government-wide and proprietary funds statements because it is not available to the government.

⑦ Agency funds hold resources only temporarily on behalf of others—everything held by these funds is due to be passed along to the governments or other organizations it belongs to. Therefore, assets (plus deferred outflows) equal liabilities (plus deferred inflows) at all times, and there is no residual net position.

⑧ Depending on the type of pension or OPEB plan a government participates in, it may provide additional information about its pension and OPEB plans in the notes and RSI. See Parts Five and Six for more details.

⑨ You will find statements for pension plans and investment pools in the notes to a government's financial statements if the plans or pools do not issue separate statements of their own.

Figure 79 Notes

① Agency funds are not included in this statement because their assets equal their liabilities and thus they do not have residual net position.

② Additions increase the net position of a fiduciary fund, and commonly include contributions from the government and employees to the pension plan and earnings from investments.

③ Deductions reduce net position and primarily take the form of benefit payments, though they also include general administrative costs.

Figure 79. Statement of Changes in Fiduciary Net Position

Local City
Statement of Changes in Fiduciary Net Position
Fiduciary Funds
for the Year Ended December 31, 2017

	Employee Retirement Plan	Private-Purpose Trust ①
ADDITIONS ②		
Contributions:		
Employer	$ 2,721,341	$ —
Plan members	1,421,233	—
Total contributions	4,142,574	—
Investment earnings:		
Net (decrease) in fair value of investments	(272,522)	—
Interest	2,460,871	4,560
Dividends	1,445,273	—
Total investment earnings	3,633,622	4,560
Less investment expense	216,428	—
Net investment earnings	3,417,194	4,560
Total additions	7,559,768	4,560 → +
DEDUCTIONS ③		
Benefits	2,453,047	3,800
Refunds of contributions	464,691	—
Administrative expenses	87,532	678
Total deductions	3,005,270	4,478 → −
Change in net position	4,554,498	82
Net position—beginning of the year	61,241,605	80,694
Net position—end of the year	$ 65,796,103	$ 80,776 ← =

Figure 80 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements. Local City does not have more than one fund of any fiduciary fund classification.

② If these funds had deferred outflows or deferred inflows, they would appear after the assets or liabilities, respectively.

Figure 80. Combining Statement of Fiduciary Net Position

Derek County
Combining Statement of Fiduciary Net Position ①
Fiduciary Funds
As of June 30, 2017

	Pension Trust Funds		Private-Purpose Trust	Agency Funds			
	County Retirement System	Police Officers Retirement System	Tuition Program	Insurance Company Deposits	Payroll Clearing	Property Tax Collection	Total Fiduciary Funds
ASSETS							
Cash and cash equivalents	$ 2,219,417	$ 356,948	$ 48,641	$ —	$ 11,170	$ 151,027	$ 2,787,203
Receivables	369,047	41,857	27,861	—	25	13,841	452,631
Due from other funds	15,371	3,258	—	—	46,524	5,501	70,654
Investments	16,266,351	1,877,003	21,552	—	—	21,507	18,186,413
Securities held in lieu of surety bonds	—	—	—	369,918	—	165	370,083
Capital assets, net	3,758	384	—	—	—	—	4,142
Total assets	**18,873,944**	**2,279,450**	**98,054**	**369,918**	**57,719**	**192,041**	**21,871,126**
②							
LIABILITIES							
Accounts payable	37,472	4,395	88,069	—	161	8,629	138,726
Due to other funds	21,141	638	—	—	10,995	15	32,789
Accrued liabilities	5,536	846	—	—	—	—	6,382
Due to other governments	—	—	—	—	—	183,397	183,397
Deposits	—	—	—	369,918	—	—	369,918
Amounts held in custody for others	—	—	—	—	46,563	—	46,563
Deferred retirement benefits	229,590	—	—	—	—	—	229,590
Total liabilities	**293,739**	**5,879**	**88,069**	**369,918**	**57,719**	**192,041**	**1,007,365**
NET POSITION							
Held in trust for pension benefits	18,580,205	2,273,571	—	—	—	—	20,853,776
Held in trust for others	—	—	9,985	—	—	—	9,985
Total net position	**$ 18,580,205**	**$ 2,273,571**	**$ 9,985**	**$ —**	**$ —**	**$ —**	**$ 20,863,761**

Figure 81. Combining Statement of Changes in Fiduciary Net Position

Derek County
Combining Statement of Changes in Fiduciary Net Position ①
Fiduciary Funds
for the Fiscal Year Ended June 30, 2017

	Pension Trust Funds		Private-Purpose Trust	
	County Retirement System	Police Officers Retirement System	Tuition Program	Total Fiduciary Funds
ADDITIONS				
Retirement contributions:				
Employer	$ 509,044	$ 88,608	$ —	$ 597,652
Employees	413,850	56,562	—	470,412
Investment income, net of expenses	162,089	17,978	1,495	181,562
Tuition plan deposits	—	—	42,445	42,445
Transfers in	3,141	92	—	3,233
Total additions	**1,088,124**	**163,240**	**43,940**	**1,295,304**
DEDUCTIONS				
Regular retirement benefits	957,114	111,216	—	1,068,330
Supplemental benefits	3,141	92	—	3,233
Deferred benefits	193,283	—	—	193,283
Refunds	63,936	11,214	—	75,150
Accidental death benefits	—	858	—	858
Depreciation	107	11	—	118
Tuition plan disbursements	—	—	33,505	33,505
Administrative expense	12,699	1,509	1,005	15,213
Transfers out	2,104	—	365	2,469
Total deductions	**1,232,384**	**124,900**	**34,875**	**1,392,159**
Change in net position	**(144,260)**	**38,340**	**9,065**	**(96,855)**
Net position, beginning	**18,724,465**	**2,235,231**	**920**	**20,960,616**
Net position, ending	**$ 18,580,205**	**$ 2,273,571**	**$ 9,985**	**$ 20,863,761**

Figure 81 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements. Local City does not have more than one fund of any fiduciary fund classification.

Figure 82. Combining Statement of Changes in Assets and Liabilities, Agency Funds

Derek County
Combining Statement of Changes in Assets and Liabilities ①
Agency Funds
for the Fiscal Year Ended June 30, 2017

	Balance July 1, 2016	② Additions	③ Deductions	④ Balance June 30, 2017
Insurance Company Deposits				
Assets:				
Cash and cash equivalents	$ —	$ 1,572	$ 1,572	$ —
Securities held in lieu of surety bonds	368,346	80,945	79,373	369,918
Total assets	**$ 368,346**	**$ 82,517**	**$ 80,945**	**$ 369,918**
Liabilities:				
Deposits	$ 368,346	$ 80,944	$ 79,372	$ 369,918
Total liabilities	**$ 368,346**	**$ 80,944**	**$ 79,372**	**$ 369,918**
Payroll Clearing				
Assets:				
Cash and cash equivalents	$ 11,324	$ 1,087,435	$ 1,087,589	$ 11,170
Receivables	23	25	23	25
Due from other funds	51,781	46,524	51,781	46,524
Total assets	**$ 63,128**	**$ 1,133,984**	**$ 1,139,393**	**$ 57,719**
Liabilities:				
Accounts payable	$ 120	$ 170	$ 129	$ 161
Due to other funds	11,214	10,995	11,214	10,995
Amounts held in custody for others	51,794	926,126	931,357	46,563
Total liabilities	**$ 63,128**	**$ 937,291**	**$ 942,700**	**$ 57,719**
Property Tax Collection				
Assets:				
Cash and cash equivalents	$ 213,675	$ 1,793,140	$ 1,855,788	$ 151,027
Taxes receivable	15,469	85,869	87,497	13,841
Due from other funds	9,751	70,081	74,331	5,501
Investments	21,965	22,987	23,445	21,507
Securities held in lieu of surety bonds	—	165	—	165
Total assets	**$ 260,860**	**$ 1,972,242**	**$ 2,041,061**	**$ 192,041**
Liabilities:				
Accounts payable	$ 4,929	$ 12,112	$ 8,412	$ 8,629
Due to other funds	73,842	15	73,842	15
Due to other governments	182,089	1,523,384	1,522,076	183,397
Total liabilities	**$ 260,860**	**$ 1,535,511**	**$ 1,604,330**	**$ 192,041**
Total, All Agency Funds				
Assets:				
Cash and cash equivalents	$ 224,999	$ 2,882,147	$ 2,944,949	$ 162,197
Receivables	23	25	23	25
Taxes receivable	15,469	85,869	87,497	13,841
Due from other funds	61,532	116,605	126,112	52,025
Investments	21,965	22,987	23,445	21,507
Securities held in lieu of surety bonds	368,346	81,110	79,373	370,083
Total assets	**$ 692,334**	**$ 3,188,743**	**$ 3,261,399**	**$ 619,678**
Liabilities:				
Accounts payable	$ 5,049	$ 12,282	$ 8,541	$ 8,790
Due to other funds	85,056	11,010	85,056	11,010
Due to other governments	182,089	1,523,384	1,522,076	183,397
Deposits	368,346	80,944	79,372	369,918
Amounts held in custody for others	51,794	926,126	931,357	46,563
Total liabilities	**$ 692,334**	**$ 2,553,746**	**$ 2,626,402**	**$ 619,678**

Figure 82 Notes

① This statement is similar in form and function to the note disclosures of changes in capital assets (Figure 12) and long-term liabilities (Figure 16). NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements. Local City does not have more than one fund of any fiduciary fund classification.

② Additions increase the assets and liabilities of an agency fund, and include tax collections.

③ Deductions reduce assets and liabilities of an agency fund and primarily take the form of distributions to the governments or other persons or organizations to which the fund resources belong.

④ This column should match the agency fund column in the statement of fiduciary net position.

SUPPORTING INFORMATION RELATED TO FIDUCIARY FUNDS

Supporting information that is relevant to the fiduciary funds financial statements can be found in fund-type and individual fund statements.

Fund Classifications

Fiduciary funds are aggregated by classification in the fiduciary funds financial statements. For each fiduciary fund classification, the funds are shown individually in the following combining statements:

- Combining statement of fiduciary net position (Figure 80)
- Combining statement of changes in fiduciary net position (Figure 81).

An alternative presentation for agency funds is the combining statement of changes in assets and liabilities (Figure 82). This format is possible because the agency funds do not have net position.

Individual Funds

A government may use individual fund statements in order to demonstrate its compliance with a finance-related legal or contractual provision or to present comparisons with the prior reporting period.

What Can You Do with Supporting Information about Fiduciary Funds?

You can perform the same analyses and answer the same questions about fiduciary funds using their combining and individual financial statements as you can for the governmental and enterprise funds. The analytical interest in fiduciary funds often relates to a specific fund (for instance, a teachers retirement plan) rather than all of the funds of a particular type combined (aggregate numbers for all retirement plans, including the teachers plan). These combining and individual fund statements provide details that will not be found in the fiduciary funds financial statements, where there is no major fund

reporting. Individual funds generally will be found in the fiduciary funds statements if a government has just one fund of a particular classification.

Upon further review…a cash flow problem

A utility billed customers $100,000 for water during the year—these are its total revenues. It also had expenses of $95,000. On the whole, then, the utility had a surplus of $5,000 that increased net position. Unfortunately, only 80 percent of the utility's customers paid their bills during the year, while all of the expenses were due to be paid during the year. Despite balancing revenues and expenses, the utility had a *cash flow deficit* of $15,000 (cash inflows of $80,000 minus outflows of $95,000). It would be unusual for an entity to have enough cash on hand at the beginning of the year to pay *all* of its bills during the year. Consequently, (a) bills may go unpaid, (b) other assets may be sold to raise the necessary cash, or (c) short-term notes may be sold to cover the short-term cash flow problem, which the utility may not be able to repay.

Upon further review…classifications of fiduciary funds and their financial statements

There will be changes to the classification of funds reported in fiduciary fund financial statements starting in fiscal years ending December 31, 2019, and later. Accounting standards that take effect then will limit the use of the three trust fund classifications to reporting activities that are administered through a trust that meets criteria similar to those described in **Upon further review…criteria for pension and OPEB trusts** on page 105. All other fiduciary activities (including those previously reported as agency funds) will be reported in a new classification—custodial funds.

The new standards also will improve the information in the statement of changes in fiduciary net position. Perhaps most notably, custodial funds will appear in the statement, even if they do not have net position (such as the funds now called agency funds). Among their additions, governments will separately show (1) investment earnings, (2) investment costs, and (3) net investment earnings (1 minus 2) in fiduciary funds that have investments. Governments also will separately show administrative costs among the deductions.

If resources inflows are expected to be held for three months or less (as often is the case with agency funds), a government will be able to show a single aggregate amount for additions and a single aggregate amount for deductions, as long as the labels of those two amounts are sufficiently clear to communicate what they are.

PART ELEVEN

SPECIAL-PURPOSE GOVERNMENTS

The discussion of financial reporting thus far has centered mostly on *general purpose governments* (such as states, counties, and cities) and independent school districts. Many other governments can be described as *special-purpose governments*. In fact, of the roughly 90,100 state and local governments in the United States, almost 38,300 are special-purpose governments other than school districts.

Special-purpose governments are separate legal entities in their own right, although they may take the form of component units of other *stand-alone governments*. Governmental accounting standards provide guidance regarding the financial statements that special-purpose governments should prepare depending on the kinds of activities they are engaged in. Five distinct kinds of special-purpose governments can be discerned in this guidance:

- Special-purpose governments engaged in multiple governmental activities
- Special-purpose governments engaged in both governmental and business-type activities
- Special-purpose governments engaged in a single governmental program
- Special-purpose governments engaged only in BTAs, and
- Special-purpose governments engaged only in fiduciary activities.

An important contributor to the value of the annual financial report described thus far in this guide is the different but complementary information provided in the government-wide and fund financial statements. As long as the distinctions between the two kinds of statements provide meaningful and useful information about a government, the accounting standards require that both be prepared. Such is the case for governments in the first two categories above: preparing both government-wide and fund financial statements is valuable when there are multiple programs and when there are both governmental and business-type activities. (See **By the numbers…reporting by special-purpose governments** on page 268 for a concise presentation of the reporting requirements for each kind of special-purpose government.)

GOVERNMENTS ENGAGED ONLY IN BUSINESS-TYPE OR FIDUCIARY ACTIVITIES

When it comes to the other three kinds of special-purpose governments (categories 3–5 on the preceding page), the potential benefits of preparing both types of financial statements are less apparent. In most instances, BTAs are synonymous with enterprise funds, so it is unlikely that preparing both government-wide and proprietary funds statements would be beneficial to the financial statement user. These special-purpose governments prepare the three proprietary funds statements, notes, and RSI (including MD&A). They also may present fiduciary funds statements if they engage in fiduciary activities, such as sponsoring an employee pension fund. (Another edition in the GASB User Guide Series is devoted

entirely to these types of governments—*What You Should Know about the Finances of Your Government's Business-Type Activities: A Guide to Financial Statements*.)

If a special-purpose government is engaged only in fiduciary activities, which are not reported in the government-wide statements, it is not logical for such a government to prepare the government-wide statements. Instead, it prepares at a minimum the two fiduciary funds statements, notes, and RSI (including MD&A).

By the numbers...reporting by special-purpose governments

Kind of Special-Purpose Government	Required Financial Statements
1. Engaged in multiple governmental activities	All applicable basic financial statements (including notes) and RSI
2. Engaged in both governmental and business-type activities	All applicable basic financial statements (including notes) and RSI
3. Engaged in a single governmental program	Combined government-wide and fund financial statements, using a columnar format to reconcile the financial data on the face of the statement (see Figures 85–87), plus notes to financial statements and applicable RSI OR Separate government-wide and fund financial statements, but employing a different format for the statement of activities (see Figures 83 and 84), plus notes to financial statements and applicable RSI
4. Engaged only in BTAs	The three proprietary funds financial statements, plus notes to financial statements and applicable RSI
5. Engaged only in fiduciary activities	The two fiduciary funds financial statements, plus notes to financial statements and applicable RSI

GOVERNMENTS ENGAGED IN A SINGLE GOVERNMENTAL PROGRAM

Examples of special-purpose governments engaged in a single governmental program include fire protection districts, cemetery districts, assessment districts, mosquito abatement districts, and drainage districts. For such governments, it still is valuable to have both the comprehensive financial information of the governmental activities in the government-wide statements *and* the predominantly short-term information in the governmental funds statements. However, because there is only a single program, the format of some of the financial statements may seem awkward.

With this in mind, the accounting standards allow these kinds of governments to employ alternative forms of presentation that involve either:

- Preparing separate government-wide and fund financial statements, but using a different format for the statement of activities, OR
- Combining the government-wide and fund financial statements using a columnar format that reconciles the two kinds of financial data in a separate column on each statement.

Figures 83 and 84 are examples of what the statement of net position and statement of activities might look like for this kind of special-purpose government, if it chose to prepare separate government-wide and fund statements. If this kind of special-purpose government decides to combine the government-wide and fund statements, it would prepare a balance sheet/statement of net position that looks something like Figure 85. Its combined statement of revenues, expenditures, and changes in fund balances/statement of activities might look like either Figure 86 (which presents a statement of activities format) or Figure 87 (which is more like a fund statement format).

Figure 83. Statement of Net Position for a Single-Program Government (Single-Column Presentation)

Shelbydover Fire Protection District
Statement of Net Position
As of May 31, 2017

ASSETS	
Cash and investments	$ 7,716,749
Taxes receivable	1,480,536
Other receivables	574,481
Prepaid expenses	7,763
Inventories	197,308
Capital assets, net of accumulated depreciation, where applicable:	
Land	301,576
Buildings and improvements	3,311,094
Fire apparatus—automotive	907,482
Furniture, fixtures, and equipment	911,754
Total capital assets, net	5,431,906
Total assets	15,408,743
DEFERRED OUTFLOWS OF RESOURCES	87,300
LIABILITIES	
Accounts payable	106,999
Salaries and benefits payable	273,367
Accrued interest payable	1,511
Payments received in advance	273,746
Compensated absences:	
Payable within one year	300,182
Payable after one year	200,601
Bonds and notes payable:	
Portion due within one year	235,453
Portion due after one year	3,195,905
Total liabilities	4,587,764
DEFERRED INFLOWS OF RESOURCES	101,020
NET POSITION	
Net investment in capital assets	2,000,548
Restricted for debt service	468,167
Unrestricted	8,338,544
Total net position	$ 10,807,259

Figure 84. Statement of Activities for a Single-Program Government (Single-Column Presentation)

Shelbydover Fire Protection District
Statement of Activities
for the Year Ended May 31, 2017

Expenses:	
Public safety—fire protection:	
Personal services	$ 9,440,023
Materials and services	1,250,788
Depreciation	306,623
Interest	205,779
Total program expenses	11,203,213
Program revenues:	
Charges for services	622,590
Net program expense	10,580,623
General revenues:	
Property taxes	11,412,154
Investment earnings	597,661
Miscellaneous	29,245
Total general revenues	12,039,060
Change in net position	1,458,437
Net position—beginning of the year	9,348,822
Net position—end of the year	$10,807,259

Figure 85. Balance Sheet and Statement of Net Position for a Single-Program Government (Combined Presentation)

Shelbydover Fire Protection District
Governmental Funds Balance Sheet/Statement of Net Position
for the Year Ended May 31, 2017

	General Fund	Other Funds	Total	① Adjustments (Note D)	Statement of Net Position
ASSETS					
Cash and investments	$ 6,505,557	$ 1,211,192	$ 7,716,749	$ —	$ 7,716,749
Taxes receivable	1,427,885	52,651	1,480,536	—	1,480,536
Other receivables	567,607	6,874	574,481	—	574,481
Internal receivables	—	12,293	12,293	(12,293)	—
Prepayments	7,763	—	7,763	—	7,763
Inventories	197,308	—	197,308	—	197,308
Capital assets, net of accumulated depreciation	—	—	—	5,431,906	5,431,906
Total assets	8,706,120	1,283,010	9,989,130	5,419,613	15,408,743
DEFERRED OUTFLOWS OF RESOURCES	—	—	—	87,300	87,300
Total assets and deferred outflows of resources	$ 8,706,120	$ 1,283,010	$ 9,989,130		
LIABILITIES					
Accounts payable	$ 73,828	$ 33,171	$ 106,999	—	106,999
Salaries and benefits payable	273,367	—	273,367	—	273,367
Accrued interest payable	—	1,294	1,294	217	1,511
Internal payables	12,293	—	12,293	(12,293)	—
Payments received in advance	230,955	42,791	273,746	—	273,746
Long-term liabilities:					
Due within one year	—	—	—	535,635	535,635
Due after one year	—	—	—	3,396,506	3,396,506
Total liabilities	590,443	77,256	667,699	3,920,065	4,587,764
DEFERRED INFLOWS OF RESOURCES	1,303,366	—	1,303,366	(1,202,346)	101,020
FUND BALANCES/NET POSITION					
Fund balances:					
Nonspendable: Inventories	197,308	—	197,308	(197,308)	—
Unassigned	6,615,003	1,205,754	7,820,757	(7,820,757)	—
Total fund balances	6,812,311	1,205,754	8,018,065	(8,018,065)	—
Total liabilities, deferred inflows of resources, and fund balances	$ 8,706,120	$ 1,283,010	$ 9,989,130		
Net position:					
Net investment in capital assets				2,000,548	2,000,548
Restricted for debt service				468,167	468,167
Unrestricted				8,338,544	8,338,544
Total net position				$ 10,807,259	$ 10,807,259

Figure 86. Statement of Revenues, Expenditures, and Changes in Fund Balances and Statement of Activities for a Single-Program Government (Combined Presentation and Statement of Activities Format)

Shelbydover Fire Protection District
Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances/Statement of Activities
for the Year Ended May 31, 2017

	General Fund	Other Funds	Total	① Adjustments (Note D)	Statement of Activities
Expenditures/expenses:					
Fire protection—operations	$ 10,684,793	$ —	$ 10,684,793	$ 312,641	$ 10,997,434
Capital outlay	76,090	219,175	295,265	(295,265)	—
Debt service:					
Principal	5,452	220,000	225,452	(225,452)	—
Interest	1,534	204,028	205,562	217	205,779
Total expenditures/expenses	10,767,869	643,203	11,411,072	(207,859)	11,203,213
Program revenues:					
Charges for services	622,590	—	622,590	—	622,590
Net program expense					10,580,623
General revenues:					
Property taxes	10,750,111	391,442	11,141,553	270,601	11,412,154
Investment earnings	526,079	71,582	597,661	—	597,661
Miscellaneous	29,245	—	29,245	—	29,245
Transfers—internal activities	(500,000)	500,000	—	—	—
Total general revenues and transfers	10,805,435	963,024	11,768,459	270,601	12,039,060
Excess of revenues and transfers in over expenditures and transfers out	660,156	319,821	979,977	(979,977)	—
Change in net position	—	—	—	1,458,437	1,458,437
Fund balance/net position:					
Beginning of the year	8,045,964	963,189	9,009,153	339,669	9,348,822
End of the year	$ 8,706,120	$ 1,283,010	$ 9,989,130	$ 818,129	$ 10,807,259

Figure 87. Statement of Revenues, Expenditures, and Changes in Fund Balances and Statement of Activities for a Single-Program Government (Combined Presentation and Fund Statement Format)

Shelbydover Fire Protection District
Government Funds Statement of Revenues, Expenditures, and Changes in Fund Balances/Statement of Activities
for the Year Ended May 31, 2017

	General Fund	Other Funds	Total	① Adjustments (Note D)	Statement of Activities
Revenues:					
Property taxes	$ 10,750,111	$ 391,442	$ 11,141,553	$ 270,601	$ 11,412,154
Investment earnings	526,079	71,582	597,661	—	597,661
Charges for services	622,590	—	622,590	—	622,590
Miscellaneous	29,245	—	29,245	—	29,245
Total revenues	11,928,025	463,024	12,391,049	270,601	12,661,650
Expenditures/expenses:					
Current:					
Personal services	9,434,005	—	9,434,005	6,018	9,440,023
Materials and services	1,250,788	—	1,250,788	—	1,250,788
Depreciation	—	—	—	306,623	306,623
Capital outlay	76,090	219,175	295,265	(295,265)	—
Debt service:					
Principal	5,452	220,000	225,452	(225,452)	—
Interest	1,534	204,028	205,562	217	205,779
Total expenditures/expenses	10,767,869	643,203	11,411,072	(207,859)	11,203,213
Excess (deficiency) of revenues over expenditures	1,160,156	(180,179)	979,977	478,460	—
Other financing sources/uses:					
Transfers—internal activities	(500,000)	500,000	—	—	—
Excess (deficiency) of revenues and transfers in over expenditures and transfers out	660,156	319,821	979,977	(979,977)	—
Change in net position	—	—	—	1,458,437	1,458,437
Fund balances/net position:					
Beginning of the year	8,045,964	963,189	9,009,153	339,669	9,348,822
End of the year	$ 8,706,120	$ 1,283,010	$ 9,989,130	$ 818,129	$ 10,807,259

PUBLIC COLLEGE AND UNIVERSITY FINANCIAL STATEMENTS

Colleges and universities that are legally separate governmental entities are special-purpose governments and they apply the guidance just discussed. The accounting standards make a basic assumption that there are no public colleges and universities that engage solely in fiduciary activities or only in governmental programs (single or multiple). Virtually every public college and university engages in some kind of BTA, whether it be operating a bookstore, dormitories, student unions, or food services. As a consequence, the decision regarding what financial statements to prepare boils down to whether the public institution:

- Reports both governmental activities *and* BTAs, OR

- Reports only BTAs.

In the former instance, the public college or university would prepare the same set of basic financial statements—the two government-wide statements and the governmental, proprietary, and fiduciary funds statements—including notes and applicable RSI (including MD&A) as a general purpose government. A sample set of financial statements for a community college engaged in both governmental activities and BTAs may be found in Appendix D. (Note that this community college does not engage in any fiduciary activities; therefore, no fiduciary funds statements are presented.)

Public colleges and universities that report only as BTAs prepare applicable RSI, including MD&A, and the three proprietary funds financial statements (plus notes):

- Statement of net position (illustrated for a public university in Figure 88)
- Statement of revenues, expenses, and changes in fund net position (Figure 89)
- Statement of cash flows (Figure 90).

Deciding which of these circumstances is applicable is a matter of the professional judgment of the institution's finance officers. The crux of the decision is how the institution classifies its basic educational activities. Public colleges and universities generally charge some tuition to students, which bears a resemblance to a BTA. However, public higher education generally is subsidized by tax-financed operating support, primarily from the federal and state governments; in this way, public colleges and universities appear to be like governmental activities. This situation is similar to that of public mass transit, which generally charges a fare to riders, but in an amount that frequently is not sufficient to cover the transit system's costs; rather, mass transit systems also are subsidized. (See page 161.) An example that is easier to categorize is a community college that has the authority to levy a property tax to finance its activities; such an entity may be engaged in one or more governmental activities based on its method of financing.

Figure 88. Statement of Net Position for a College or University Engaged Only in Business-Type Activities

Price-Kathryn University
Statement of Net Position
As of June 30, 2017

	Primary Institution	① Component Unit Hospital
ASSETS		
Current assets:		
Cash and cash equivalents	$ 4,571,218	$ 977,694
Short-term investments	15,278,981	2,248,884
Accounts receivable, net	6,412,520	9,529,196
Inventories	585,874	1,268,045
Deposit with bond trustee	4,254,341	—
Notes and mortgages receivable, net	359,175	—
Other assets	432,263	426,427
Total current assets	31,894,372	14,450,246
Noncurrent assets:		
Restricted cash and cash equivalents	24,200	18,500
Endowment investments	21,548,723	—
Notes and mortgages receivable, net	2,035,323	—
Other long-term investments	—	6,441,710
Investments in real estate	6,426,555	—
Capital assets, net	158,977,329	32,602,940
Total noncurrent assets	189,012,130	39,063,150
Total assets	220,906,502	53,513,396
DEFERRED OUTFLOWS OF RESOURCES	2,528,914	175,539
LIABILITIES		
Current liabilities:		
Accounts payable and accrued liabilities	4,897,470	2,911,419
Unearned revenue	3,070,213	—
Long-term liabilities—current portion	4,082,486	989,321
Total current liabilities	12,050,169	3,900,740
Noncurrent liabilities:		
Deposits	1,124,128	—
Advances	1,500,000	—
Long-term liabilities	31,611,427	2,194,236
Total noncurrent liabilities	34,235,555	2,194,236
Total liabilities	46,285,724	6,094,976
DEFERRED INFLOWS OF RESOURCES	1,896,686	131,654
NET POSITION		
Net investment in capital assets	126,861,400	32,199,938
Restricted for:		
Nonexpendable: ②		
Scholarships and fellowships	10,839,473	—
Research	3,767,564	2,286,865
Expendable:		
Scholarships and fellowships	2,803,756	—
Research	5,202,732	—
Instructional department uses	938,571	—
Loans	2,417,101	—
Capital projects	4,952,101	913,758
Debt service	4,254,341	152,947
Other	403,632	—
Unrestricted	12,812,336	11,908,797
Total net position	$ 175,253,007	$ 47,462,305

Figure 89. Statement of Revenues, Expenses, and Changes in Net Position for a College or University Engaged Only in Business-Type Activities

Price-Kathryn University
Statement of Revenues, Expenses, and Changes in Net Position
for the Year Ended June 30, 2017

	Primary Institution	Component Unit Hospital
REVENUES		
Operating revenues:		
Student tuition and fees (net of scholarship allowances of $3,214,454) ①	$ 36,913,194	$ —
Patient services (net of provision for bad debt of $5,114,352)	—	46,296,957
Intergovernmental contracts	10,614,660	—
Nongovernmental contracts	3,036,953	7,475,987
Sales and services of educational departments	873,740	—
Auxiliary enterprises:	19,802	—
Residential life (net of scholarship allowances of $428,641)	28,079,274	—
Bookstore (net of scholarship allowances of $166,279)	9,092,363	—
Other operating revenues	143,357	421,571
Total operating revenues	88,773,343	54,194,515
EXPENSES		
Operating expenses:		
Salaries:		
Faculty (physicians for the hospital)	34,829,499	16,703,805
Exempt staff	29,597,676	8,209,882
Nonexempt wages	5,913,762	2,065,267
Benefits	18,486,559	7,752,067
Scholarships and fellowships	3,809,374	—
Utilities	16,463,492	9,121,352
Supplies and other services	12,451,064	7,342,009
Depreciation	6,847,377	2,976,212
Total operating expenses	128,398,803	54,170,594
Operating income (loss)	(39,625,460)	23,921
NONOPERATING REVENUES (EXPENSES)		
State appropriations ②	39,760,508	—
Gifts	1,822,442	—
Investment income (net of investment expense of $87,316 for the primary institution and $19,823 for the hospital) ③	2,182,921	495,594
Interest on capital asset-related debt	(1,330,126)	(34,538)
Other nonoperating revenues	313,001	321,449
Net nonoperating revenues	42,748,746	782,505
Income before other revenues, expenses, gains, or losses	3,123,286	806,426
Capital contributions	2,766,563	711,619
Additions to permanent endowments	85,203	—
Increase in net position	5,975,052	1,518,045
NET POSITION		
Net position—beginning of year	169,277,955	45,944,260
Net position—end of year	$ 175,253,007	$ 47,462,305

Figure 90. Statement of Cash Flows for a College or University Engaged Only in Business-Type Activities

Price-Kathryn University
Statement of Cash Flows
for the Year Ended June 30, 2017

	Primary Institution	Component Unit Hospital
CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	$ 33,628,945	$ —
Research grants and contracts	13,884,747	—
Payments from insurance and patients	—	18,582,530
Medicaid and Medicare	—	31,640,524
Payments to suppliers	(28,175,500)	(13,084,643)
Payments to employees	(87,233,881)	(32,988,044)
Loans issued to students and employees	(384,628)	—
Collection of loans to students	291,642	—
Auxiliary enterprise charges:		
Residence halls	26,327,644	—
Bookstore	8,463,939	—
Other receipts (payments)	1,415,502	(997,502)
Net cash provided (used) by operating activities	(31,781,590)	3,152,865
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	39,473,737	—
Net cash flows provided by noncapital financing activities	39,473,737	—
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt	4,125,000	—
Capital appropriations	1,918,750	—
Capital grants and gifts received	640,813	711,619
Proceeds from sale of capital assets	22,335	5,066
Purchases of capital assets	(8,420,247)	(1,950,410)
Principal paid on capital debt and lease	(3,788,102)	(134,095)
Interest paid on capital debt and lease	(1,330,126)	(34,538)
Net cash used by capital and related financing activities	(6,831,577)	(1,402,358)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	16,741,252	2,843,124
Interest on investments	2,111,597	70,501
Purchases of investments	(17,680,113)	(4,546,278)
Net cash provided (used) by investing activities	1,172,736	(1,632,653)
Net increase in cash	2,033,306	117,854
Cash—beginning of year	2,562,112	878,340
Cash—end of year	① $ 4,595,418	$ 996,194

Figure 90. Statement of Cash Flows for a College or University Engaged Only in Business-Type Activities (continued)

Reconciliation of net operating revenues (expenses) to net cash provided (used) by operating activities:			
Operating income (loss)	$ (39,625,460)	$	23,921
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:			
Depreciation expense	6,847,377		2,976,212
Change in assets and liabilities:			
Receivables, net	1,295,704		330,414
Inventories	37,284		(160,922)
Deposit with bond trustee	67,115		—
Other assets	(136,229)		75,456
Accounts payable	(323,989)		(75,973)
Unearned revenue	217,630		—
Deposits held for others	(299,428)		—
Compensated absences	138,406		(16,243)
Net cash provided (used) by operating activities ②	$ (31,781,590)	$	3,152,865

Figure 88 Notes

① This university has a discretely presented component unit, a hospital, which it is required to show in a separate column.

② If net position includes permanent endowments or permanent funds, restricted net position is divided between *expendable* and *nonexpendable,* the latter of which represents the corpus or principal that must be maintained intact and not spent.

Figure 89 Notes

① Colleges and universities often show the amount of scholarship funding that is subtracted from a total revenue amount. The portion of gross revenues coming from scholarship money is deducted because the institution itself is providing that money to the students and does not count its own scholarships as revenue.

② State appropriations represent general financial support provided to the university by the state government. Intergovernmental aid that is received from a government for specific services provided to the government—for example, a contract that will result in a product being provided to the other government—is presented with the operating revenues.

③ Investment income is reported net of the cost of investing—investment expense—though governments are not required to show the netted amounts on the face of the financial statement.

Figure 90 Notes

① These end-of-year cash amounts should be the same as the combination of the amounts reported in the statement of net position (see Figure 88) for unrestricted and restricted cash.

② This university either did not have any noncash investing, capital, or financing activities that affected assets and liabilities, or it presented them separately from the cash flows statement.

PART TWELVE

ENTITIES RELATED TO A GOVERNMENT

A government's financial statements may give you some clues about how the government is organized and the activities it engages in, but generally in broad strokes. The organizational chart in the introductory section of the CAFR should be helpful, as well as the operating information (discussed in Part Thirteen) found in the statistical section. The SSAP contains several descriptions that should help you understand what the various columns in the financial statements mean. For each major fund, the internal service funds, and each fiduciary fund classification reported in a government's financial statements, the SSAP identifies the activities they include. As mentioned in Part Nine, the purpose of each of the major special revenue funds is described in the notes.

The SSAP also describes a government's component units, both those whose financial information is *blended* (combined) with the governmental and business-type activities and those that are *discretely presented* (shown in a separate column) in the government-wide financial statements. The descriptions should include the nature of the component units' relationships with the government, the reasons why the government included the component units (in other words, which criteria in the accounting standards led to the conclusion), and why it was required to blend them or present them discretely (again, citing the specific criteria).

A government also provides more detailed information about its discretely presented component units and blended components, and other entities it has a relationship with, in notes to financial statements and supporting information.

WHAT'S AHEAD?

- WHAT ORGANIZATIONS IS A GOVERNMENT FINANCIALLY ACCOUNTABLE FOR?
- WHAT OTHER ORGANIZATIONS ARE RELATED TO A GOVERNMENT?

COMPONENT UNITS

A government's reporting entity encompasses its governmental activities, BTAs, and component units. Component units are legally separate organizations, predominately governmental, for which the elected officials of a government are financially accountable. Colleges and universities are common component units of state governments. School districts sometimes are component units of local governments. Other activities that frequently are established as component units include water, sewer, and electric services; economic development; construction finance; housing; toll roads; and mass transit.

A government's component units may prepare and release to the public their own audited financial statements. But the ultimate financial responsibility that a government bears for its component units requires that they also be reported in statements of the government. Even if a separate organization does not meet the criteria that demonstrate the government is financially accountable for it, the organization may be included as a component unit if the nature and significance of its relationship with the government are such that excluding the organization would cause the government's financial statements to be misleading. The SSAP tells you why the government has included the component units, as well as how to obtain their separately issued financial reports, if available.

Usually, you will find discretely presented component units totaled in a single column in the government-wide statements of net position and activities (though some governments do show component units individually). If the component units are combined in the government-wide statements, you can find additional information regarding the component units in one of two forms:

- Combining financial statements of major component units, appearing between the fund financial statements and the notes (Figures 91 and 92), OR
- Condensed financial statements in the notes to financial statements (Figure 93).

(An explanation of what constitutes a *major* component unit can be found in **By the numbers…major component units.**)

Individual BLENDED COMPONENT UNITS (those that are included within the governmental and business-type activities columns) are reported in combining statements as if they were an activity of the primary government. The criteria that determine that a component unit should be blended rather than discretely presented can be found on page 283 in **Upon further review…how component units are shown.**

As their name suggests, condensed statements are a boiled-down version of the complete financial information that component units present in their own audited financial statements. This approach is illustrated in Figure 93, a note that includes condensed statements of net position and activities. That illustration presents the minimum required information that a government is required to disclose in condensed statements; a government may present more detailed information if it wishes.

What Can You Do with Component Unit Information?

The information in the component unit statements is no different from the information in the other statements of net position and statements of activities. The statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Consequently, the component unit statements are amenable to the same kinds of analyses one might apply to the government-wide and proprietary funds financial statements. The decision about whether or not to use the component unit statements and the information they contain depends on your individual information needs and the circumstances of each government. For instance, they can be particularly useful for analysts interested in bonds sold to finance the projects of a particular component unit, such as a redevelopment agency

that secures its bonds with incremental property tax revenues from the geographic area the agency covers.

Upon further review…how component units are shown

Most of the time, a government shows its component units in a separate column in the government-wide financial statements. This is called *discrete presentation.* However, some component units are so intertwined with a government that they are instead *blended* (combined) with the governmental and business-type activities. A government will blend a component unit in *any* of the following four circumstances:

- The component unit's total debt outstanding is expected to be repaid with the government's resources.
- The component unit provides service exclusively or almost exclusively to the government, like an internal service fund.
- The component unit's governing body is substantively the same as the governing body of the government *and* one or both of the following is true:
  - The component unit represents a financial benefit or burden to the government
  - The government effectively operates the component unit as if it were a department or program of the government.
- The component unit is a not-for-profit corporation in which the government is the sole corporate member.

As with its discretely presented component units, a government presents individual blended component units that it considers major in combining or condensed financial statements. (See By the numbers…major component units.)

Figure 91. Combining Statement of Net Position, Major Component Units

Local City
Combining Statement of Net Position ①
Component Units
As of December 31, 2017

	Local Public School District ②	Local City Landfill Authority	③ Total
ASSETS			
Cash and cash equivalents	$ 303,485	$ 450	$ 303,935
Investments	3,658,520	1,770,432	5,428,952
Receivables, net	3,717,026	325,264	4,042,290
Inventories	83,697	—	83,697
Restricted assets—landfill closure ④	—	2,000,000	2,000,000
Capital assets, net	34,759,986	2,984,800	37,744,786
Total assets	42,522,714	7,080,946	49,603,660
DEFERRED OUTFLOWS OF RESOURCES			
Pensions	1,339,299	148,811	1,488,110
Retiree health insurance	803,579	89,287	892,866
Accumulated decrease in fair value of hedging derivatives	—	2,987,635	2,987,635
Total deferred outflows of resources	2,142,878	3,225,733	5,368,611
LIABILITIES			
Accounts payable ⑤	4,311,870	479,097	4,790,967
Long-term liabilities:			
Due within one year	1,426,639	—	1,426,639
Due in more than one year	36,810,520	6,168,802	42,979,322
Total liabilities	42,549,029	6,647,899	49,196,928
DEFERRED INFLOWS OF RESOURCES			
Pensions	625,006	69,445	694,451
Retiree health insurance	375,004	41,667	416,671
Total deferred inflows of resources	1,000,010	111,112	1,111,122
NET POSITION			
Net investment in capital assets	12,921,592	2,984,800	15,906,392
Restricted for capital projects	492,445	—	492,445
Unrestricted	(12,297,484)	562,868	(11,734,616)
Total net position	$ 1,116,553	$ 3,547,668	$ 4,664,221

Figure 91 Notes

① In addition to the information in the combining statements or notes (see Figures 92 and 93), a government discloses in the notes to the financial statements the nature and amount of significant transactions between each major component unit and the primary government or other component units. See **By the numbers…financial activity between component units** on page 283.

② This combining statement presents the *major* component units.

③ The total column information appears in the government-wide statement of net position, but in a classified format. (See Figure 1.)

④ These investments may be used under state law only for the purpose of closing the landfill and caring for it afterward. That is why they are labeled as restricted.

⑤ This illustrative statement does not use the classified format, though it may; these amounts are shown together instead of separately in current and noncurrent liabilities.

Figure 92 Notes

① More information about the workings of a statement of activities can be found in the notes to Figure 42 and Part Seven.

② This section of the total column is identical to the component units column in the government-wide statement of activities (Figure 42).

③ In addition to the information in the combining statements or notes (see Figures 91 and 93), a government discloses in the notes to the financial statements the nature and amount of significant transactions between each major component unit and the primary government. See **By the numbers…financial activity between component units** on page 283.

Figure 93 Notes

① If a government does not display major component units in separate columns in the government-wide statements or prepare combining statements (Figures 91 and 92) for them, it presents this note disclosure instead.

② This illustration presents the minimum information required by accounting standards; a government may provide additional information.

③ In addition to the information in the combining statements or notes, a government discloses in the notes to the financial statements the nature and amount of significant transactions between each major component unit and the primary government or other component units. See **By the numbers…financial activity between component units** on page 283.

Figure 92. Combining Statement of Activities, Major Component Units

Local City
Combining Statement of Activities ①
Component Units
for the Year Ended December 31, 2017

		Program Revenues			Net (Expense) Revenue		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	School District	Landfill Authority	Total
Local Public School District							
Instructional	$ 16,924,321	$ 147,739	$ 2,825,109	$ —	$ (13,951,473)	$ —	$ (13,951,473)
Support services	7,972,559	300	751,711	—	(7,220,548)	—	(7,220,548)
Operation of noninstructional services	1,523,340	557,726	359,092	—	(606,522)	—	(606,522)
Facilities acquisition and construction services	48,136	—	1,171	—	(46,965)	—	(46,965)
Interest on long-term debt	546,382	—	—	—	(546,382)	—	(546,382)
Unallocated depreciation	4,171,760	—	—	—	(4,171,760)	—	(4,171,760)
Total—Local Public School District	31,186,498	705,765	3,937,083	—	(26,543,650)	—	—
Local City Landfill Authority							
Landfill operations	3,382,157	3,857,858	—	11,397	—	487,098	487,098
Total component units	$ 34,568,655	$ 4,563,623	$ 3,937,083	$ 11,397			(26,056,552)
							②
	General revenues:						
	Payment from Local City				21,893,273	—	21,893,273
	Grants, entitlements, and contributions not restricted to specific programs				6,461,708	—	6,461,708
	Investment earnings				674,036	207,727	881,763
	Miscellaneous				19,950	2,514	22,464
③	Total general revenues				29,048,967	210,241	29,259,208
	Change in net position				2,505,317	697,339	3,202,656
	Net position—beginning				(1,388,764)	2,850,329	1,461,565
	Net position—ending				$ 1,116,553	$ 3,547,668	$ 4,664,221

Figure 93. Condensed Statements of Net Position and Activities, Major Component Units

①

Condensed Statement of Net Position

	Local Public School District	Local City Landfill Authority	Total Component Units
Assets:			
Cash, investments, and other assets	$ 7,762,728	$ 4,096,146	$ 11,858,874
Capital assets, net	34,759,986	2,984,800	37,744,786
Total assets	42,522,714	7,080,946	49,603,660
Deferred outflows of resources	2,142,878	3,225,733	5,368,611
Liabilities:			
Accounts payable	4,311,870	479,097	4,790,967
Long-term liabilities	38,237,159	6,168,802	44,405,961
Total liabilities	42,549,029	6,647,899	49,196,928
Net position:			
Net investment in capital assets	12,921,592	2,984,800	15,906,392
Restricted	492,445	—	492,445
Unrestricted (deficit)	(12,297,484)	562,868	(11,734,616)
Total net position	$ 1,116,553	$ 3,547,668	$ 4,664,221

②

Condensed Statement of Activities

		Program Revenues			Net (Expense) Revenue and Changes in Net Position		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	School District	Landfill Authority	Total
Local Public School District							
Instructional	$ 16,924,321	$ 147,739	$ 2,825,109	$ —	$ (13,951,473)	$ —	$ (13,951,473)
Support services	7,972,559	300	751,711	—	(7,220,548)	—	(7,220,548)
Operation of noninstructional services	1,523,340	557,726	359,092	—	(606,522)	—	(606,522)
Facilities acquisition and construction services	48,136	—	1,171	—	(46,965)	—	(46,965)
Interest on long-term debt	546,382	—	—	—	(546,382)	—	(546,382)
Unallocated depreciation	4,171,760	—	—	—	(4,171,760)	—	(4,171,760)
Total—Local Public School District	31,186,498	705,765	3,937,083	—	(26,543,650)	—	—
Local City Landfill Authority							
Waste disposal operations	3,382,157	3,857,858	—	11,397	—	487,098	487,098
Total component units	$ 34,568,655	$ 4,563,623	$ 3,937,083	$ 11,397			(26,056,552)
General revenues:							
Payment from Local City					21,893,273	—	21,893,273
③ Grants, entitlements, and contributions not restricted to specific programs					6,461,708	—	6,461,708
Other general revenues					693,986	210,241	904,227
Total general revenues					29,048,967	210,241	29,259,208
Change in net assets					2,505,317	697,339	3,202,656
Net position—beginning					(1,388,764)	2,850,329	1,461,565
Net position—ending					$ 1,116,553	$ 3,547,668	$ 4,664,221

RELATED ORGANIZATIONS, JOINT VENTURES, AND JOINTLY GOVERNED ORGANIZATIONS

There are entities that a government is involved in, and may even appoint the leaders of, but which do not qualify as component units. Consequently, they are not included in the government's financial statements. If a government appoints the majority of the board of an organization, but is not financially accountable for it, that organization is called a RELATED ORGANIZATION. Because there is no financial accountability and it generally would not be misleading to exclude them from the government's financial statements, such organizations are not included. However, a government discloses the existence of these organizations in the notes to financial statements (often in the SSAP) and the nature of its accountability for them. The government in the SSAP in Figure E-2 discloses two organizations for which it appoints the board members—a fine arts league and an historical society.

Sometimes multiple governments band together to create a separate governmental entity to provide services to their citizens. For example, several neighboring governments might create a regional sewerage district that provides sewage treatment services to those jurisdictions. If the governments that created this legally separate entity share control of it and retain an ongoing financial interest in or responsibility for the entity, it is known as a JOINT VENTURE. (The city government in the SSAP is involved in a joint venture with its county government to operate a zoo.) "Financial interest" entails some sort of access to the entity's resources, such as receiving payments from the entity's surpluses, owning stock or shares in the entity (an "equity interest"), or benefiting from the projects the entity undertakes. (If a government has an equity interest in a joint venture, it reports that portion of the joint venture organization that it owns as an asset in its financial statements.) "Financial responsibility" could mean that the creating governments are obligated in some way for the entity's debt, or that the entity requires continued funding from the governments. The financial involvement of the governments in the entity is key, because if the governments share control of the entity but do not retain financial interest or responsibility, it is considered a JOINTLY GOVERNED ORGANIZATION.

If a government is involved in a joint venture, it provides in the notes a general description of the venture, including what its ongoing financial involvement is, whether separate financial statements are available for the entity, and any transactions it had with the entity. If there is no financial involvement, a government need only disclose any transactions that occurred with the jointly governed organization.

What Can You Do with This Information?

To the extent that a government is in some manner involved with other organizations that are not reported in the government's financial statements, you might need information about those organizations to assess what financial impact they could have, if any, on the government. If an entity or organization is experiencing financial difficulties, you should know if the government will in any way be responsible for assisting it—by repaying its debt, for instance, or providing it with additional resources.

Such an organization would be competing for the same scarce resources that the government needs to provide its own services. On the other hand, if the organization has accumulated resources that the government can obtain or has a right to receive, you would want to know about that, too. Such resources might allow the government to provide new or additional services, or make needed capital investments, or address its own financial problems.

PART THIRTEEN

OTHER INFORMATION

This section of the guide discusses some of the more significant notes and supporting information that do not fit into the categories of information covered in the preceding chapters. Topics include technical accounting issues such as prior-period adjustments, accounting changes, corrections of errors, going concern, and subsequent events, as well as legal compliance, municipal bankruptcy, demographic and economic information, and operating information.

WHAT'S AHEAD?

- HAS A GOVERNMENT MADE REVISIONS TO INFORMATION IN PREVIOUSLY ISSUED FINANCIAL STATEMENTS? WHY?
- IS THERE ANY REASON TO QUESTION THE CONTINUING FINANCIAL VIABILITY OF A GOVERNMENT?
- DID ANYTHING HAPPEN AFTER THE FISCAL YEAR THAT WILL HAVE AN IMPACT ON A GOVERNMENT'S FINANCES?

PRIOR-PERIOD ADJUSTMENTS: CORRECTIONS OF ERRORS AND ACCOUNTING CHANGES

Generally, there are two reasons that a government would need to revise amounts in a prior year's financial statements—to correct an error or to implement a change in how something is accounted for. CORRECTIONS OF ERRORS involve resolving a mistake (for instance, the government's finance officers were unaware of a relevant fact or a provision of GAAP was incorrectly applied) made in the preparation of the financial statements of an earlier year.

Two kinds of ACCOUNTING CHANGES result in adjustments of the financial statements for previous years—CHANGES IN ACCOUNTING PRINCIPLE and CHANGES IN THE REPORTING ENTITY. A change in accounting principle means that a government applied one provision of GAAP in one year and then applied a different provision the next year. A common change in accounting principle involves implementing new accounting standards for a particular transaction. Other changes in accounting principle relate to standards that give a government a choice, such as how to measure the value of inventory or the method for depreciating the historical cost of capital assets. For instance, if a government switches from the last-in-first-out method for valuing inventory to first-in-first-out, that is a change in accounting principle.

As described in Part Twelve, the reporting entity describes the extent of the government that is covered by the financial statements—the primary government (governmental activities and BTAs, including blended component units) and its discretely presented component units. A change in reporting entity involves a new organization being added to the reporting entity or a previously included organization no longer being included. For instance, a new component unit might have been created or acquired.

Consequently, the reporting entity now encompassed by the financial statements is not the same reporting entity covered in preceding years.

To address error corrections and accounting changes, governments make **PRIOR-PERIOD ADJUSTMENTS** in their financial statements. For all types of prior-period adjustments, a government adjusts the beginning balance of net position in the current year's statement of net position. If financial statements for more than one year are presented, the statements of financial position (including the governmental funds balance sheet) and flows statements (statement of activities, statement of revenues, expenditures, and changes in fund balances, and so on) for all years are adjusted accordingly. For a change in the reporting entity that does not result from implementing new accounting standards, however, a government *restates* (presents new) financial statements for the earlier periods based on the new reporting entity. This is required because the effect of the change is not merely an aggregate adjustment to net position; a different reporting entity likely will affect assets, liabilities, deferrals, expenses/expenditures, and revenues as well.

The notes disclose the amount of the effect of any prior-period adjustment on the beginning balance of net position of the current year and on the change in net position of the previous year. If financial statements are presented for more than one year, the notes include the impact on the change in net position and beginning net position of any prior year presented. If, for some reason, a government cannot determine the amounts of the impact, it explains why not.

A government voluntarily making a change in accounting principle (such as the change in inventory method) explains the switch in the notes and explains *why the new method is preferable.* It is expected that such a change will take place only if the new method is preferable to the old one (for example, because it more accurately accounts for transactions or provides better information to financial report readers). Changes due to the implementation of new accounting standards are highlighted in the notes, typically in the SSAP.

CHANGES IN ACCOUNTING ESTIMATE

A third kind of accounting change involves **CHANGES IN ACCOUNTING ESTIMATE.** A change in accounting estimate is what it says: a change in an estimated amount that appears in the financial statements or is used in calculating an amount in the statements. For example, governments report receivables in accrual-basis financial statements as follows: outstanding amount owed to the government minus uncollectible amounts. The portion of receivables that the government believes will not be collected is an estimate (usually a percentage of the total) based on prior experience. If a government had reason to believe that the uncollectible portion of receivables had changed significantly, it would report a change in accounting estimate.

Changes in accounting estimate do not result in restatements or adjustments of prior-period financial information. Rather, the effect of the change is incorporated into the financial statements of the year in which the change takes place (and succeeding years if it continues to affect the information being reported in the financial statements and notes). If the change in accounting estimate has a continuing effect in future years, a government will continue to disclose in the notes the impact on net position for the current year.

GOING CONCERN

The concept of a GOING CONCERN means that a government is believed to be capable of operating and meeting its financial obligations over the course of the 15 months following the date of the financial statements. If the financial statements have been issued and the auditor's report does not mention going concern issues, both the government's finance officers and the auditor have considered whether the government is a going concern and concluded that it is.

Some of the things that the finance officers and auditor consider in a going concern evaluation are:

- Negative financial trends, such as repeated operating deficits, or negative cash flows for a BTA
- Failure to make payments on outstanding bonds, inability to borrow, or being close to or exceeding legal tax and borrowing limits
- Internal matters, such as a labor strike or a government's financial viability depending heavily on the success of a particular program, and
- External matters, such as legislation of a higher level government or the loss of a major customer or taxpayer.

Any one of those factors may not indicate that a government is no longer a going concern, but several in combination could raise doubts. It should be stressed, however, that this does not necessarily mean a government is about to go out of business.

If there are substantial doubts about whether a government is a going concern, the government discloses the following:

- The specific events or conditions that raised the doubts and their potential impact on the government
- The government's evaluation of the seriousness of those events or conditions and any mitigating factors
- The possibility that the government will cease to operate
- The government's plans for dealing with the events or conditions, and
- Information about the government's ability to recover its assets and contend with its liabilities.

The government also may need to discuss this matter in the section of MD&A addressing currently known facts and circumstances.

SUBSEQUENT EVENTS

Suppose that a major event occurs after the end of the fiscal year covered by a government's financial statements but before the financial statements are issued. It might have a significant financial impact on the government and, therefore, affect the decisions you make based on the information in the financial statements or the conclusions you draw about the government's financial health. Such an occurrence is known as a **SUBSEQUENT EVENT**.

There are two kinds of subsequent events. **RECOGNIZED SUBSEQUENT EVENTS** relate to conditions that existed as of the date of the financial statements. Consider, for example, a public utility that had a large account receivable from a major customer as of the fiscal year-end. After the end of the fiscal year, the utility learns that the customer has filed for bankruptcy, thereby calling into question whether the utility will be able to collect the receivable. Recognized subsequent events may require a government to adjust amounts already recognized; in this example, the utility might need to reduce or eliminate the receivable it previously expected to collect.

UNRECOGNIZED SUBSEQUENT EVENTS involve conditions that were not in place as of the date of the financial statements. Because the conditions affected by the subsequent event took place *after* the fiscal year, the impact of the subsequent event is not reflected in the financial statements. In order to avoid misleading you, a government discloses unrecognized subsequent events in the notes.

An example of an unrecognized subsequent event might be the collapse of a major bridge owned by the government, which will cost millions of dollars to replace. Another example could be the relocation to another state of a government's largest single employer, taking with it a considerable amount of tax revenue.

WHAT'S AHEAD?

- HAS A GOVERNMENT VIOLATED ANY LEGAL OR CONTRACTUAL PROVISIONS?
- HOW DOES IT PLAN TO RESOLVE THEM?

FINANCE-RELATED LEGAL AND CONTRACTUAL PROVISIONS

If a government has committed a significant violation of a finance-related legal or contractual provision, it discloses that fact in the notes. This is an important disclosure if you are interested in assessing a government's legal or contractual compliance. A bondholder would want to know if a government had violated any of the provisions of its bond covenants. Such a disclosure might look like Figure 94.

If a state has a law that prohibits deficit fund balances, you might want to know if a government had violated this law. In such a circumstance, a government might make a disclosure like Figure 95.

Figure 94. Note Disclosure of Violation of Bond Covenant and Actions to Resolve

At December 31, 2017, Pelton County was not in compliance with the provisions of the Series 2003 parking facility revenue bond covenants that require assets to be accumulated in a restricted account for the payment of future debt service. The covenants require, at a minimum, that an amount equivalent to one year's debt service payments (currently $1,525,000) be maintained at all times. As of year-end, the County had restricted cash and investments of only $1,052,000. In January 2018, the County transferred an additional $473,000 to this restricted account to correct this deficiency.

Figure 95. Note Disclosure of Violation of Fund Balance Requirements and Actions to Resolve

At June 30, 2017, the following funds reported deficits in fund balance or fund net position, which are violations of state statute:

	Deficit
Governmental fund: Local gas tax	$ (456,000)
Internal service fund: Health insurance	$ (850,000)

The 2018 budget for the local gas tax fund authorizes expenditures in an amount $500,000 less than the amount authorized for revenues. The City Council also has approved a 10 percent increase in the charges assessed by the health insurance fund.

In both of these examples, not only is the instance of the violation or violations identified, but the actions taken to address them also are described.

WHAT'S AHEAD?

- WHAT IS THE STATUS OF THE LOCAL ECONOMY?
- WHO ARE THE BIGGEST EMPLOYERS IN THE LOCAL ECONOMY?
- WHAT DATA ARE AVAILABLE FOR CONSTRUCTING RATIOS?

DEMOGRAPHIC AND ECONOMIC INFORMATION

A government's statistical section includes at least two SI schedules that contain demographic and economic information about the government's geographic area. One schedule includes, at a minimum, 4 pieces of information for the past 10 years (see Figure 96):

- Population
- Total personal income (alternatively, this may be presented in the ratios of outstanding debt schedule, which includes a ratio of debt-to-personal-income; see Figure 36)

- Per capita personal income (total personal income divided by population)
- Unemployment rate.

Figure 96. Statistical Section Schedule of Demographic and Economic Statistics

City of Monumental
Demographic and Economic Statistics
Last 10 Calendar Years

① ②

Calendar Year	Population	Personal Income *(thousands of dollars)*	Per Capita Personal Income	Education Level in Years of Schooling: Median Age	School Enrollment	Unemployment Rate
20W9	88,260	$ 2,373,285	$ 26,890	31.0	14.1	21,647	6.7%
20X0	92,584	2,477,522	26,760	31.3	14.3	22,015	7.7
20X1	94,485	2,607,966	27,602	31.6	14.4	22,544	6.9
20X2	98,102	2,633,412	26,844	31.9	14.5	23,020	6.0
20X3	99,478	2,816,038	28,308	32.2	14.7	23,548	6.0
20X4	102,794	2,857,718	27,800	32.6	14.8	24,687	5.4
20X5	111,507	3,088,421	27,697	32.8	14.9	27,084	4.9
20X6	117,292	3,433,399	29,272	32.9	15.0	29,624	3.2
20X7	122,989	3,762,912	30,596	33.0	15.1	31,854	2.6
20X8	131,246	3,936,501	29,993	33.1	15.2	34,215	4.4

Sources: Population, median age, and education level information provided by the State Department of Planning. Personal income and unemployment data provided by the State Department of Commerce and Labor. School enrollment data provided by the Stonehenge Independent School District.

Note: Population, median age, and education level information are based on surveys conducted during the last quarter of the calendar year. Personal income information is a total for the year. Unemployment rate information is an adjusted yearly average. School enrollment is based on the census at the start of the school year.

Figure 96 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② These are not required; they are provided voluntarily by the illustrative government. A government may provide demographic and economic information beyond the minimum required by accounting standards if it believes the information will be useful to the readers of its financial report.

A government also may present other indicators, such as median age of the population, average educational attainment, employment, school enrollment, and so on. Some governments present information for more than 10 years. Others include comparative indicators for their state or the nation. As long as the four basic indicators or appropriate alternatives are included, a government may add other indicators that help to convey the state of the economy the government resides in and that are meaningful to the users of the government's financial report.

In fact, governments have considerable latitude in deciding what relevant information to include in this schedule. For some governments, especially special-purpose governments like public colleges and universities, airports, hospitals, and so on, these indicators may not be particularly meaningful. For example, although some higher education entities, such as community colleges, are identified with a specific geographic area, many colleges and universities are not (if anything, they relate to their state). What area's population or unemployment rate would they report? Reporting those indicators for the state as a whole may not be useful or relevant. If such a government knows of indicators that are more relevant to its activities and more useful to the users of its financial report, it may present them instead.

Figure 96: The unemployment rate in 20X7 was 2.6%.

Some governments may have difficulty obtaining the required indicators. For instance, official Census Bureau data regarding population is published on an annual basis for states and larger county and local governments, but for smaller jurisdictions, population data are available only from the decennial Census (in other words, every 10 years). Some data take more than a year to assemble and, therefore, may not be available by the time a government's financial report is issued. The general approach a government follows is to present the data that is most current and most specific to the government. Some governments obtain estimates of information for intervening years from other sources, such as state or county departments of planning, economic development, or labor, or from private sources such as business associations or chambers of commerce. Others present information just for the years that are available. Whatever choices a government makes, it includes a note in the schedule that identifies the sources of the information and describes any estimating procedures it employed or assumptions it made. (See **By the numbers…notes to the statistical section schedules** on page 141.)

Figure 97. Statistical Section Schedule of Principal Employers

City of Monumental
Principal Employers
Current Year and Nine Years Ago ②

①

	Calendar Year					
	20X8			20W9		
Employer	Employees	Rank	Percentage of Total City Employment	Employees	Rank	Percentage of Total City Employment
Topaz Laboratories	2,100	1	2.63%	1,800	1	2.57%
Fitty Scent Car Fresheners	960	2	1.20	850	2	1.21
City of Monumental	810	3	1.01	650	4	0.93
Volcano Health Plan, Inc.	650	4	0.81	750	3	1.07
Really Big Chain Store	595	5	0.74	—		—
Sulfur Industries	410	6	0.51	420	6	0.60
Pearl Partners LLP	332	7	0.42	—		—
Diamond Properties	180	8	0.23	200	7	0.29
Bronson, Brunson & Branson	120	9	0.15	—		—
Megagoogleplex Cinemas	115	10	0.14	—		—
Pet Container Corp.	—		—	450	5	0.64
Puffin LLP	—		—	190	8	0.27
Inward Outreach	—		—	120	9	0.17
Titanium Energy Partners Ltd.	—		—	90	10	0.13
Total	6,272		7.84%	5,520		7.89%

Source: City Economic Development Division.

Figure 97 Notes

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

② At first blush, the requirement to present information for the current year and the period 9 years prior may seem strange, because the statistical section schedules are mostly 10-year schedules. However, you should notice that the 2 years reported here are the same as the first and last years of the 10-year trend in Figure 96 and, therefore, it covers the same 10-year period. It simply does not present the information for the intervening years.

Principal Employers

A government also presents a schedule of the 10 largest employers in its jurisdiction for the current year and the period 9 years prior. (A government may present fewer than 10 employers if they amount to half or more of total employment.) In addition to identifying the largest employers, the schedule presents the number of persons each employs and the number of employees divided by total employment. (See Figure 97.)

What Can You Do with Demographic and Economic Information?

There are two basic reasons why a government includes this information in the statistical section. First, it helps you to understand the economic environment the government operates in. The state of the economy can impact the government in a variety of ways. The financial well-being of the citizens and businesses affects how much economic activity they engage in, how much and what they buy, where they live and work, how much they earn, and so on. If the government is dependent on obtaining resources by taxing purchases, income, or home values, or any other base that is impacted by the economy, its revenues will be affected, too. Certain service costs also change depending on the strength of the economy, both because of rising costs for labor, capital, supplies, and such, and because demand for services also changes.

The list of major employers helps you to assess whether the economy is reliant on a few large employers. When a significant percentage of total employment is related to just a handful of companies, the closure, downsizing, or relocation of one of those companies could have a dramatic impact on the economy (and, consequently, on the government's finances).

The second reason this information is presented is because the users of financial reports need this kind of raw data to produce financial ratios. You have seen several ratios in this guide that compare financial information to an indicator that puts the financial information in context and allows you to analyze it over time and compare it with other governments. These include the ratios of debt divided by population, personal income, and property values; the ratios of fiduciary net position divided by total pension and OPEB liabilities; and the debt-service-to-noncapital-expenditures ratio. With the economic and demographic indicators in these statistical section schedules, you can construct your own ratios from the information in the financial statements, notes, RSI, and SI.

OPERATING INFORMATION

The statistical section includes three SI schedules that provide information for the last 10 fiscal years about a government's operations and resources to help you place the financial statements and notes in context—numbers of government employees, operating indicators, and capital assets. (The capital assets information is discussed in Part Six and illustrated in Figure 35.)

Government Employees

This schedule (Figure 98) includes the number of persons a government employs, typically arranged by the functional, programmatic, or identifiable activity categories of the statement of activities or statement of revenues, expenses, and changes in fund net position. However, different categories may be used if a government does not keep track of its employment in that fashion, or if it would not be meaningful to the users of the financial report to report employment that way.

Figure 98: Full-time equivalent finance staff increased from 33 to 44 between 20X0 and 20X9.

Operating Indicators

The second SI schedule includes indicators of demand or level of service for each of the functions, programs, or identifiable activities reported in the statement of activities or statement of revenues, expenses, and changes in fund net position. The illustrative schedule in Figure 99 contains a variety of measures for each function and program, but a government may present just a single indicator as long as it offers a clear sense of *how much service a government provides*. If a function covers a variety of disparate activities, more than one indicator may be needed.

Figure 99: Volumes borrowed from the library in 20X5 totaled 394,326. An average of 225.6 tons of garbage was collected daily in 20X3.

Figure 98. Statistical Section Schedule of Government Employees

City of Phenomenal
① Full-Time Equivalent City Government Employees by Function/Program
Last 10 Fiscal Years

	Full-Time Equivalent Employees as of June 30									
Function/Program	**20X0**	**20X1**	**20X2**	**20X3**	**20X4**	**20X5**	**20X6**	**20X7**	**20X8**	**20X9**
General government										
Management services	26	26	27	27	26	26	25	30	31	31
Finance	33	34	34	36	36	37	38	39	46	44
Planning	17	17	17	17	17	17	18	18	18	19
Building	15	14	15	16	16	15	16	17	17	20
Other	6	6	6	6	6	6	6	6	6	8
Police										
Officers [a]	143	145	148	151	158	153	156	166	187	201
Civilians	70	72	73	69	70	72	74	78	84	85
Fire										
Firefighters and officers	78	80	81	77	77	78	80	80	80	89
Civilians	30	31	32	32	33	35	36	39	40	31
Refuse collection	17	18	17	18	18	18	18	18	20	22
Other public works										
Engineering [b]	46	48	51	50	48	49	50	54	56	57
Other	12	12	12	13	13	13	13	14	15	14
Redevelopment	14	15	15	15	16	16	17	17	18	18
Parks and recreation	47	49	48	49	50	49	49	49	49	50
Library	21	21	21	21	21	21	21	20	20	19
Water [b]	35	37	39	41	41	43	45	52	57	57
Wastewater	33	33	33	35	37	39	41	37	37	37
Transit	7	7	7	7	7	7	7	7	8	8
Total	650	665	676	680	690	694	710	741	789	810

Source: City Budget Office.

[a] The police department began the hiring of additional police officers in 20X7 to staff community policing positions.

[b] The City has added additional engineering and water staff in recent years in connection with several infrastructure improvement initiatives.

Figures 98 and 99 Note

① NOTE: This is a different government from Local City and, therefore, this illustration does not tie to the financial statements.

Figure 99. Statistical Section Schedule of Operating Indicators

City of Phenomenal
Operating Indicators by Function/Program ①
Last 10 Fiscal Years

	Fiscal Year									
Function/Program	**20X0**	**20X1**	**20X2**	**20X3**	**20X4**	**20X5**	**20X6**	**20X7**	**20X8**	**20X9**
Police										
Physical arrests	11,427	11,542	11,016	11,127	11,471	11,587	11,704	12,192	12,700	13,511
Parking violations	27,014	27,565	28,128	28,702	29,288	29,885	30,495	31,118	29,921	28,770
Traffic violations	22,099	22,550	23,010	23,479	23,958	24,447	24,946	25,455	24,476	23,535
Fire										
Emergency responses	10,950	12,045	11,607	11,279	12,264	12,483	12,812	12,593	12,921	13,359
Fires extinguished	1,643	1,807	1,741	1,692	1,840	1,872	1,922	1,889	1,938	2,004
Inspections	27,375	27,923	28,481	29,051	28,470	27,900	27,342	26,522	25,726	24,954
Refuse collection [a]										
Refuse collected (tons per day)	215.6	218.8	222.2	225.6	229.0	203.6	204.6	205.6	206.7	207.7
Recyclables collected (tons per day)	27.7	28.2	28.8	29.4	30.0	60.0	62.5	65.1	67.8	70.6
Other public works										
Street resurfacing (miles)	25.7	26.0	26.2	26.5	26.8	27.1	27.3	27.6	27.9	28.2
Potholes repaired	898	906	913	921	928	988	996	1,003	1,011	1,019
Parks and recreation										
Athletic field permits issued [b]	1,386	1,512	1,632	1,825	1,850	1,550	1,776	1,887	1,924	1,991
Community center admissions	130,000	131,950	133,929	135,938	137,977	140,047	142,148	144,280	146,444	148,641
Library										
Volumes in collection	145,687	146,415	147,148	147,883	148,623	149,366	150,113	150,863	151,617	152,376
Total volumes borrowed	384,614	386,537	388,469	390,412	392,364	394,326	396,297	398,279	400,270	402,272
Water										
New connections	146	142	144	145	147	148	150	151	153	154
Water main breaks	9	9	4	7	12	10	6	5	10	14
Average daily consumption (thousands of gallons)	3,177	3,241	3,308	3,375	3,444	3,514	3,586	3,659	3,734	3,810
Peak daily consumption (thousands of gallons)	6,991	7,134	7,279	7,428	7,579	7,734	7,892	8,053	8,217	8,385
Wastewater										
Average daily sewage treatment (thousands of gallons)	2,516	2,568	2,620	2,673	2,728	2,784	2,841	2,898	2,958	3,018
Transit										
Total route miles	96,900	96,900	96,900	96,900	96,900	96,900	96,900	96,900	96,900	96,900
Passengers	140,347	138,957	137,581	136,219	134,870	133,535	132,213	129,684	131,433	135,900

Sources: Various City departments.
Note: Indicators are not available for the general government function.

[a] The Department of Sanitation implemented a recycling initiative in 20X5.

[b] The 12 athletic fields in Schoonmaker Park were out of service during most of 20X5 while they were rehabilitated.

What Can You Do with Operating Information?

This information can be very valuable for understanding trends in the cost of services. For most governments, the lion's share of the cost of many services is employee compensation. Therefore, if you have information about how the number of employees has changed over time, you have an important insight into why costs have risen or fallen for particular functions, programs, activities, or services.

Service costs equally are the result of the level of service provided. Furthermore, the level of service provided is impacted by the number of persons employed. Several interesting comparisons can be made with the operating indicators and the information in the financial statements and other statistical section schedules. For example, how does the percentage change in the expenses of a particular function or program compare with the percentage change in the number of persons employed or the level of service provided? How do changes in the number of employees compare with changes in the level of service? If the number of employees is rising, is the level of service rising, too? If the level of service is falling or remaining flat, there may be a loss of efficiency. Conversely, if the level of service is rising but the number of employees is flat or declining, efficiency could be improving.

OTHER SCHEDULES

In addition to the combining and individual statements, the financial section of a government's CAFR also may include extra schedules presented as SI. These schedules may be presented for one of three reasons.

First, a government may include schedules to demonstrate its compliance with finance-related legal or contractual provisions. For example, accounting standards require governments to present budgetary comparison schedules for the general fund and for major special revenue funds for which they have a legally adopted budget. (See Part Nine and Figures 60 and 61.) However, it may show budgetary comparisons for other funds in order to meet the requirements of state finance law. Such statements and schedules are presented as SI in the financial section of the CAFR.

Second, a government may present schedules that bring together or show in greater detail information that is spread throughout the various financial statements. For instance, a government might present schedules of taxes receivable and delinquent taxes, or schedules that offer detailed information about investments; long-term debt; capital assets; or cash receipts, disbursements, and balances. Figure E-4 illustrates an SI schedule of capital assets by function that some governments present in their CAFRs.

Third, a government may present schedules that provide information found in the financial statements in greater detail or organized differently. Some governments include schedules of revenues and expenses for their individual departments or agencies. Others present a schedule of expenses organized by object—salaries, benefits, rent, utilities, supplies, contracts, and so on.

CHANGES IN ACCOUNTING PRINCIPLE result from a government applying a different accounting requirement than in prior years

CHANGES IN THE REPORTING ENTITY result from changes in the scope of the government that is covered by the financial statements

PRIOR-PERIOD ADJUSTMENTS are revisions to amounts in previous financial reports because of the use of new accounting principles, errors, or changes in the organizations included in the reporting entity

PART FOURTEEN

GOVERNMENTAL FINANCIAL ANALYSIS

In many cases, the information in a government's financial statements will not simply volunteer answers to all of your questions—you have to make it talk. The process of drawing meaning from financial statement data is called *financial analysis*. In most cases, analytical techniques utilize financial ratios—measures created by dividing one number into another. This section presents some basic ratios that may be applied to government financial statements.

CAVEATS OF FINANCIAL ANALYSIS

It is important to keep in mind that financial statement analysis is more of an art form than a science. There are not many absolutes when it comes to assessing the financial status of a government because different people are interested in different aspects of financial health. While some may be concerned with the cost of police protection, education, or other services, others may be focused on a government's ability to repay long-term debt, and still others may want to look at the short-term availability of cash. Furthermore, even if two people are interested in the same financial issue, their judgments remain subjective and are likely to be different as a result. In other words, one person may consider a $100,000 increase in net position to be acceptable, while another may believe it is insufficient for a government's needs. Who is right? The only suitable answer may be, "It depends. . . ."

Fortunately, there are ways to bolster the validity of the conclusions you draw from the results of your analytical work. Others may disagree with your conclusions, but it will be difficult for them to challenge your methods if you are mindful of four issues: definitions, context, persistence, and thoroughness.

Definitions

First, *the definitions of financial ratios are not set in stone.* Different people may employ different equations but call them by the same name. For instance, some analysts add receivables to the cash and investments in the numerator of the **QUICK RATIO** (first described on page 41 and explained on page 318). If you are presented with ratio information, you should be careful to ask how it was calculated. Similarly, you should take care to specify the components of the ratios you use in your own analyses.

Context

Second, *ratios need to be placed in context.* Governmental operations and transactions do not occur in a vacuum. Good financial analysis cannot exist in a vacuum, either—it requires context to be meaningful. For example, it is not sufficient just to calculate a **CURRENT RATIO**—current assets divided by current liabilities—and find that it is 1.5. What does a ratio of 1.5 mean? One might answer, "The government's

most liquid assets amount to 50 percent more than the short-term liabilities in its financial statements." But that sounds more like a general definition than a meaningful answer for that particular government.

To give meaning to financial ratios, and financial analysis in general, you need a point of reference, a comparison, or a benchmark. For example:

- How does the ratio compare to earlier years for the same government—improving, declining, holding steady?
- How does the ratio compare to other, similar governments—higher, lower, roughly the same?
- Is there a commonly accepted rule of thumb to compare the ratio to?

Persistence

Third, *financial analysis is an iterative process*. It seems sometimes that ratios raise more questions than they answer. Consider the current ratio example above. We have inserted the necessary information from the statement of net position and calculated a ratio of 1.5. The result immediately raised another question: What does a ratio of 1.5 mean? Other than restating the obvious, we were not sure. So again, we asked more questions: How does that ratio compare with past years? How does it compare with other, similar governments?

Should we be satisfied with having answered those questions, too? The answer is no. Thorough analysis covers all the bases and looks for *explanations* of the differences between governments and *reasons* for changes over time. Financial analysis is an iterative process, much like peeling away the layers of an onion.

Thoroughness

Finally, *thorough analysis makes better analysis*. Take these truisms to heart: "No ratio is an island" and "An analyst does not live by one ratio alone." The financial story of a government is not told with a single ratio, an individual snapshot of a portion of the government, but with an accumulation of ratios and other information that together form a comprehensive, multi-dimensional picture of the fiscal health of a government.

COMMON-SIZE RATIOS

At the most basic level, financial ratios are comparisons of one amount or group of amounts with another amount or group of amounts. The "comparison" is made via division—one amount or group of amounts is divided by another. The resulting number is the ratio—the indicator of the magnitude of a particular financial or nonfinancial characteristic of a government. The ratio is placed in context and given meaning by tracking how it changes over multiple fiscal periods and by contrasting it with the same ratio for other, similar governments.

Nowhere are the most elementary features of financial ratios more clearly displayed than in the common-size ratios. As we shall see, percentage distribution is no more complicated than dividing one single number by another single number. This simple calculation, however, produces immensely important information that—with percentage change—serves as the initial step in analyzing a government's financial statements.

Common-size ratios serve two valuable purposes. First, they can provide a quick overview of the finances of a government and how they have changed since last year. Did assets grow or shrink? Were taxes the source of a larger or smaller share of revenue? Second, they put the financial data of a government in a form that can be compared with other governments, regardless of their size (hence the name "common-size"). In addition, they can be applied to virtually any kind of financial statement information.

Percentage Change

Percentage change represents the *magnitude* of change in a particular item, rather than the aggregate dollar difference from one year to the next. Percentage change is calculated using this formula:

([current year amount – earlier year amount] ÷ earlier year amount) × 100
= percentage change from earlier year to current year

Figure 100 demonstrates the mechanics of calculating percentage change ratios for the assets in the government-wide statement of net position (Figure 1).

The particular usefulness of percentage change ratios can be seen by comparing receivables and capital assets in Figure 100. Capital assets increased $11.7 million between 2016 and 2017, while receivables increased by a smaller $6.4 million. The percentage changes show that, although the dollar growth for receivables was smaller, the percentage change was much greater—an increase of almost 64 percent. Growth on such a scale should lead you to look further in that area to determine what happened and whether it has any implications for a government's finances. On the other hand, a relatively large percentage increase in a relatively small dollar amount may not be important: Growth in an expense from $100,000 to $300,000 is a 200 percent increase, but how important is $300,000 if total expenses are $100 million? Different people will answer that question differently, depending on their concerns.

Percentage Distribution

Percentage distribution shows the portion of a financial statement total or subtotal represented by individual elements. Consider a hypothetical set of numbers: It probably is not meaningful to know only that the City of Large had $1 *billion* of taxes receivable and the Village of Small had $1 *million*. But knowing that taxes receivable represented 3 percent of total assets in Large and 14 percent in Small tells you something about the extent to which each is reliant on resources it has not yet collected.

Percentage distribution uses this formula:

(individual element amount ÷ total amount for category) × 100
= percentage distribution for individual element

Figure 101 shows the mechanics of calculating the percentage distribution ratio, utilizing expense information from the government-wide statement of activities. (Refer to Figure 42.)

Figure 100. Percentage Change Calculations for Assets in Figure 1

	As of 12/31/17		As of 12/31/16		Dollar Change		As of 12/31/16		Percentage Change
		m i		*e q*		*d i v*		*e q*	
Cash and cash equivalents	$ 23,819,319	*n*	$ 21,072,220	*u*	$ 2,747,099	*i*	$ 21,072,220	*u*	13.04%
Investments	74,961,466	*u*	78,807,300	*a*	(3,845,834)	*d*	78,807,300	*a*	-4.88
Receivables (net)	16,441,747	*s*	10,052,465	*l*	6,389,282	*e*	10,052,465	*l*	63.56
Inventories	448,823		402,001	*s*	46,822	*d*	402,001	*s*	11.65
Restricted cash and cash equivalents	1,493,322		1,372,284		121,038		1,372,284		8.82
Capital assets (net)	321,412,511		309,719,424		11,693,087	*b*	309,719,424		3.78
Total assets	$ 438,577,188		$ 374,425,694		$ 64,151,494	*y*	$ 374,425,694		17.13

Figure 101. Percentage Distribution Calculations for Expenses in Figure 42

	Program Expenses	*d i*	Total Expenses	*e q*	Percentage Distribution
General government	$ 9,571,410	*v*	$ 105,807,013	*u*	9.05%
Public safety	34,844,749	*i*	105,807,013	*a*	32.93
Public works	10,128,538	*d*	105,807,013	*l*	9.57
Engineering services	1,299,645	*e*	105,807,013	*s*	1.23
Health and sanitation	6,738,672	*d*	105,807,013		6.37
Cemetery	735,866		105,807,013		0.70
Culture and recreation	11,532,350	*b*	105,807,013		10.90
Community development	2,994,389	*y*	105,807,013		2.83
Education (payment to school)	21,893,273		105,807,013		20.69
Interest on long-term debt	6,068,121		105,807,013		5.74
Total expenses, governmental activities	$ 105,807,013		105,807,013		100.00%

Adjusting for Inflation

Inflation can be defined as the increase over time in the prevailing prices that are paid for goods and services. A portion of the growth in spending exhibited by a government each year is the effect of higher prices for motor fuel, supplies, food, professional services, and so on.

Many analysts adjust their financial trend data to remove this impact before calculating percentage changes and other ratios. One reason they do this is to obtain a more precise read on financial changes related to policy and operating decisions made by a government's officials, rather than changes that occurred because a government must pay higher prices.

The process of converting the "nominal" dollars stated in each year's financial statements to "constant-dollar" numbers that do not include inflation commonly relies on the Consumer Price Index (CPI) compiled by the U.S. Bureau of Labor Statistics for various regions of the country. The CPI has a base that is an average of the prices in 1982 through 1984—this base is given a value of 100. In each subsequent year, the index grows by the amount of inflation for that year. For example, if inflation had been 5 percent in the first year, the index would have risen from 100 to 105.

Using the CPI to adjust financial data essentially involves adding inflation to or subtracting it from all data so that the amounts for the earlier years are stated on the same basis as a selected base year (often the last year in a trend). This is the formula:

(base or current year CPI ÷ earlier year CPI) ×
nominal dollar amount for earlier year
= constant-dollar amount for earlier year

The following two examples illustrate the value of adjusting for inflation.

Inflation-adjusted change in expenditures

Consider a situation in which you want to compare expenditures for emergency rescue services in one year ($1,000,000) with 10 years ago ($900,000), and you want to adjust for inflation by making the older figures comparable with last year's. The CPI for the more recent year was 237 and 10 years ago it was 202. The calculations would look like this:

(237 ÷ 202) × $900,000 = $1,055,941

In other words, the $900,000 spent 10 years prior, restated in the most recent year's dollars, equals $1,055,941. Before the adjustments, the percentage change between $900,000 and $1,000,000 was an 11.1 percent increase. However, once you calculate the constant-dollar amount for the earlier year, you see that the percentage change is a 5.3 percent *decrease* in "real" or inflation-adjusted terms. In other words, were it not for the effects of inflation, expenditures for emergency rescue services actually would have fallen over the 10-year period.

Inflation-adjusted change in revenues

Consider another situation in which you want to compare revenues for property taxes last year ($15 million) with 15 years ago ($12 million), and you want to adjust for inflation by making the older figures

comparable with last year's. The CPI for the more recent year was 237 and 15 years ago it was 177. The calculation would look like this:

$$(237 \div 177) \times \$12{,}000{,}000 = \$16{,}067{,}797$$

The nominal or unadjusted increase in property tax revenues from $12 million to $15 million was 25 percent. However, the real or inflation-adjusted change actually was a 6.6 percent *decrease*:

$$(\$15{,}000{,}000 - 16{,}067{,}797) \div 16{,}067{,}797 = -0.066 \times 100 = -6.6 \text{ percent}$$

In other words, after removing the effects of inflation, this government effectively had less property tax revenue to spend on services. Stated differently, the property tax revenue has less purchasing power in the most recent year—the same amount of revenue in the most recent year cannot finance as much service as it did in the earlier year.

Potential Applications

As mentioned previously, the common-size ratios act as the gateway to financial statement analysis. They raise red flags for potentially important issues, directing the user to areas where additional analysis is required before satisfactory answers can be obtained. For instance, a user might see a decline in the percentage of assets represented by cash and be concerned about the government's ability to come up with ready resources to pay its bills as they arrive. This person might want to explore this issue further by calculating additional ratios specifically designed to parse a government's liquidity. These ratios are discussed on pages 47, 48, and 318–320.

Consider the following information for a state government:

	2016	2017	Percentage Change
Due to local governments	$ 65,985,231	$ 92,116,323	39.6%

The amount this state government owes the local governments at the end of the year rose 39.6 percent in a single year. Should this be a cause for concern? Is the state government experiencing cash flow problems that led it to delay grant payments due late in the year? Has there been a change in the payment schedule for a significant local aid program? Will the government have sufficient liquid resources in the coming year to handle this growth in liabilities? At this point, we do not know the answers to these questions. But, we have been tipped off to a potential issue that we can now investigate further.

Now look at this net position information from a school district:

	2016	Percentage Distribution	2017	Percentage Distribution
Net investment in capital assets	$ 15,859,312	62.2%	$ 16,148,238	58.5%
Restricted	5,544,803	21.7	5,916,400	21.4
Unrestricted	4,111,989	16.1	5,546,174	20.1
Total	$ 25,516,104	100.0%	$ 27,610,812	100.0%

Relative to the other two categories of net position, this district's unrestricted net position has grown—from about 16 percent to 20 percent of total net position. This could be good news; the growth in unrestricted net position may signal an improvement in the district's fiscal health. Now we will want to look further for other evidence that, together with this information, will give us a more complete picture. In other words, this single comparison of ratios alone should not lead you to conclude that all is well in this school district, because other indicators could tell a different story.

Common-size ratios are not only a door opener, however. The information they produce is useful and informative in and of itself. An important use for percentage distribution is determining a government's level of revenue dispersion. The degree of dispersion or diversity in a government's sources of revenue can tell you something about its exposure to financial difficulty if a particular revenue source dries up. Examining the individual components of total revenues, you might find that a government relies on a broad range of revenues to support its activities and, therefore, is relatively less likely to be dramatically affected if one type of revenue does not meet expectations. Alternatively, you might find that it relies heavily on one or two sources of revenue—reductions in those kinds of revenues could harm a government financially because it is very dependent on those revenues to run its operations.

	County Y	Percentage Distribution	County Z	Percentage Distribution
Property taxes	$ 35,349,452	54.7%	$ 16,322,782	24.8%
Sales taxes	9,434,098	14.6	15,000,365	22.8
State aid	8,287,998	12.8	12,234,045	18.6
Fees and charges	5,223,403	8.1	8,993,476	13.6
Investment income	2,224,777	3.4	7,634,876	11.6
Other	4,101,754	6.3	5,546,174	8.4
Total	$ 64,621,482	100.0%	$ 65,731,718	100.0%

This comparison of the percentage distribution of two counties' revenues can inform judgments about their relative revenue dispersion. Nearly 55 percent of County Y's revenues come from a single source—its property tax. County Z's revenues, in contrast, are more evenly distributed. So, County Z must be healthier than County Y. Perhaps, perhaps not. Consider that County Z is more reliant on sales taxes, which tend to be more volatile than property taxes; in other words, they tend to drop substantially in a down economy, whereas property taxes tend to stay fairly constant. Further, County Z is more

dependent on state aid and investment income, two revenue sources over which it has little control (meaning, a county may be able to raise tax rates, but it probably cannot directly control how much intergovernmental revenue it receives). So, County Y must be healthier than County Z. Maybe, maybe not. You will need to examine revenue dispersion along with a lot of other ratios before deciding which government is in better shape financially.

ECONOMIC CONDITION ANALYSIS

In the literature that discusses the hows and whys of analyzing a government's financial health, two concepts are commonly bandied about—financial position and financial condition. Some care is required when using these terms because it is common to find disagreement regarding how they are defined. Some analysts use one phrase or the other, and some use them interchangeably. Still others differentiate between the concepts to varying degrees, ranging from vast to subtle differences.

When setting accounting standards, the GASB employs a concept that describes a broad measurement of financial health, encompassing both financial position and financial condition—economic condition:

> Economic condition is a composite of a government's financial position, fiscal capacity, and service capacity:
>
> > Financial position is the status of a government's assets, deferred outflows, liabilities, deferred inflows, and net position, as displayed in the basic financial statements.
> >
> > FISCAL CAPACITY is the government's ability and willingness to meet its financial obligations as they come due on an ongoing basis.
> >
> > SERVICE CAPACITY is the government's ability and willingness to meet its commitments to provide services on an ongoing basis.

Financial Position

The simplest and most straightforward way to assess a government's present financial situation is to compare its total assets and liabilities. (Refer to the government-wide statement of net position in Figure 1.) Does it own more than it owes, or vice versa? You do not even need a calculator, because the net position figure essentially is the difference between the two (and between deferred outflows and deferred inflows as well).

To add some additional meaning to the net position figure, you could compare it to the previous year's net position. (This kind of information can be found in Table A-1 of the sample MD&A as well.) Did net position increase? Then financial position improved. Decrease? Then financial position deteriorated. You also could divide net position by total assets and compare the result with other governments.

In either case, you can utilize only unrestricted net position if you wish to assess or compare the most broadly available resources. In order to obtain a sense of the *magnitude* of the change in financial position,

some analysts compare the aggregate net position amount to the government's overall level of financial activity. It is calculated here for the Local City Landfill Authority, using information in the component unit combining statements (Figures 91 and 92):

total net position ÷ total expenses =
$3,547,668 ÷ 3,382,157 = 1.0489, or 104.9 percent

Alternatively, you might use revenues in the denominator:

total net position ÷ total revenues =
$3,547,668 ÷ 4,079,496 = 0.8696, or 87.0 percent

Either ratio can be examined over time and compared to other, similar entities now that they have been placed in context. This is necessary because comparing aggregate net position or change in net position amounts would be misleading if a government's level of financial activity changes over time or if governments of various sizes are compared. If two governments—one with annual expenses of $20 million and the other $80 million—each had a $1 million increase in net position, it obviously is much more significant for the government with the lower annual expenses. In a sense, you are making a common-size ratio out of financial position.

Similar ratios can be calculated using general fund information (these amounts come from Local City's governmental funds statements—Figures 53 and 54):

total fund balance ÷ total expenditures and other financing uses =
$1,655,366 ÷ (88,717,173 + 2,163,759) = 0.01821, or 1.8 percent

---

total fund balance ÷ total revenues and other financing sources =
$1,655,366 ÷ (86,022,165 + 129,323) = 0.01921, or 1.9 percent

This ratio is a good example of how ratio definitions vary from analyst to analyst. Some analysts use only expenditures in the denominator. Others include other financing uses because methods of financing and fund structures differ from government to government. Some will include the net difference between other financing sources and uses. Still others use revenues instead of expenditures. Before you use ratios that someone else calculated, be careful that you understand how those ratios are calculated and what they include.

Implicit in these comparisons is the idea that net position (or fund balance) is a "reserve" that the government may draw down when needed to finance unplanned expenses (expenditures), or as a hedge against a revenue shortfall. In this context, it may be most appropriate to include only unrestricted net position (from Figure 91) or unassigned fund balance (from Figure 53) in the numerator of the ratio, as follows:

unrestricted net position ÷ total expenses
$562,868 ÷ 3,382,157 = 0.1664, or 16.6 percent

---

unassigned fund balance ÷ total expenditures and other financing uses =
$1,022,226 ÷ (88,717,173 + 2,163,759) = 0.01125, or 1.1 percent

Fiscal Capacity

Ratios that measure fiscal capacity can be divided into four groups—liquidity, solvency, ability to pay, and financial efficiency.

Liquidity

A government's ability to meet its obligations can be examined on two levels—short term and long term. Liquidity relates to the availability of resources to finance near-term obligations. Liquidity ratios, therefore, are concerned with a government's ability to pay for its most immediate obligations. In other words, they can help you determine whether, over the next year (or less), a government will have enough cash (or assets that can be quickly converted to cash) on hand to pay the bills that come due. One measure of liquidity is the current ratio:

current ratio = current assets ÷ current liabilities

For instance, insert the governmental activities data from Local City's government-wide statement of net position:

$54,292,401 ÷ 17,774,206 = 3.05

This means that Local City's governmental activities have current assets three times greater than their current liabilities. Deciding whether this is the right level for the government you are analyzing depends upon your personal views—some might be comfortable with this level of liquidity, whereas others might believe it to be too high or too low.

A narrower measure of liquidity is the quick ratio, which compares only the *most liquid* assets of a government—generally cash, near-cash assets such as money market funds, other short-term investments, and sometimes receivables—to its current liabilities. This is a more conservative indicator of a government's ability to meet obligations, assuming implicitly that its current liabilities will come due so soon that other current assets cannot be converted to cash (liquidated) quickly enough to pay for them.

quick ratio = (cash + current investments) ÷ current liabilities

Again, calculate the ratio using the governmental activities information from the statement of net position:

($13,597,899 + 27,365,221) ÷ 17,774,206 = 2.30

Is 2.30 "good enough"? Ultimately, it is up to you to decide what a satisfactory number is for the purposes of the decisions you wish to make. Although there are plenty of "rules of thumb" you may choose to compare a government to, they should be handled with extreme care. The circumstances of governments vary greatly from jurisdiction to jurisdiction, raising the very real possibility of comparing apples to oranges. A particular rule of thumb may be predicated on a set of assumptions that are not applicable to the government you are examining—in which case, the comparison may be meaningless or, worse, misleading.

Even though this guide cannot state categorically how large current assets should be relative to current liabilities, it is appropriate, at least, to mention some possible implications. Some observers think that a smaller liquidity ratio indicates a government will be less able to cover its obligations as they are due or expected to be paid in the next year. On the other hand, some believe that a higher ratio suggests that more of a government's resources are in the form of cash or near-cash assets than is necessary to pay bills as they come due. In their view, the government would be better off investing more of these highly liquid assets on a longer term basis, which would generate more investment income for the government than leaving them in low-interest bank accounts and short-term investments.

Another way to measure liquidity is to calculate **DAYS CASH ON HAND.** This ratio compares a government's available unrestricted cash as of the date of the financial statements (Figure 1) with its expenses that require cash to be satisfied (Figures 12 and 42). Calculated for Local City's governmental activities, it would be:

days cash on hand =
[unrestricted cash and cash equivalents ÷ (total expenses – depreciation)] × 365 =
[$13,597,899 ÷ (105,807,013 – 4,387,000)] × 365 = 48.94 days

The ratio indicates that Local City's governmental activities have enough cash to continue operating and paying bills for about 49 days. The same ratio could be calculated for its BTAs. Tracking the ratio over multiple years or comparing it with the ratios for similar governments would give you a sense of whether this is a positive or negative result.

Alternatively, days cash on hand might be calculated using general fund information (Figures 53 and 54), as follows:

general fund days cash on hand =
[unrestricted cash and cash equivalents ÷ (total expenditures – capital outlay)] × 365 =
[$3,418,485 ÷ (88,717,173 – 0)] × 365 = 14.06 days

If a government reports special revenue funds, some of its "operating" expenditures will be found in those funds as well. In such a case, you may want to combine general fund information with special

revenue funds information (both major funds and nonmajor funds; see Figure 63) to calculate days cash on hand.

Solvency

SOLVENCY RATIOS, like liquidity ratios, are used to examine a government's ability to fulfill its obligations. But solvency ratios focus on a government's *long-term* obligations. Solvency ratios come in two general forms—**LEVERAGE RATIOS** and coverage ratios.

Leverage ratios. Leverage—the degree to which a government's assets are financed through borrowing and other long-term obligations—can be assessed with two ratios. The **LIABILITIES-TO-ASSETS RATIO** is straightforward—total liabilities divided by total assets. Alternatively, you might calculate the **LIABILITIES-TO-NET-POSITION RATIO**, although it tells you literally the same things as the liabilities-to-assets ratio despite producing a different number. The ratios are calculated below using statement of net position information (Figure 1) for the total primary government:

liabilities-to-assets ratio = total liabilities ÷ total assets
$338,791,841 ÷ 438,577,188 = 0.77

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liabilities-to-net-position ratio = total liabilities ÷ total net position
$338,791,841 ÷ 112,398,922 = 3.01

The first calculation produces a ratio of 0.77, or 77 percent. This means that more than three-quarters of Local City's assets are financed with borrowing of one form or another. The latter ratio is 3.01, meaning that for every dollar of resources Local City has available to use for providing public services, it owes $3.01.

Coverage ratios. One typical coverage ratio, the **INTEREST COVERAGE RATIO** (or "times-interest-earned"), compares cash flows generated by operations to interest payments on debt. Another, debt service coverage, compares cash flows to a government's entire debt repayments, both interest and principal. These ratios generally can be computed for the enterprise funds (and BTAs, if they are the same) using information from the statement of revenues, expenses, and changes in fund net position, statement of cash flows (Figures 69 and 70, respectively), and long-term liabilities note disclosure (Figure 16).

times-interest-earned =
(cash flow from operations + interest expense) ÷ interest expense
($1,921,872 + 2,767,376) ÷ 2,767,376 = 1.69

---

debt service coverage =
(cash flow from operations + debt service) ÷ debt service
($1,921,872 + 2,767,376 + 2,588,000) ÷ (2,767,376 + 2,588,000) = 1.36

Unfortunately, it is not as straightforward to calculate either of these ratios for the governmental activities or the total primary government, principally because the statements contain no cash flows information for either. Governmental activities debt generally takes the form of GO or tax-backed bonds, however, for which coverage ratios are less important than for the revenue bonds of BTAs. If one were to attempt to calculate coverage ratios for the primary government, the formulas end up being quite long:

times-interest-earned =
(cash flow from operations + interest expense) ÷ interest expense
= ([excess/deficiency of general fund revenues over expenditures +
enterprise funds cash flows from operations] + [interest on long-term debt for governmental +
business-type activities]) ÷ (interest on long-term debt for governmental + business-type activities)
= ([−$2,695,008 + 1,921,872] + [6,068,121 + 2,767,376]) ÷ (6,068,121 + 2,767,376) = 0.91

---

debt service coverage =
(cash flow from operations + debt service) ÷ debt service
= ([excess/deficiency of general fund revenues over expenditures +
enterprise funds cash flow from operations] + [interest on long-term debt +
principal repayments for governmental and business-type activities]) ÷
(interest on long-term debt for governmental and business-type activities +
principal repayments for governmental and business-type activities)
= ([−$2,695,008 + 1,921,872] + [6,068,121 + 2,767,376 + 6,898,000 + 2,588,000])
÷ (6,068,121 + 2,767,376 + 6,898,000 + 2,588,000) = 0.96

The most significant problem with this equation is not its length, however, but the fact that it contains potentially imprecise substitute numbers. The governmental funds financial statements use a current financial resources measurement focus and a modified accrual basis of accounting, which encompass more than just cash. Although it is closer to cash than the economic resources measurement focus and accrual basis of accounting in the other financial statements, it is *not* cash. Therefore, the excess/deficiency could be significantly different from the real cash flows from operations for governmental activities.

An additional complication is that not all of the resources of the governmental activities may be generally available. Some resources, like education aid from the state government, can be used only for a specific purpose, and that purpose probably is not repaying debt. Consequently, those resources should not be included in a coverage ratio. The solution applied on the preceding page is to include only the excess/deficiency from the general operating fund of the government.

Furthermore, the cash disbursed for BTA principal repayments may not be the same as the principal payments actually due to be paid. If a government does not make a required principal payment, cash flows are unaffected; yet, for the purpose of determining a government's ability to repay its debt, we need to know what the debt service requirements actually are, but the cash flows number would be too low. (Of course, assuming that same government catches up with that principal payment the next year, its cash flows for repaying debt next year will be *larger* than the amount actually due.)

Does all this mean that coverage cannot be measured for debt related to governmental activities? Of course not. It merely points out an important fact: financial statements are a key source of information, but they are not the *only* source. You will need to obtain information from other publicly available documents, such as budgets and cash flow reports released by the government, offering statements that accompany bond issues, and reports prepared by oversight, legislative, and citizen groups. Ultimately, you also may need to approach the finance officers of the government directly to obtain what you require. The finance officers should be able to provide you with precise figures for cash flows and principal payments.

The coverage ratios are interpreted in much the same way as the liquidity ratios, comparing available (or likely to be available) resources with resource needs. A times-interest-earned ratio of 1.69 suggests that a government will have about 1.7 times as much cash as will be needed to make its annual interest payments on long-term debt (or, stated differently, a cushion of additional resources equal to 70 percent of interest payments). Similarly, the debt service coverage ratio implies resources 1.36 times (or 36 percent greater than) the amount expected to be needed to make interest and principal payments.

Ability to Pay

A set of ratios that address similar concerns as coverage ratios may be categorized as ability-to-pay ratios. By combining financial statement information with certain nonfinancial data and comparing the resulting ratios over time and with other, similar governments, you can gain insights into a government's financial capacity. These ratios compare revenues, expenses, and outstanding debts with economic indicators that imply a constituency's ability to pay for government services. Some of the necessary economic information may be in a government's CAFR; if it is not, or if a government does not prepare a CAFR, there are other easily accessible sources of the necessary information. (See **Tools of the trade…sources of other data.**)

If a CAFR is available, you will find information that is particularly useful for calculating ability-to-pay ratios related to debt. The statistical section of the CAFR includes a table that shows all of the overlapping debt of the multiple governmental entities that the taxpayers of a government are responsible for repaying. (Refer to Figure 38 in Part Six.) The table calculates the percentage of each overlapping government's outstanding governmental activities debt that is applicable to the government whose CAFR it appears in, adds it to the government's own outstanding governmental activities debt, and arrives at a cumulative figure. Some analysts may consider this cumulative amount more appropriate

for calculating ability-to-pay ratios because it provides a more complete picture of the debt burden borne by the taxpayers.

Ability to pay off liabilities

The pertinent economic indicators employed typically are those related to the economic activity that a government taxes or charges fees against for the purpose of repaying debt. Because debt frequently is financed with property taxes (by local governments) and income taxes (by state governments), standard comparisons would be debt to property values or personal income. A government's statistical section contains information about the value of property within its geographic boundaries, as well as personal income. (Refer to Figure 48 in Part Eight and Figure 96 in Part Thirteen.) Population also is commonly used for measures of ability to pay. To calculate these ratios for Local City, information about property value, personal income, and population is supplied in the following formulas:

debt per $100 of assessed property value =
(total debt outstanding × 100) ÷ total assessed property value
($79,318,111 × 100) ÷ 3,923,863,884 = $2.02
per $100 of assessed property value

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debt per $1,000 of personal income =
(total debt outstanding × 1,000) ÷ total personal income
($79,318,111 × 1,000) ÷ 8,000,000,000 = $9.91
per $1,000 of personal income

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debt per capita =
total debt outstanding ÷ total population
$79,318,111 ÷ 89,945 = $882 per person

With some additional economic and demographic information, you can produce other pertinent indicators. For example, the average family size in Local City is 2.4 persons:

average debt per family =
debt per capita × average family size =
$882 × 2.4 = $2,177 per family

These ratios include just bonds and other debt instruments, but they could be calculated with all liabilities—payables, NPL and NOL, claims and judgments, and so on.

Another way to approach the burden associated with repaying outstanding debt is to compare debt service expenditures with either total expenditures or total noncapital expenditures. If a government prepares a statistical section, it will present a ratio of debt service divided by total noncapital expenditures for the governmental funds in the schedule of changes in fund balances. The government in Figure 66 reported a ratio of 22.4 percent for fiscal year 20X9, meaning that repaying outstanding GO and other governmental activities debt accounted for close to a quarter of all noncapital expenditures.

If a government does not prepare a statistical section, you can calculate the ratio using information in the governmental funds statement of revenues, expenditures, and changes in fund balances (Figure 54):

[(principal expenditures + interest expenditures) ÷
(total expenditures – capital outlay)] × 100 =
[($3,450,000 + 5,215,151) ÷ (121,332,470 – 16,718,649)] × 100 = 8.28%

This type of analysis also could include annual payments on other long-term liabilities in addition to outstanding debt. For instance, the numerator of the preceding ratio also could include contributions to pension and OPEB plans and payments on claims and judgments. The result would be an indicator of how much of annual expenditures is devoted to paying off long-term obligations as a whole.

Special-purpose governments and business-type activities. For special-purpose governments and BTAs, long-term debt often is compared to relevant indicators of activity:

Public School District (see Figure C-1 in Appendix C)

long-term debt per student =
total long-term debt ÷ total student enrollment
($13,446,974 + 70,958,588) ÷ 9,250 = $9,125 per student

Public University (refer to Figure 88 in Part Eleven)

long-term debt per full-time equivalent (FTE) student
= total long-term debt ÷ FTE enrollment

($4,082,486 + 31,611,427) ÷ 3,035 = $11,760 per FTE student

Municipal Airport

debt per enplanement = total long-term debt ÷ total annual enplanements
$123,497,617 ÷ 1,264,381 = $97.67 per enplanement

Public Hospital

debt per admission = total debt outstanding ÷ annual patient admissions
($348,200 + 5,750,000) ÷ 2,215 = $2,753 per admission

Ability to raise revenues and pay for services

A common ability-to-pay ratio for revenues compares specific revenues with the economic base they are derived from. Such an equation produces an *effective tax rate*—an amount that represents the percentage of a particular economic base or economic activity that actually is paid in taxes. This can be very different from the nominal tax rate that is levied by the government. For example, a state may levy a 3 percent tax on personal income; however, because of exemptions and deductions, the personal income taxes that actually are paid in a given year will be less than 3 percent of total personal income. Calculating effective tax rates can be useful for comparative purposes when the governments you are examining apply more than one tax rate, such as a progressive income tax that rises with income or a property tax that applies higher rates to commercial and industrial property than to residential property. Care always should be taken, however, to make sure that the economic data you are using is consistent from government to government. This may be particularly true for property taxes. (See **Keep in mind…comparing assessed property values in multiple jurisdictions** on page 191.) The first of these three examples uses Local City information:

property tax revenues ÷ assessed property value =
$56,419,817 ÷ 3,923,863,884 = 0.01438, or 1.44%

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sales tax revenues ÷ total retail sales
$23,715,191 ÷ 524,253,000 = 0.04523, or 4.52%

---

income tax revenues ÷ total personal income
$191,328,165 ÷ 5,359,000,000 = 0.03570, or 3.57%

These types of ratios also can be calculated using the fees and charges for services of BTAs:

Public University (refer to Figure 89 in Part Eleven)

effective full-time tuition = tuition revenues ÷ FTE enrollment
$36,913,194 ÷ 3,035 = $12,163

Water Utility

effective water charge =
water customer revenues ÷ total water consumption
($10,015,310 ÷ 1,943,052,059 gallons) × 1,000 = $5.15 per 1,000 gallons

Dividing revenue and expense information by population provides a useful form of comparison across jurisdictions. The first two examples are for Local City:

health and sanitation expenses per capita = expenses ÷ total population
$6,738,672 ÷ 89,945 = $75 per person

---

taxes per capita = total taxes ÷ total population
($51,693,573 + 4,726,244 + 4,055,505 + 8,969,887) ÷ 89,945 = $772 per person

From the perspective of a city, county, or state government providing aid to a school district:

financial support per pupil =
payment to the school district ÷ total student enrollment
$21,893,273 ÷ 13,605 = $1,609 per student

From the perspective of the school district receiving aid:

intergovernmental aid per pupil =
operating grants ÷ total student enrollment
$44,258,475 ÷ 13,605 = $3,253 per student

These ratios can be used for making comparisons with similar governments, although you should be cautious to ensure comparability in the way governments measure the amount in the denominator.

The comparisons inform the issue of fiscal capacity by giving you a reference point; specifically, where the government you are analyzing stands relative to an index group of similar governments. If the government's ratio is lower than the comparison group average, it may suggest the government has additional revenue-raising or spending capacity that it can tap if necessary. A higher ratio may suggest the opposite. Any of these ratios also can be examined over time to determine if they are rising or falling. One way to build on the foregoing straightforward comparisons and provide some context for trend comparisons is to divide a specific government's ratio by the average of a relevant comparison group of similar governments. In this way, you can get a sense not just of how a government's ratios have changed in aggregate, but also of how the ratios have risen or fallen relative to changes in other governments.

Figure 102 compares ratios calculated in this section for Local City with a group of 10 other governments in its state with populations between 75,000 and 100,000.

Figure 102. Comparison of Ratios with Peer Governments

	(a) Local City	(b) Average of 10 Cities	(a) ÷ (b) Index
Debt per $100 of assessed property value	$ 2.02	$ 2.31	0.875
Debt per $1,000 of personal income	9.91	11.95	0.829
Debt per capita	882	1,070	0.824
Property tax revenues ÷ assessed property value	1.44	1.17	1.231
Taxes per capita	722	706	1.093

The first 3 comparisons suggest that Local City's debt burden is lower than that of the 10 comparison cities. All other things being equal, this might lead to a conclusion that it can afford to issue more debt if needed. However, if its debt is repaid with property tax revenues, the last two comparisons might temper that conclusion. Local City's property tax burden is higher than that of the 10 comparison cities, suggesting that it is less able to raise property taxes to repay more GO debt. The solution for Local City might be to issue debt that is backed by a revenue other than the property tax, which would take advantage of the capacity it has for issuing more debt (by comparison with the 10-city average) without further increasing its high property tax burden (relative to the other cities).

Revenue-Backed Debt

The ratio analysis discussed thus far can be useful for examining governments with revenue-backed debt, as well as those with GO and TAX-BACKED DEBT. It is valuable, for instance, to compare GO and tax-backed debt to the broad tax bases from which revenues will be raised to repay them. However, revenue-backed debt is repaid with a *specific* revenue source (or sources, occasionally) generated by a particular activity (generally a BTA) and not with a government's general resources. (Of course, this also would be the case for a BTA government like a public utility, all or most of whose debt is repaid with revenue from fees and charges. The discussion that follows applies equally to BTAs.) In other words, the performance of a specific revenue is more important than the general, overall financial health of the government, because the general resources of the government are not available to repay revenue-backed debt. To analyze revenue-backed debt, therefore, other ratios have been developed using only the financial information related to the activity generating the revenue backing the debt.

One ratio is the previously discussed liquidity measure, days cash on hand. This ratio is a similarly conservative measure as the quick ratio, focusing not on current assets but on cash and near-cash investments. The ratio is calculated below for Local City's water and sewer utility (Figures 68 and 69):

days cash on hand =

([cash + cash equivalents] ÷ [operating expenses − depreciation expense]) × 365 = ($8,416,653 ÷ [6,907,756 − 1,163,140]) × 365 = 535 days of cash on hand

The utility has enough cash on hand to cover its operating expenses (less noncash expenses like depreciation) for almost a year and a half (535 days). This ratio can be interpreted much like other liquidity ratios—lower ratios may raise concerns about a government's ability to pay its bills on time, whereas higher ratios may indicate that a government has excess cash on hand that could be invested to produce additional income.

A twist on coverage ratios is the maximum annual debt service (MADS) coverage ratio. Whereas coverage ratios typically place the most recent year's actual debt service in the denominator, MADS employs the highest future annual debt service payment. This amount may not be obtainable from the financial report, depending on when the maximum payment is expected to occur. As illustrated in Figure 43, governments are required to disclose their required debt service payments for each of the next five years, and then in five-year increments until the debt is totally paid off. It may not be possible to identify the maximum debt service payment because of the aggregation beyond the fifth year. One possible solution would be to calculate average annual debt service payments for each of the five-year periods by dividing the total debt service for the period by five. If you do this for the water and sewer bonds in Figure 43, you will find that none of the five-year averages would be the maximum debt service. That occurs in fiscal year 2021, when the debt service requirement is $8,151,000. The MADS coverage ratio using that amount would be (for this purpose, we will assume that Figure 43 relates to Local City):

maximum annual debt service coverage = (net income + depreciation + interest expense) ÷ maximum annual debt service = ($4,422,127 + 1,163,140 + 1,600,830) ÷ 8,151,000 = 0.88

Other ratios for revenue-backed debt adapt previously discussed ratios to the financial information that is available for activities that issue it. For instance, you might calculate debt service as a percentage of operating revenues (Figures 69 and 70), instead of the ratio of debt service to noncapital governmental funds expenditures. (See Figure 66.) Rather than a ratio of liabilities to assets or net position, you might calculate this leverage ratio: outstanding long-term debt divided by total capital (long-term debt plus unrestricted net position). The approach to analyzing these ratios basically is the same as for similar ratios discussed elsewhere in this part of the guide.

Pension and OPEB Information

As we saw in Parts Five and Six, the required disclosures about governmental pension and OPEB systems contain not only raw financial information but also three ratios calculated from them:

- Asset sufficiency ratio—fiduciary net position divided by the TPL or TOL. You also could calculate an *insufficiency* ratio by dividing the NPL by the TPL (or the NOL by the TOL).

- Net liability-to-payroll ratio—the NPL or NOL divided by the payroll on which contributions to the plan are based (or total payroll for some governments; see **By the numbers…OPEB and covered-employee payroll** on page 127).
- Employer contributions—a government's actual contributions to its pension plan divided by payroll.

These disclosures were designed to give users of financial statements some of the information they need to evaluate the financial health of the pension or OPEB plan, as well as the participating government.

If a government contributes less than its actuarially determined contribution (ADC), a ratio of its actual contribution divided by the ADC, subtracted from one, indicates the degree to which it falls short of meeting its contribution needs.

There are ratios like the ratio of debt service divided by noncapital expenditures (discussed previously) that speak to the burden of satisfying the NPL or NOL. For example, *actual contributions* to a pension or OPEB plan (from the related notes to financial statements) *divided by noncapital expenditures* (from the governmental funds financial statements) indicates the share of annual expenditures that are devoted to providing assets to the pension or OPEB plan. Alternatively, *pension or OPEB expense* (from the related notes) *divided by total governmental activities expenses* (from the government-wide statement of activities) helps you to evaluate the portion of a government's annual cost of services that results from its promises to provide retiree benefits.

Risk

The flip side of ability-to-pay is *exposure to risk*. The same factors that reveal a government's capacity to make ends meet and to finance necessary services also reflect on a government's ability to withstand financial difficulties. Revenue dispersion, for example, addresses the risk of a government's reliance on a single revenue source. Bowman and Calia[1]espouse two other ratios for assessing risk—RISK EXPOSURE RATIO and TAX LEVERAGE RATIO. (Bowman and Calia's work on governmental financial analysis, written before governments began preparing government-wide financial statements, is adapted slightly here.)

The risk exposure ratio focuses on revenue sources that are potentially subject to large, abrupt changes, specifically investment income and intergovernmental aid. The ratio expresses the percentage increase in property taxes that would be required to make up for a 1 percent shortfall in those two sources of funding. It is calculated below using Local City's statement of activities (Figure 42):

risk exposure ratio =

[1] Woods Bowman and Roland Calia, *Evaluating Local Government Financial Health: Financial Indicators for Cook, DuPage, Kane, Lake, McHenry and Will Counties* (Chicago: The Civic Federation, 1997), and Woods Bowman and Roland Calia, *Evaluating Local Government Financial Health: Financial Indicators for Major Municipalities in Northeastern Illinois* (Chicago: The Civic Federation, July 1999).

(investment revenue + intergovernmental aid) ÷
unrestricted property tax revenue
($1,958,144 + 5,176,310 + 4,894,915 + 1,457,820) ÷ (51,693,573) = 0.2609

In other words, a 1 percent shortfall in those revenues would require a 0.26 percent increase in the general purpose property tax levy. (General purpose is emphasized here because, if a government has a separate levy for debt service or another specific purpose, you would not want to include those revenues. The reason is simple—those levies can be raised only for debt service or the other specific purpose.)

You can compare this information with what you find by calculating measures of ability to pay. A high risk exposure ratio could be cause for concern if a government does not have much available capacity to raise taxes or to borrow because its taxes and debt already are relatively burdensome compared with other, similar governments. That government may not have the financial wherewithal to effectively respond to a downturn in those revenue sources.

The tax leverage ratio, like risk exposure, is expressed as a percentage increase in property taxes. In this case, the ratio shows how much property tax revenue would need to increase to cover a 1 percent increase in costs. This is how the ratio is calculated using Local City information (in order to get operating expenses, you first need to remove depreciation and interest on long-term debt):

tax leverage ratio =
operating expenses ÷ unrestricted property tax revenue
($105,807,013 – 4,387,000 – 6,068,121) ÷ 51,693,573 = 1.8445

The result shows that a 1 percent increase in operating expenses would require an increase in property taxes of more than 1.8 percent. With the tax-raising capacity information in hand, you can utilize the tax leverage ratio to assess a government's ability to react to an unplanned increase in costs.

Financial Efficiency

Financial efficiency ratios comprise a set of commonly used ratios in business financial analysis. These ratios are used to assess the efficiency with which a firm utilizes resources such as accounts receivable. Efficiency ratios are not as frequently applied to governments, but they are nevertheless informative about a government's ability to collect on the taxes and charges it levies. This information clearly bears on a government's ongoing financial viability: if it cannot collect its revenues, it may not be able to pay its own bills.

Receivables

A simple approach to analyzing receivables is to directly divide ending receivables by their related revenues. A **RECEIVABLES EFFICIENCY RATIO** for property taxes might look like this (note that the amounts in the receivables and payables ratios that follow are *not* from Local City's financial statements):

(property taxes receivable ÷ property tax revenues) × 100 =
($7,117,832 × (121,398,078 ÷ 100 = 5.86%

This ratio enables you to track whether a government is collecting more or less of its property taxes over time. The lower the ratio, the more that is being collected (or, conversely, the less that remains uncollected). If this ratio were to rise over time, for instance, it might indicate that property owners are having greater difficulty making their payments, which may be an indication of broader economic problems. Alternatively, the government may not be doing as good a job at collecting on late tax payments; perhaps the number of enforcement staff has declined.

Another way to look at receivables is a **RECEIVABLES TURNOVER RATIO:**

property tax revenues ÷ average property taxes receivable =
$121,398,078 ÷7,789,448 = 15.58

(Average property taxes are obtained by adding this year's and last year's property tax receivable amounts and dividing by two.) This ratio indicates how quickly a government collects on amounts that it is owed; a higher ratio indicates quicker collection. It might be easier for you to understand if you divide 365 days by the ratio. In the sample calculation above, that would be a little more than 23 days.

An alternative ratio that directly results in the number of days to collect is the **DAYS RECEIVABLE RATIO,** which shows how long, on average, it takes to collect on receivables:

days property tax receivable =
(average property tax receivables × 365) ÷ property tax revenue
($7,789,448 × 365) ÷ 121,398,078 = 23.42

This result can be placed in a meaningful context by examining the ratio for previous years and for other, similar governments. It also can be examined in light of the property tax collections information presented in the statistical section, which tracks the percentage of property tax levies that a government actually collects. (Refer to Figure 52 in Part Eight.)

Payables

Similar ratios can be calculated for payables. For example, you might divide a government's vendors payable at the end of the fiscal year by its supplies expense for the year.

PAYABLES EFFICIENCYRATIO for supplies:

(vendors payable ÷ supplies expense) × 100 =
($8,389,022 × (77,000,823 ÷ 100 = 10.89%

The lower the ratio, the less the government owes to the vendors from which it purchases supplies. If this ratio were to rise over time, it might indicate that the government is having difficulty making its payments. This might mean the government is slowing down payments because it is short on cash, or that it has fewer employees processing bills. As with other ratios, it is a stepping-off point for further exploration.

PAYABLES TURNOVER RATIO:

supplies expense ÷ average vendors payable =
$77,000,823 ÷ 7,912,765 = 9.73

This ratio indicates how quickly the government is paying its bills; a higher ratio indicates quicker payment. Even more than the receivables turnover ratio, the payables turnover ratio benefits from conversion into days. In the sample calculation above, 365 divided by 9.73 equals 37.5 days on average to make payments on vendors payable.

DAYS PAYABLES RATIO:

days grants payable =
(average grants payable × 365) ÷ grant expense
($7,912,765 × 365) ÷ 77,000,823 = 37.51

Risk pools

The days receivable ratio also could be adapted to examine risk pool information. The ratio could be used to contrast a pool's claims processing activity with the flow of claims during the year. This adapted measure can be called a **DAYS UNPAID CLAIMS RATIO**, which tells you, on average, how long it takes to process claims. The calculations below utilize the Public Insurance Fund information for 2016 from Figure 33.

days unpaid claims =
(average unpaid claims × 365) ÷ claims paid
([{$659 + 476} ÷ 2] × 365) ÷ 573 = 361.5

On average, the Public Insurance Fund took nearly a whole year (361.5 days) to pay claims. Did this performance improve or decline in 2017?

([{$941 + 659} ÷ 2] × 365) ÷ 747 = 390.9

In 2017, it took the Fund approximately 391 days on average to pay claims, or almost 1 month longer than in 2016. On the face of it, the Fund appears to have gotten less efficient, though further investigation is warranted to determine the causes of the increase in the average claims payment period.

Inventory

Although efficiency ratios also are applied to the inventory of private firms, they are not as commonly applied to governmental entities because government inventories typically are not goods for sale (they

are more likely supplies used in operations). Nonetheless, in cases in which a specific type of inventory can be discretely identified, or in which a governmental entity indeed engages in the sale of goods, efficiency ratios can be useful. Consider a municipal garage that must keep on hand a supply of tires for the municipality's automobiles. Each year, the garage must finance the cost of storing the tires; if it could keep less tires on hand at any given time, it might be able to lower its warehousing costs. In order to keep less on hand but still meet its need for tires, the garage would need to purchase tires more frequently; in other words, the supply of tires would "turn over" more rapidly. The **DAYS INVENTORY RATIO** can be used to measure inventory efficiency; it is calculated below using numbers for a municipal garage.

days inventory =
(average inventory balance × 365) ÷ cost of inventory used
([{$1,231 + 2,006} ÷ 2] × 365) ÷ 10,568 = 55.9

The garage's supply of tires turned over every 56 days on average. When compared over time and with similar garages in other governments, this ratio can be used to judge efficiency. Generally, the lower the number, the more efficient the use of inventory, all other factors being equal. This garage might decide to keep less on hand and order more frequently if the savings from less storage outweighed the costs of more frequent purchases. If it did so, the garage's days inventory ratio would be lower. Alternatively, it might find that the benefits of ordering less frequently—such as volume discounts—outweigh the added costs of storage. In addition, governments may attempt to hedge against rising prices by buying more than they need at present and storing it for the future.

Capital assets

Another way in which efficiency ratios are employed relates to capital assets. In the section on capital asset disclosures in Part Four, there is a discussion of a ratio that measures the remaining useful lives of capital assets. Using information on buildings and improvements from the note disclosure for Local City in Figure 12:

CAPITAL ASSET DEPLETION RATIO:

[(historical cost – accumulated depreciation) ÷ historical cost] × 100 =
[($40,695 – 11,049) ÷ 40,695] × 100 = 72.8%

As stated in Part Four, this ratio declined from the preceding fiscal year, when it was 74.1 percent, meaning that the average remaining lives of Local City's buildings shrank.

Whereas this ratio measures the capital assets a government has for use going forward at a specific point in time, another ratio measures whether a government is replenishing its capital assets. The **CAPITAL ASSET REPLENISHMENT RATIO** also helps to explain why the depletion ratio is increasing or decreasing over time. Using information from Figure 12 and the governmental funds statement of revenues, expenditures, and changes in fund balances in Figure 54:

capital expenditures ÷ depreciation expense =
$16,719 ÷ 4,387 = 3.81

Anytime this ratio exceeds 1.0, it means that the government is adding more to its stock of capital assets than is being lost to physical deterioration (as estimated by depreciation). The ratio for Local City for fiscal year 2017 reflects a level of investment in new capital assets or improvements to existing ones that far exceeds the pace of depreciation. However, it should be noted that capital expenditures can rise and fall significantly from year to year—they tend be *lumpy,* because more capital projects are completed in some years than in others and, for smaller governments, large capital investments may happen infrequently. In other words, Local City's capital expenditures were much higher than depreciation expense in 2017, but they could be lower in the next year or several years.

Service Capacity

Much of the information needed to analyze fiscal capacity can be found in a government's CAFR. By contrast, most of the information necessary to evaluate service capacity is found elsewhere. As a guide to financial statements, this is not the place to delve too deeply into service capacity.[22] However, a brief overview of the kinds of service capacity information and identification of the relevant information that *can* be found in the CAFR are in order.

The information that most directly informs service capacity is called **SERVICE EFFORTS AND ACCOMPLISHMENTS (SEA) INFORMATION.** SEA information can be aggregated into four groups—inputs, outputs, outcomes, and service efficiency. **INPUTS** measure the money, labor, and capital that a government employs to provide services. The entire financial report speaks to monetary inputs.

Capital inputs are addressed in the note disclosures (Figure 12 in Part Five), in the RSI if a government uses the modified approach (Figure 32 in Part Six), in the statistical section schedule of capital indicators (Figure 35 in Part Six), and in the capital assets schedule that some governments voluntarily present as SI (Figure E-4). Labor information can be found in the statistical section schedule of government employees (Figure 98 in Part Thirteen).

OUTPUTS are the services that a government provides with the use of the inputs. Measures of outputs include the number of people served (students enrolled in public schools, persons receiving income support, passengers), the level of activity (gallons of wastewater treated, average daily jail population, tons of garbage collected), and other indicators of *how much service* was provided. Some output information can be found in the statistical section schedule of operating indicators (Figure 99 in Part Thirteen).

[2] Instead, see Paul Epstein, James Fountain, Wilson Campbell, Terry Patton, and Kimberly Keaton, *Government Service Efforts and Accomplishments Performance Reports: A Guide to Understanding* (Norwalk, CT: GASB, 2005).

OUTCOMES measure the degree to which a government has achieved the goals of a service. For example, output measures of police protection might be the number of 911 responses, the number of arrests, or the average number of daily patrols, but the *outcome* measures of the service might be the percentage of citizens stating that they feel safe, the number of crimes committed per capita, the clearance rate (the percentage of reported crimes that result in an arrest), or the time it takes police to respond to emergency calls. The specific measures used depend upon the goals established by the government. In general, outcomes measure the **EFFECTIVENESS** of services at accomplishing what they are intended to do. Another way to describe outcomes is that they measure the *quality* of government services.

SERVICE EFFICIENCY indicators (as distinguished from the *financial* efficiency ratios discussed earlier) measure how much service can be provided (inputs divided by outputs, or vice versa) or what level of effectiveness can be achieved (inputs divided by outcomes, or vice versa) given a certain level of input. Output-input measures most often include spending, employment, and population. Examples of output-input measures include: expenses or expenditures per child inoculated, faculty per FTE student, police officers per capita, expenses (or expenditures) per ton of garbage collected, and daily average number of building inspections conducted per fire inspector. Examples of outcome-input measures include: instructional expenses (expenditures) per student graduating and continuing on to college; expenses (expenditures) per drug or alcohol abuse patient successfully treated; or children in foster care successfully adopted per caseworker.

Although SEA information generally is nonfinancial, some of the general analytical techniques employed for financial analysis can be applied to analyzing service capacity information. For example, percentage change can be used to measure whether service levels, effectiveness, and efficiency are improving or declining over time.

OTHER RELEVANT RATIOS AND INFORMATION

The ratios that you could calculate to produce decision-useful information certainly are not limited to those presented thus far. Nor, for that matter, is the information relevant to a government's economic condition limited to that found in a government's financial statements or its CAFR. For example, in a report prepared for the GASB,[33] Berne cited a lengthy list that included many of the measures already discussed in this guide, as well as these:

[3] Robert Berne, *The Relationships between Financial Reporting and the Measurement of Financial Condition* (Norwalk, CT: Governmental Accounting Standards Board, 1992).

Selected Measures of Economic Condition

Economy and demographics

Population (age distribution [especially over 65 and under 18], education levels)
Income (per capita, per family; averages, medians)
Labor force and employment (total employment, participation rates, unemploy- ment rates, employment by industry and occupation)
Industrial structure (export employment and earnings)

Revenue base

Property base (by categories; building permits)
Sales tax base
Income tax base
Other tax bases
Revenue base elasticities

Revenues

Legal limits and percentages of limits currently used
Tax and revenue reserves
Intergovernmental revenues and distribution systems

Current and capital expenditures

Measures of expenditure needs and costs (poverty levels, crime measures, population density, cost and price indexes, age of housing, health data)
Risk management
Measures of service efforts and accomplishments (miles of streets paved, reading and math achievement scores, tons of trash per worker, and so on)

Debt

Outstanding debt by security (to determine debt of the government, separate from enterprises)
Maturity structure of debt, including average years to maturity and percent of debt to mature in 10 years
Debt service compared to total and own source revenues

Pensions and OPEB

Pension/OPEB structure and funding methods
Pension/OPEB receipts compared to pension disbursements
Pension/OPEB earnings compared to benefits

Internal resources

Fund balances (compared to revenues, compared to population)
Surpluses and deficits (total, compared to revenues)
Tax delinquencies and other collection and payment rates
Receipts and disbursements and short-term borrowing
Transfers to and from other funds and enterprises

COMMON-SIZE RATIOS measure the magnitude by which an amount has increased or decreased over time (percentage change) or the proportion an amount represents of a larger group of amounts (percentage distribution)

LIQUIDITY RATIOS measure the availability of cash and other assets that can be converted to cash promptly for the purpose of satisfying liabilities

SOLVENCY RATIOS measure a government's ability to finance its long-term liabilities

LEVERAGE RATIOS measure the degree to which a government's assets have been financed with the use of debt and other long-term liabilities

COVERAGE RATIOS measure the sufficiency of revenue streams to make debt service payments

ABILITY-TO-PAY RATIOS measure affordability by comparing financial and nonfinancial data

Upon further review...other ways to apply percentage distributions

Although the percentages in Figure 101 are calculated using total primary government data, you could just as easily calculate them for the governmental activities or BTAs or for the component units. Furthermore, instead of columns, you could calculate percentage distributions in rows; for instance, what percentage of a government's total investments is held by the BTAs versus governmental activities?

Keep in mind...liquidity and the property tax calendar

As with other financial ratios, one must consider the results of liquidity calculations within the context of the particular government's environment. An important aspect of that environment is when its large revenue sources are expected to be received. For example, one might be less concerned about a low end-of-year liquidity ratio if a government receives substantial tax payments or intergovernmental aid shortly after the beginning of the year. An important source of information about the timing of tax receipts is the property tax calendar, which governments present in their SSAP note. The calendar relates when taxes are levied, when payments are expected, and when overdue payments are considered delinquent. This information also can help you judge whether the property tax receivables a government reports in its financial statements can be included among its current resources for paying bills.

Upon further review...are high coverage ratios always desirable?

From the perspective of investors, the higher the coverage ratio is, the more secure they feel about the government's ability to repay the money it borrowed. However, "the higher" may not always be "the better." Some observers believe high coverage ratios may imply that a government is charging too much or taxing too much for the services it provides, thereby generating large, unneeded surpluses; conversely, it may be said that the government is not providing enough services for the amounts it taxes and charges. Keep in mind, however, that there are few absolutes in financial analysis. An alternative explanation could be that a government is deliberately generating surpluses to accumulate resources to replace an old bridge or to buy a building.

Sources for information in coverage ratios calculations:

Cash flows from proprietary funds cash flows statement (Figure 70)

Interest expense from statement of revenues, expenses, and changes in fund net position (Figure 69)

Debt service equals interest expense plus principal repayments, which come from the long-term liabilities note (Figure 16)

Interest for governmental and business-type activities: government-wide statement of activities (Figure 42) and proprietary funds statement of revenues, expenses, and changes in fund net position (Figure 69), respectively

Principal repayments for governmental activities and *excess/deficiency:* governmental funds statement of revenues, expenditures, and changes in fund balances (Figure 54)

Principal repayments for BTAs: proprietary funds cash flows statement (Figure 70)

Tools of the trade...sources of other data

Some of the economic data you might want to use for financial ratios can be found in the statistical section. If it is not there, it is easy to go to the source the government probably got the data from in the first place—the federal government. These agencies have websites with online statistics:

Bureau of the Census: social and economic characteristics of population, poverty, retail trade <www.census.gov>

Bureau of Economic Analysis: personal income, gross state product <www.bea.gov>

Bureau of Labor Statistics: employment, unemployment, inflation rates <www.bls.gov>

Bureau of Justice Statistics: crime rates, inmates in jail, drug use <www.bjs.gov>

Bureau of Transportation Statistics: highway statistics, passenger levels, aviation <www.bts.gov>

Environmental Protection Agency: pollution, environmental quality <www.epa.gov>

National Center for Education Statistics: elementary and secondary education and higher education information <nces.ed.gov>

National Center for Health Statistics: birth and mortality rates, life expectancy, disease rates www.cdc.gov/nchs

Professional organizations that represent different kinds of BTAs also may be sources of information:

Airports Council International <www.airports.org>

American Association of State Colleges and Universities <www.aascu.org>

American Hospital Association <www.aha.org>

American Public Power Association <www.publicpower.org>

American Public Transportation Association <www.apta.com>

American Public Works Association <www.apwa.net>

American Water Works Association <www.awwa.org>

Association of American Colleges and Universities<www.aacu.org>

Association of Public and Land-Grant Universities <www.aplu.org>

Healthcare Financial Management Association <www.hfma.org>

National Association of College and University Business Officers <www.nacubo.org>

Upon further review…an example of trend and cross-government comparisons

Your examination of liquidity may be more useful if you compare the government you are analyzing with other, similar governments and with itself over time. Consider Hobbiton County, which has current assets that are 1.2 times greater than its current liabilities—perhaps you are concerned that this is not high enough. But what if you knew that this had risen steadily over the past 5 years from just 0.6? The fact that Hobbiton County's liquidity was improving might allay your concerns. On the other hand, you might become more worried if you learned that the ratio had been declining over the past few years. What if you knew that, on average, other counties similar to Hobbiton County had an average ratio of current assets to current liabilities of 0.9? In such a light, Hobbiton County's situation seems brighter. Conversely, if the average ratio were higher than Hobbiton County's, you might be more concerned.

Upon further review…property tax receivables

Some caution needs to be shown with property tax receivables information. Property taxes are recorded as receivables of a government as soon as the government has a legally enforceable claim to them (the lien or levy date). However, the taxes may not actually be due until months later. If this were the case, the efficiency ratio could be greatly overstated; in other words, the ratio would make the government look much less efficient than it actually is. To avoid misinterpretation, you should review the information governments disclose in the notes to financial statements regarding the property tax calendar and revenue recognition policies in the SSAP.

APPENDIX A

FIGURE A. MANAGEMENT'S DISCUSSION AND ANALYSIS

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of Local City's annual financial report presents our discussion and analysis of the City's financial performance during the fiscal year that ended on December 31, 2017. Please read it in conjunction with the transmittal letter at the front of this report and the City's financial statements, which immediately follow this section.

FINANCIAL HIGHLIGHTS

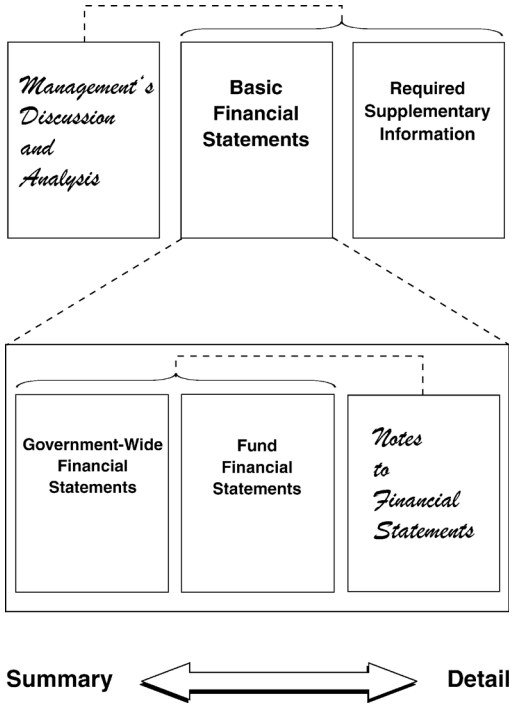
- The City's total net position remained virtually unchanged over the course of this year's operations. However, whereas the net position of our business-type activities *increased* $3.2 million (4 percent), this was offset by a *decrease* of $3.1 million (almost 9 percent) in the net position of our governmental activities.
- The City's assets grew nearly 4 percent, but the increase in liabilities was 3 times greater due to significant issuances of new bonds (12 percent increase) and growth in the net liabilities for pensions and retiree health insurance (13 percent).
- During the year, the City's expenses were $6.3 million more than the $99.5 million generated in taxes and other revenues for governmental programs (before special items). This is better than last year, when expenses exceeded revenues by $8.9 million.
- In the City's business-type activities, revenues increased close to 6 percent to $15 million, while expenses decreased almost 2 percent.
- The general fund reported a deficit this year of $1.3 million despite one-time proceeds of $3.5 million from the sale of some of our park land.
- The resources available for appropriation were $1.1 million less than budgeted for the general fund. However, we kept expenditures within spending limits primarily through a midyear hiring and overtime freeze and our staff restructuring efforts.

OVERVIEW OF THE FINANCIAL STATEMENTS ①

This annual report consists of three parts—*management's discussion and analysis* (this section), the *basic financial statements*, and *required supplementary information*. The basic financial statements include two kinds of statements that present different views of the City:

- The first two statements are *government-wide financial statements* that provide both *long-term* and *short-term* information about the City's *overall* financial status, including its component units.
- The remaining statements are *fund financial statements* that focus on *individual parts* of the City government, reporting the City's operations *in more detail* than the government-wide statements.
  - The *governmental funds* statements tell how *general government* services such as police and parks were financed in the *short term* as well as what remains for future spending.
  - *Proprietary funds* statements offer *short-* and *long-term* financial information about the activities for which the City charges a fee to customers, such as the water and sewer system.
  - *Fiduciary funds* statements provide information about the financial relationships in which the City acts solely as a *trustee* or *agent* for the benefit of those outside of the government, to whom the resources in question belong.

Figure A-1
Required Components of
Local City's Annual Financial Report



The financial statements also include *notes* that explain some of the information in the financial statements and provide more detail. The notes are followed by a section of *required supplementary information* that further explains and supports certain information in the financial statements. Figure A-1 shows how the required parts of this annual report are arranged and are related to one another. In addition to these required elements, we have included a section with combining statements that provide

details about our nonmajor governmental funds and internal service funds, each of which are added together and presented in single columns in the basic financial statements.

Figure A-2 summarizes the major features of the City's financial statements, including the portion of the City government they cover and the types of information they contain. The remainder of this overview section of management's discussion and analysis explains the structure and contents of each of the statements.

Government-Wide Statements

The government-wide statements report information about the City as a whole, using an accrual basis of accounting and economic resources measurement focus. Consequently, the statement of net position includes *all* of the government's assets and liabilities, as well as deferred inflows of resources and deferred outflows of resources (deferrals). All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the City's net position and how it has changed. Net position—essentially the difference between the City's assets and liabilities—is one way to measure the City's financial health.

- Over time, increases or decreases in the City's net position are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City, you need to consider additional factors such as changes in the City's property tax base and the condition of the City's roads.

In the government-wide financial statements, the City's activities are divided into three categories:

- *Governmental activities*—Most of the City's basic services are included here, such as the police, fire, public works, and parks departments, and general administration. Property taxes and state and federal grants finance most of these activities.
- *Business-type activities*—The City charges fees to customers to help cover the costs of certain services it provides. The City's water and sewer system and parking facilities are included here.
- *Component units*—The City includes two other entities in its report—the Local Public School District and the Local City Landfill Authority. Although legally separate, these "component units" are important because the City is financially accountable for them.

Figure A-2
Major Features of Local City's Government-Wide and Fund Financial Statements

		Funds Statements		
	Government-Wide	**Governmental Funds**	**Proprietary Funds**	**Fiduciary Funds**
Scope	Entire City government (except fiduciary activities such as the employee retirement plan)	The activities of the City that are not proprietary or fiduciary, such as police, fire, and parks	Activities for which the City charges a fee to customers: the water and sewer system and the parking facilities	Instances in which the City is the trustee or agent for resources belonging to others, such as the employee retirement plan
Required financial statements	• Statement of net position • Statement of activities	• Balance sheet • Statement of revenues, expenditures, and changes in fund balances	• Statement of net position • Statement of revenues, expenses, and changes in fund net position • Statement of cash flows	• Statement of fiduciary net position • Statement of changes in fiduciary net position
Accounting basis and measurement focus	Accrual accounting and economic resources measurement focus	Modified accrual accounting and current financial resources measurement focus	Accrual accounting and economic resources measurement focus	Accrual accounting and economic resources measurement focus
Type of asset/liability information	All assets and liabilities, both financial and capital, short term and long term	Generally, assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets or long-term liabilities included	All assets and liabilities, both financial and capital, short term and long term	All assets and liabilities, both financial and capital, short term and long term
Type of inflow/outflow information	All revenues and expenses during the year, regardless of when cash is received or paid	Revenues for which transactions have occurred and cash is received during or soon after the end of the year; expenditures when goods or services have been received and the required liability is normally due and payable	All revenues and expenses during the year, regardless of when cash is received or paid	All additions to and and deductions from fiduciary net position during the year, regardless of when cash is received or paid

Fund Financial Statements

The fund financial statements provide more detailed information about the City's most significant *funds*—not the City as a whole. Funds are accounting devices that the City uses to keep track of specific sources of funding and spending on particular programs.

- Some funds are required by State law and by bond covenants.
- The City Council establishes other funds to control and manage money for particular purposes (like the Route 7 reconstruction project) or to show that it is properly using certain taxes and grants (like aid from the U.S. Department of Housing and Urban Development).

The City has three kinds of funds:

- *Governmental funds*—Most of the City's basic services are included in governmental funds, which focus on (1) how *cash and other financial assets* that readily can be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed *short-term* view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because this information does not encompass the additional long-term focus of the government-

wide statements, we provide additional information at the bottom of the governmental funds statements that explains the relationship (or differences) between them.

- *Proprietary funds*—Services for which the City charges customers a fee generally are reported in proprietary funds. Proprietary funds report the same types of information as the government-wide statements.
  - In fact, the City's *enterprise funds* (one type of proprietary fund) are the same as its business-type activities, but they provide more detail and additional information, such as cash flows.
  - We use *internal service funds* (the other kind of proprietary fund) to report activities that provide supplies and services for the City's other programs and activities—such as the City's Telecommunications Fund.
- *Fiduciary funds*—The City is the trustee, or *fiduciary,* for its employees' pension plan. It also is responsible for other assets that—because of a trust arrangement—can be used only for the trust beneficiaries. The City is responsible for ensuring that the assets reported in these funds are used for their intended purposes. All of the City's fiduciary activities are reported in a separate statement of fiduciary net position and a statement of changes in fiduciary net position. We exclude these activities from the City's government-wide financial statements because the City cannot use these assets to finance its operations.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE ②

Net position. The City's *combined* net position was virtually unchanged between fiscal years 2016 and 2017—increasing slightly to $116.8 million. (See Table A-1.) In contrast, net position *decreased* $6.2 million last year. Looking at the net position and net expenses of governmental and business-type activities separately, however, two very different stories emerge.

Net position of the City's governmental activities decreased 8.6 percent to $32.7 million. However, all of the resources represented by that net position either are restricted to specific purposes or are invested in capital assets (buildings, roads, bridges, and so on). Consequently, *unrestricted* net position had a $93.7 million *deficit* at the end of this year. This deficit does not mean that the City does not have resources available to pay its bills next year. Rather, it is the result of having *long-term* commitments that are greater than currently available resources. Specifically, the City's net pension liability and net other postemployment benefit (OPEB) liability—the difference between the total amount owed to employees and retirees and the value of assets set aside in trusts that meet specific criteria in the accounting standards—amounted to $100.3 million this year, a 13.1 percent increase over 2016. These two liabilities represent virtually half of all liabilities. Furthermore, the City did not include in past annual budgets the full amounts needed to finance future liabilities arising from property and casualty claims and to pay for unused employee vacation and sick days. The City will include those amounts in future years' budgets as they come due.

In addition, the deficit in unrestricted governmental net position was adversely affected by two particular features of the City's recent financial activity:

- During the past two years, tax revenues and State grants fell short of expectations.
- The City Council used accumulated cash balances to avoid tax increases.

Although the net position of our business-type activities increased by 4.0 percent to $84.1 million, these resources cannot be used to make up for the net position deficit in governmental activities. The City generally can use business-type activities resources only to finance the continuing operations of the water and sewer and parking operations.

Table A-1
Local's Net Position
(in millions of dollars)

	Governmental Activities		Business-Type Activities		Total		Total Percentage Change
	2016	2017	2016	2017	2016	2017	2016–2017
Current and other assets	$ 50.4	$ 54.3	$ 61.9	$ 62.9	$ 112.3	$ 117.2	4.4%
Capital assets	162.1	170.0	147.6	151.4	309.7	321.4	3.8
Total assets	**212.5**	**224.3**	**209.5**	**214.3**	**422.0**	**438.6**	3.9
Total deferred outflows	**4.8**	**16.8**	**2.2**	**8.0**	**7.0**	**24.8**	**254.4**
Long-term debt outstanding	63.3	79.3	77.3	78.3	140.6	157.6	12.1
Net pension & OPEB liabilities	90.6	100.3	45.2	53.3	135.8	153.6	13.1
Other liabilities	22.6	21.8	1.7	1.4	24.3	23.2	(4.7)
Total liabilities	**176.5**	**201.4**	**124.2**	**133.0**	**300.7**	**334.4**	**11.2**
Total deferred inflows	**5.0**	**7.0**	**9.0**	**5.2**	**14.0**	**12.2**	**(12.9)**
Net position							
Net investment in capital assets	100.3	103.7	71.6	73.1	171.9	176.8	2.9
Restricted	27.1	22.8	2.8	1.5	29.9	24.2	(18.9)
Unrestricted	(91.6)	(93.7)	6.5	9.6	(89.5)	(84.1)	(6.0)
Total net position	**$ 35.8**	**$ 32.7**	**$ 80.9**	**$ 84.1**	**$ 116.7**	**$ 116.8**	**0.1**

Note: Totals may not add due to rounding.

Changes in net position. The City's total revenues (excluding special items) increased by 4 percent to $114.5 million. (See Table A-2.) Virtually half of the City's revenue comes from property taxes, and 60 cents of every dollar raised comes from some type of tax. (See Figure A-3.) Another quarter comes from fees charged for services, and most of the rest is State and federal aid.

The total cost of all programs and services was virtually unchanged (increasing $800,000, or less than 1 percent). The City's expenses cover a range of services, with about half related to public safety and education. (See Figure A-4.)

Figure A-3

Sources of Local's Revenues for Fiscal Year 2017

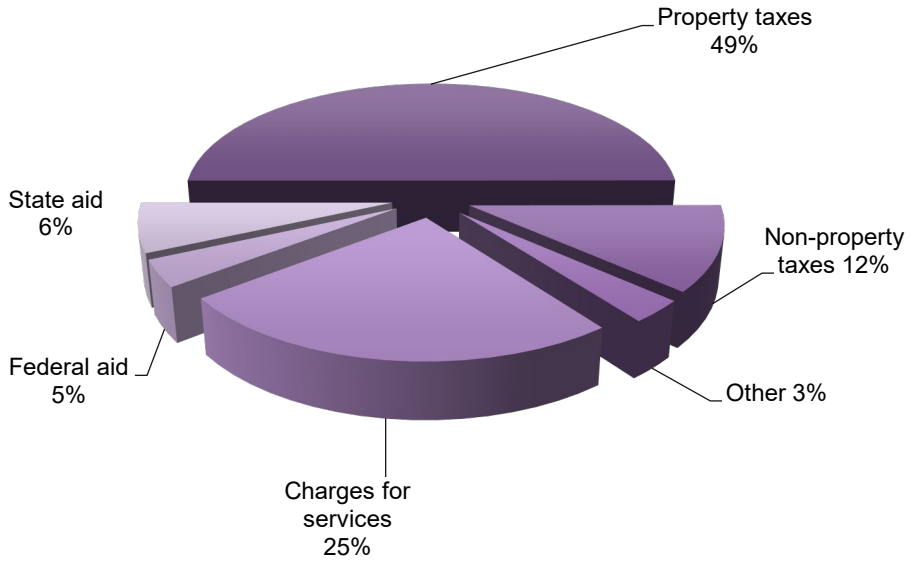
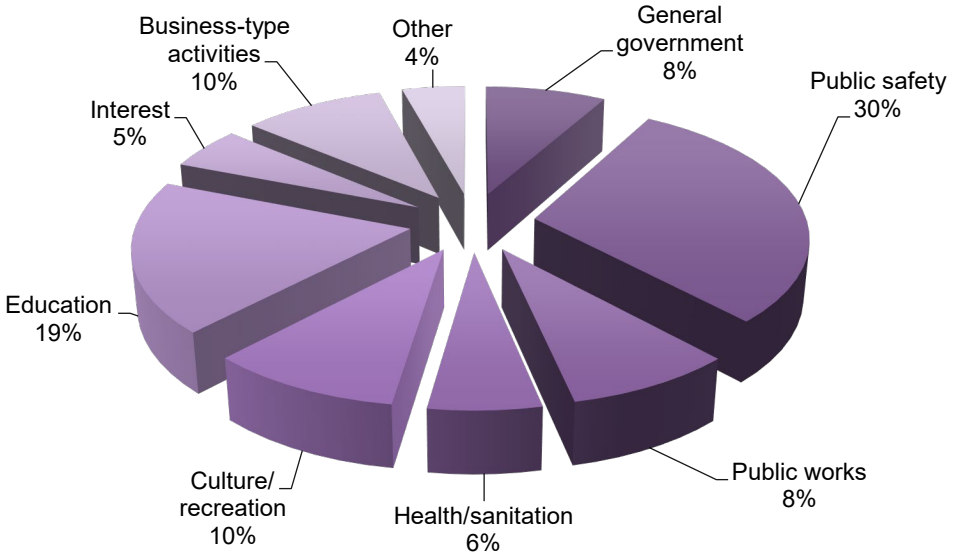


Figure A-4

Local's Expenses for Fiscal Year 2017



Even with this low growth in expenses and the sale of 1,170 acres of park land on the City's south side for a gain of $2.7 million, the City still did not cover this year's costs for governmental activities. The factors that led to the accumulated net position deficit also were the primary reasons for this year's shortfall. Table A-2 and the narrative that follows consider the operations of governmental and business-type activities separately.

Table A-2
Changes in Local's Net Position
(in millions of dollars)

	Governmental Activities		Business-Type Activities		Total		Total Percentage Change
	2016	2017	2016	2017	2016	2017	2016–2017
Revenues							
Program revenues							
Charges for services	$ 14.6	$ 15.8	$ 11.9	$ 12.7	$ 26.5	$ 28.4	7.2%
Federal grants	2.4	2.5	1.5	1.6	3.9	4.1	5.1
State grants and contributions	8.3	7.5	-	-	8.3	7.5	(9.6)
General revenues							
Property taxes	53.6	56.4	-	-	53.6	56.4	5.2
Other taxes	13.0	13.0	-	-	13.0	13.0	0.0
Federal grants and contributions	1.4	1.5	-	-	1.4	1.5	7.1
Other	2.6	2.8	0.8	0.7	3.4	3.5	2.9
Total revenues	**95.9**	**99.5**	**14.2**	**15.0**	**110.1**	**114.5**	**4.0**
Expenses							
General government	9.3	9.6	-	-	9.3	9.6	3.2
Public safety	33.8	34.9	-	-	33.8	34.9	3.3
Public works	10.5	10.1	-	-	10.5	10.1	(3.8)
Engineering services	1.4	1.3	-	-	1.4	1.3	(7.1)
Health and sanitation	6.5	6.7	-	-	6.5	6.7	3.1
Cemetery	0.5	0.7	-	-	0.5	0.7	40.0
Culture and recreation	11.9	11.5	-	-	11.9	11.5	(3.4)
Community development	3.3	3.0	-	-	3.3	3.0	(9.1)
Education (payment to school district)	21.3	21.9	-	-	21.3	21.9	2.8
Interest on long-term debt	6.3	6.1	-	-	6.3	6.1	(3.2)
Water	-	-	3.7	3.6	3.7	3.6	(2.7)
Sewer	-	-	4.8	4.9	4.8	4.9	2.1
Parking facilities	-	-	3.0	2.8	3.0	2.8	(6.7)
Total expenses	**104.8**	**105.8**	**11.5**	**11.3**	**116.3**	**117.1**	**0.7**
Excess (deficiency) before special items and transfers	(8.9)	(6.3)	2.7	3.7	(6.2)	(2.6)	(58.1)
Special item: park land sale	-	2.7	-	-	-	2.7	-
Transfers	(0.4)	0.5	0.4	(0.5)	-	-	-
Increase (decrease) in net position	**$ (9.3)**	**$ (3.1)**	**$ 3.1**	**$ 3.2**	**$ (6.2)**	**$ 0.1**	**(101.6)**

Note: Totals may not add due to rounding.

Governmental Activities

Revenues for the City's governmental activities (excluding the sale of park land) increased 3.8 percent, while total expenses increased less than 1 percent. The gain on the sale of the park land narrowed the decrease in net position for governmental activities to $3.1 million in 2017. This compares to a $9.3 million decrease in 2016.

The City's management took three major actions this year to avoid the level of deficit reported last year. Two of these actions increased revenues and a third reduced expenses:

- The City increased property tax rates an average of 5 percent. This increase, the first in 4 years, raised tax revenues $2.8 million in 2017. Based on increases in property values, tax revenues are budgeted to increase an additional $2.8 million next year.
- The City sold 3 parcels of park land for $3.5 million, for a gain (net of the $823,000 originally paid) of $2.7 million. This was a one-time special item. Although this property has been added back to the tax rolls, the tax revenues it may generate in the future are not expected to be at the same level that the City received this year by selling the land.
- The City imposed a hiring and overtime freeze (excluding the City's police, fire, and sanitation departments) in midyear that resulted in a $2.2 million savings in wages and related benefit expenses in 2017 compared to 2016. This freeze, plus cost savings of $500,000 from our continuing staff restructuring efforts, held down the increase in expenses.

Despite the rate increase, property tax revenues lagged by $844,000 compared to the originally enacted budget because delays in several major commercial and residential developments precluded adding them to this year's tax rolls. More than half of the City's other revenue sources also fell short of final budget estimates. The fire at the State Street Mall affected many retail businesses in the City. In addition, grant revenues were lower than expected because of midyear State cutbacks.

Table A-3 presents the cost of each of the City's five largest programs—police, fire, public works, education, and culture and recreation—as well as each program's *net cost* (total cost less fees generated by the activities and intergovernmental aid). The net cost shows the financial burden that was placed on the City's taxpayers by each of these functions.

- The cost of all governmental activities this year was $105.8 million.
- Some of that cost was paid by:
  - Those who directly benefited from the programs ($15.8 million)
  - Other governments and organizations that subsidized certain programs with grants and contributions ($10.0 million).
- The City paid for the $80 million "public benefit" portion of governmental activities with $69.4 million in taxes, and with other revenues such as interest and unrestricted State aid.

Table A-3
Net Cost of Local's Governmental Activities
(in millions of dollars)

	Total Cost of Services		Percentage Change	Net Cost of Services		Percentage Change
	2016	2017	2016–2017	2016	2017	2016–2017
Police department	$ 19.7	$ 20.3	3.0%	$ 19.1	$ 19.5	2.1%
Fire department	9.2	9.4	2.2	8.4	8.7	3.6
Public works	10.5	10.1	(3.8)	7.3	7.0	(4.1)
Education	21.3	21.9	2.8	21.3	21.9	2.8
Culture and recreation	11.3	11.5	1.8	5.3	5.1	(3.8)
Other	32.8	32.6	(0.6)	17.6	17.8	1.1
Total	**$ 104.8**	**$ 105.8**	**1.0**	**$ 79.0**	**$ 80.0**	**1.3**

Note: Totals may not add due to rounding.

Business-Type Activities

Revenues of the City's business-type activities *increased* 5.6 percent to $15 million and expenses *decreased* 1.7 percent to $11.3 million. (Refer to Table A-2.) Factors contributing to those results included the following:

- Water and sewer operating revenues increased 10 percent (driven by growth in hook-ups of residential customers converting from septic systems); operating expenses rose only 4 percent. The high maintenance costs caused by the harsh winter months of 2016 did not recur this year.
- Continued operating deficits at City parking facilities were $1.4 million this year versus $1.3 million in 2016. In both years, the deficit was attributable primarily to the largest of the three City-owned garages, located on State Street. This year, the garage had to be closed for two extended periods due to ruptured gas lines beneath nearby streets, which now have been repaired, and a fire at the State Street Mall.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

As the City completed the year, its governmental funds reported a *combined* fund balance of $38.1 million, slightly below last year. Included in this year's total change in fund balance, however, is a deficit of $1.3 million in the City's general fund. Furthermore, without the cash from the sale of park land, fund balances would be $3.5 million lower. The primary reasons for the general fund's deficit mirror those highlighted in the analysis of governmental activities. In addition, these other changes in fund balances should be noted:

- The City spent $11.3 million this year on the Route 7 reconstruction project, reducing the beginning fund balance in that capital projects fund by the same amount. This reduction was expected because capital fund balances at the beginning of this year included the proceeds of general obligation bonds

issued last year to finance that project. Although those and other capital expenditures reduce available fund balances, they create new assets for the City in the statement of net position (as discussed in Note 1 to the financial statements).

- In the same way, the fund balance of the community redevelopment fund increased $17.5 million this year when community redevelopment housing bonds were issued. By year-end, only $2.2 million of the debt proceeds had been used for constructing housing units, and $2.3 million was transferred to the debt service fund. Overall, fund balance grew $13.1 million.
- Each year, the state provides the City with a portion of the gasoline tax revenues it collects. This money can only be used to replace, maintain, or improve the City's roads. This year, $3 million (including $1.7 million accumulated previously) was used for 10 major repaving projects.

General Fund Budgetary Highlights

Over the course of the year, the City Council revised the City budget several times. Those budget amendments fall into three categories:

- Amendments and supplemental appropriations approved shortly after the beginning of the year to reflect the actual beginning account balances (correcting the estimated amounts in the budget adopted in October 2016).
- Changes made in the third quarter to account for the midyear hiring and overtime freeze, some of the City's staff restructuring efforts, and the sale of an additional parcel of park land.
- Increases in appropriations to prevent budget overruns.

Even with those adjustments, actual expenditures were $2.2 million below original budget amounts. The most significant positive variance ($3.2 million) resulted from a 10 percent reduction of the general administration workforce due to the staff restructuring and hiring freeze.

On the other hand, resources available for appropriation were $5.0 million below the originally budgeted amount. As noted earlier:

- Property and other tax collections were less than expected.
- Reductions in State funding also affected grant resources available for appropriation.

Those shortfalls were partially offset by a 15 percent increase in utility and cable television taxes approved by the City Council in the third quarter.

The City's general fund balance of $1.7 million differs from the general fund's *budgetary* fund balance of $1.4 million reported in the budgetary comparison schedule principally because *budgetary* fund balance excludes:

- Supplies inventories of $182,821 that are reported as expenditures for budgetary purposes when they are purchased, and
- Encumbrances of $40,292 reported as expenditures for budgetary purposes.

CAPITAL ASSET AND DEBT ADMINISTRATION ③

Capital Assets

At the end of 2017, the City had invested $321 million in a broad range of capital assets, including police and fire equipment, buildings, park facilities, roads, bridges, and water and sewer lines. (See Table A-4.) That amount represents a net increase (including additions and deductions) of $12 million (3.8 percent) over last year.

Table A-4
Local's Capital Assets
(net of depreciation, in millions of dollars)

	Governmental Activities		Business-Type Activities		Total		Total Percentage Change
	2016	2017	2016	2017	2016	2017	2016–2017
Land	$ 29.5	$ 27.1	$ 3.7	$ 3.8	$ 33.1	$ 30.9	(6.6)%
Buildings and improvements	29.6	29.6	110.1	112.9	139.7	142.5	2.0
Equipment	22.9	21.3	1.0	1.2	23.9	22.5	(5.9)
Infrastructure	77.3	90.7	27.9	30.8	105.2	121.5	15.5
Construction in progress	2.9	1.3	5.0	2.6	7.9	3.9	(50.6)
Total	**$ 162.1**	**$ 170.0**	**$ 147.6**	**$ 151.4**	**$ 309.7**	**$ 321.4**	**3.8**

Note: Totals may not add due to rounding.

The City's fiscal year 2018 capital budget calls for spending another $16 million for capital projects, principally for the completion of the Route 7 reconstruction project and to create housing units in the City's new community redevelopment housing program. The City has no plans to issue additional debt to finance these projects. Rather, we will use bond proceeds from the community redevelopment bonds issued this year and resources on hand in the City's gas tax fund. More detailed information about the City's capital assets is presented in Note 1 to the financial statements.

This year's major capital asset additions included (in millions of dollars):

- Route 7 reconstruction project, paid for with proceeds of general obligation bonds issued last year—$11.3
- Replacement of older segments of the wastewater collection system and treatment facilities, paid for with proceeds from a revenue note issued last year—$3.2
- Redevelopment housing construction, paid for with revenue bonds issued this year—$2.2
- Land acquired through the City's power of eminent domain, paid for with general fund resources—$2.0
- Water distribution mains, hydrants, and meters, paid for with water and sewer revenue bonds issued this year—$1.6.

Maintaining the City's Infrastructure Assets ④

Local City uses the *modified approach* to report its roads and highways in the government-wide statement of net position. All other infrastructure and capital assets are listed at their historical cost less any depreciation that has accumulated. Note 1 to the financial statements contains detailed information about all of the City's capital assets. While roads and highways also are listed at their historical cost, they are not depreciated. Rather, under the modified approach allowed by governmental accounting principles, the City reports annual expenses for maintaining roads and highways and the cost of preserving them at a specified condition level. Governments using this approach must disclose in the required supplementary information section certain information about the condition of their infrastructure and their efforts to maintain and preserve it. This information is summarized in Figures A-5 and A-6.

How Local City Measures Road Conditions

The condition of road pavement is measured using the XYZ pavement management system, which is based on a weighted average of six distress factors found in pavement surfaces. XYZ uses a measurement scale based on a condition index ranging from zero to 100. The index is used to classify road conditions as follows:

- Good or better condition (70–100)
- Fair condition (50–69)
- Substandard condition (less than 50).

City policy is to maintain at least 85 percent of its street system at a good or better condition level. No more than 10 percent should be in a substandard condition. Condition assessments are determined every year.

The percentage of each of the three major types of roadways in good or better condition was higher in 2017 than in 2015. (See Figure A-5.) In 2017, over 85 percent of arterial roads were in this highest category, as were 87 percent of secondary roads and 93 percent of main arteries. Overall, 88 percent of the City's roads were in good or better condition, above the City's minimum standard of 85 percent.

In two of the five years between 2013 and 2017, the City's maintenance and preservation expenses for roads were below the amount estimated by the City's road management system as necessary to keep the system above the minimum standard. (See Figure A-6.) However, overall actual spending during the period *exceeded* necessary spending by $423,000. The primary reason for underspending in 2014 and 2015 was particularly inclement weather that limited the amount of road work that could be accomplished.

Figure A-5

Local City Roads in Good or Better Condition

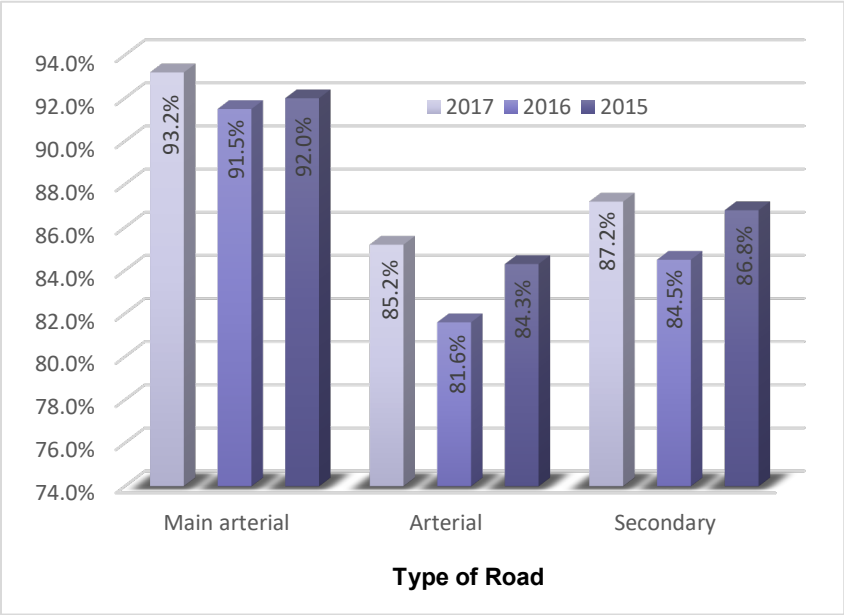
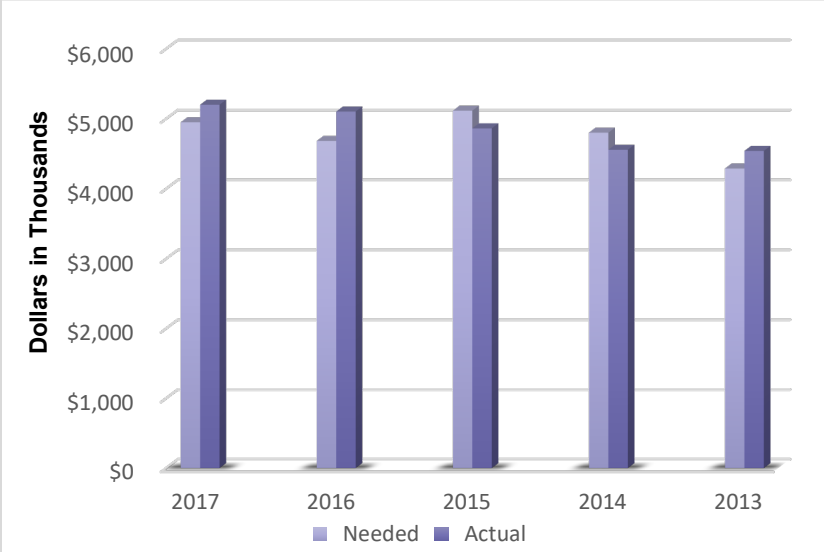


Figure A-6

Comparison of Local City's Actual and Needed Preservation/Maintenance Spending



Long-Term Debt

At year-end, the City had $158 million in bonds and notes outstanding—an increase of 12 percent over last year—as shown in Table A-5. More detailed information about the City's long-term liabilities is presented in Note 12 to the financial statements. New debt resulted mainly from issuing revenue bonds for two new projects—$19.8 million of community redevelopment housing bonds and $3.6 million of water system improvement bonds.

Limitations on debt

The State limits the amount of general obligation debt the City can issue to 3 percent of the assessed value of all taxable property within the City's corporate limits. Our outstanding debt is significantly below that limit, which currently is $134 million.

Bond ratings

Since 2005, the City's general obligation bonds have been rated Q-2 (the fourth highest rating possible). The City's other debt—principally, revenue bonds and notes—carries the fifth highest rating, Q-3+.

Table A-5
Local's Outstanding Debt
(in millions of dollars)

	Governmental Activities		Business-Type Activities		Total		Total Percentage Change
	2016	2017	2016	2017	2016	2017	2016–2017
General obligation bonds (backed by the City)	$ 32.7	$ 31.3	-	-	$ 32.7	$ 31.3	(4.3)%
Revenue bonds and notes (backed by specific fee revenues)	30.7	48.0	$ 77.3	$ 78.3	108.0	126.3	16.9
Total	**$ 63.4**	**$ 79.3**	**$ 77.3**	**$ 78.3**	**$ 140.7**	**$ 157.6**	**12.0**

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES ⑤

- Nonagricultural employment increased 6.2 percent overall during 2013–2017.
- Unemployment now stands at 3.4 percent versus 3.6 percent a year ago. This compares favorably with the state's rate of 4.4 percent and the national rate of 4.1 percent.
- Inflation in the metropolitan area continues to be somewhat higher than the national consumer price index due in part to residential housing market and energy price increases.
  - City inflation was 2.0 percent for fiscal year 2017.
  - The average U.S. city rate was 2.1 percent.

Those indicators were taken into account when adopting the general fund budget for 2018. Amounts available for appropriation in the general fund budget are $96.4 million, an increase of 4 percent over

the final 2017 budget of $92.7 million. Property taxes (benefiting from the 2017 rate increases and growth in assessed valuations), public service taxes (with the 15 percent rate increase discussed above), and grant revenue (boosted by increased State funding in several of our current programs) are expected to lead this increase. The City will use those increases in revenues to finance programs we currently offer and the expected impact of inflation on program costs.

Budgeted expenditures are expected to rise nearly 4 percent to $95.9 million. The largest increments are increased wage and cost-of-living adjustments of $800,000 based on agreements reached with the police, fire, and sanitation department unions in 2015. The City has added no major new programs or initiatives to the 2018 budget.

If those estimates are realized, the City's budgetary general fund balance is expected to increase modestly by the close of 2018. More important, however, it will have been accomplished without repeating the selling of capital assets or restructuring of the workforce to alleviate cash flow pressures that occurred this year. In addition, the City recently purchased commercial insurance for all property and casualty claims incurred after December 31, 2017.

As for the City's business-type activities, we expect that the 2018 results also will improve based on these recent rate decisions:

- The Public Service Commission approved a 2 percent rate increase for all water customers effective January 1. Sewer charges will not change.
- The City Council authorized a 15 percent increase in parking fees at the City-owned garages and on-street meters.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Local City Controller's Office, 38 Tompkins Place, Local, ST 00000.

APPENDIX B

FINANCIAL STATEMENTS FOR A STATE GOVERNMENT

Page Number

Figure B-1. Government-Wide Statement of Net Position, State Government B-3

Figure B-2. Government-Wide Statement of Activities, State Government (Two-Page Presentation) B-4

Figure B-3. Governmental Funds Balance Sheet, State Government B-6

Figure B-4. Reconciliation of Total Governmental Fund Balances to Total Net Position of the Governmental Activities, State Government B-7

Figure B-5. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, State Government B-8

Figure B-6. Reconciliation of Net Changes in Governmental Fund Balances to Governmental Activities Change in Net Position, State Government B-9

Figure B-7. Proprietary Funds Statement of Net Position, State Government B-10

Figure B-8. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, State Government B-11

Figure B-9. Proprietary Funds Statement of Cash Flows, State Government B-12

Figure B-10. Statement of Fiduciary Net Position, State Government B-13

Figure B-11. Statement of Changes in Fiduciary Net Position, State Government B-14

Figure B-1. Government-Wide Statement of Net Position, State Government

State of Seabury
Statement of Net Position
As of June 30, 2017
(dollars in thousands)

	Primary Government			
	Governmental Activities	Business-Type Activities	Total	Component Units
ASSETS				
Current assets:	$ 1,891,267	$ 132,666	$ 2,023,933	$ 647,190
Cash and cash equivalents	1,808,587	144,836	1,953,423	—
Taxes, interest, and penalties receivable	—	—	—	8,126
Due from state	1,740,116	18,341	1,758,457	393,665
Other receivables	205,501	1,953,980	2,159,481	475,224
Investments	54,662	32,462	87,124	15,477
Inventories	508,319	60,169	568,488	337,525
Other current assets	6,208,452	2,342,454	8,550,906	1,877,207
Total current assets				
Noncurrent assets:				
Taxes, interest, and penalties receivable	64,576	—	64,576	—
Other receivables	186,633	—	186,633	1,079,363
Mortgages and loans receivable	—	—	—	2,074,012
Investments	122,334	869,433	991,767	1,669,091
Investments in joint venture	32,356	—	32,356	—
Other noncurrent assets	95,670	—	95,670	88,694
Capital assets:				
Land	1,080,204	98	1,080,302	141,516
Infrastructure	8,218,393	—	8,218,393	—
Property, plant, and equipment	3,853,332	21,193	3,874,525	2,617,710
Less accumulated depreciation	(3,313,645)	(15,715)	(3,329,360)	(650,588)
Total capital assets, net of depreciation	9,838,283	5,576	9,843,859	2,108,638
Total noncurrent assets	10,339,852	875,009	11,214,861	7,019,798
Total assets	16,548,304	3,217,463	19,765,767	8,897,005
DEFERRED OUTFLOWS OF RESOURCES	603,203	—	603,203	332,132
LIABILITIES				
Current liabilities:				
Accounts payable and other current liabilities	2,390,961	248,884	2,639,845	163,075
Income tax refunds payable	393,722	—	393,722	—
Internal balances	156	(156)	—	—
Due to component units	8,126	—	8,126	—
Bonds, notes, and leases payable	517,661	—	517,661	525,842
Claims, judgments, and compensated absence	176,143	—	176,143	—
Accrued interest	426,250	—	426,250	121,352
Payments received in advance	80,202	1,370	81,572	50,911
Total current liabilities	3,993,221	250,098	4,243,319	861,180
Long-term liabilities:				
Lottery prize awards payable	—	900,486	900,486	—
Bonds, notes, and leases payable	3,152,844	—	3,152,844	3,892,142
Claims, judgments, and compensated absence	1,158,391	5,463	1,163,854	1,017,242
Postemployment benefits—net liabilities	2,450,987	—	2,450,987	805,508
Total long-term liabilities	6,762,222	905,949	7,668,171	5,714,892
Total liabilities	10,755,443	1,156,047	11,911,490	6,576,072
DEFERRED INFLOWS OF RESOURCES	556,347	—	556,347	222,333
NET POSITION				
Net investment in capital assets	6,214,634	5,576	6,220,210	2,221,302
Restricted for:				
Transportation programs	553,174	—	553,174	—
Elementary and secondary education	127,848	—	127,848	—
Conservation and recreation	413,116	—	413,116	—
Unemployment compensation	—	2,049,712	2,049,712	—
Other purposes	596,563	—	596,563	168,385
Unrestricted	(2,065,618)	6,128	(2,059,490)	41,045
Total net position	$ 5,839,717	$ 2,061,416	$ 7,901,133	$ 2,430,732

Figure B-2. Government-Wide Statement of Activities, State Government (Two-Page Presentation)

State of Seabury
Statement of Activities
for the Year Ended June 30, 2017
(dollars in thousands)

Functions/Programs	Expenses	Program Revenues: Charges for Services	Program Revenues: Operating Grants and Contributions	Program Revenues: Capital Grants and Contributions	Net (Expense) Revenue
Primary government:					
Government activities:					
General government	$ 1,159,715	$ 104,277	$ 377,434	$ —	$ (678,004)
Education—elementary and secondary	9,790,623	13,509	712,171	—	(9,064,943)
Education—state aid to the universities	567,568		—	—	(567,538)
Health and welfare	8,636,008	102,242	5,872,725	—	(2,661,041)
Public safety and connections	1,611,415	34,753	14,770	85,000	(1,476,892)
Conservation, recreation, and agriculture	519,223	109,142	154,105	—	(256,976)
Labor, commerce, and regulatory	568,428	127,705	396,081	—	44,642
Mental health	1,519,549	42,047	333,541	123,321	(1,020,640)
Transportation	901,335	165,133	42,351	481,128	(212,723)
Intergovernmental—grants and revenue sharing	1,941,999	—	—	—	(1,941,999)
Depreciation expense ①	217,275	—	—	—	(217,275)
Interest expense	214,623	—	—	—	(214,623)
Total governmental activities	27,647,731	698,808	7,903,178	689,449	(18,356,296)
Business-type activities:					
Lottery	987,014	1,456,251	—	—	469,237
Unemployment insurance	1,174,657	1,250,997	165,964	—	242,304
Liquor control	370,430	482,306	160	—	112,036
Other	7,302	5,896	—	—	(1,406)
Total business-type activities	2,539,403	3,195,450	166,124	—	822,171
Total primary government	$ 30,187,134	$ 3,894,258	$ 8,069,302	$ 689,449	$ (17,534,125)
Component units:					
State universities	$ 1,451,857	$ 710,148	$ 274,528	$ 48,010	$ (419,171)
Higher education financial assistance programs	174,007	32,258	68,642	—	(73,107)
Other component units	347,904	52,304	9,543	54,469	(231,588)
Total component units	$ 1,973,768	$ 794,710	$ 352,713	$ 102,749	$ (723,866)

②

(The statement of activities continues on the following page.)

Figure B-2 Notes

① This amount does not include depreciation that is reported in the direct expenses of the various programs.

② In this format, net (expense) revenue is shown in a single column, rather than the three-column presentation in the continuous format of Figure 42.

Figure B-2. Government-Wide Statement of Activities, State Government (continued)

State of Seabury
Statement of Activities
for the Year Ended June 30, 2017
(dollars in thousands)

	Net (Expense) Revenue and Changes in Net Position			
	Primary Government			
	Governmental Activities	Business-Type Activities	Total	Component Units
Changes in net position:				
Net (expense) revenue	$ (18,356,296)	$ 822,171	$(17,534,125)	$ (723,866)
General revenues:				
Taxes:				
Personal and corporate income	7,068,167	—	7,068,167	—
Sales and use	2,047,291	—	2,047,291	—
Others	825,577	—	825,577	—
Redistricted for educational purposes:				
Sales and use	5,463,610	—	5,463,610	—
Personal and corporate income	918,182	—	918,182	—
Others	475,566	—	475,566	—
Redistricted for transportation purposes:				
Motor fuel taxes	1,334,349	—	1,334,349	—
Others	58,187	—	58,187	—
Total taxes	18,190,929	—	18,190,929	—
Unrestricted investment earnings	172,119	195,482	367,601	393,407
State aid	—	—	—	567,538
Transfers—internal activities	650,732	(650,732)	—	—
Total general revenues and transfers	19,013,780	(455,250)	18,558,530	960,945
Changes in net position	657,484	366,921	1,024,405	237,079
Net position—beginning	5,182,233	1,694,495	6,876,728	2,193,653
Net position—ending	$ 5,839,717	$ 2,061,416	$ 7,901,133	$ 2,430,732

Figure B-3. Governmental Funds Balance Sheet, State Government

State of Seabury
Balance Sheet
Governmental Funds
As of June 30, 2017
(dollars in thousands)

	General Fund	Transportation Fund	Local Aid Fund	School Aid Fund	Other Funds	Total
ASSETS						
Cash and cash equivalents	$ 37,032	$ 573,238	$ 488,738	$ 46	$ 605,565	$ 1,704,619
Taxes, interest, and penalties receivable	1,187,449	69,206	—	613,612	2,896	1,873,163
Receivable from:						
Other funds	608,100	98,587	684,674	—	161,006	1,552,367
Component units	3,254	369	—	—	1,132	4,755
Federal agencies	1,120,253	184,916	—	4,688	1,969	1,311,826
Local governments	462,846	81,455	—	45,270	25,354	614,925
Investments	—	—	—	—	327,836	327,836
Inventories	28,586	7,487	—	—	30	36,103
Other assets	481,819	19,051	10,000	9	13,851	524,730
Total assets	3,929,339	1,034,309	1,183,412	663,625	1,139,639	7,950,324
LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND FUND BALANCES						
Liabilities:						
Accounts payable and other liabilities	1,671,975	367,718	—	71,564	159,008	2,270,265
Income tax refunds payable	393,722	—	—	—	—	393,722
Payable to:						
Other funds	698,989	103,484	29,850	464,213	264,038	1,560,574
Pension trust funds	28,787	—	—	—	—	28,787
Component units	3,382	—	—	—	9,499	12,881
Matured bonds and notes payable	—	—	—	—	321,561	321,561
Payments received in advance	61,545	9,933	—	7,598	702	79,778
Total liabilities	2,858,400	481,135	29,850	543,375	754,808	4,667,568
Deferred inflows of resources: Unavailable revenue	249,812	—	—	—	—	249,812
Fund balances:						
Nonspendable	131,500	93,378	10,000	1,095	4,396	240,369
Restricted	490,600	296,745	—	—	156,151	943,496
Assigned	69,319	163,051	1,143,562	119,155	224,284	719,371
Unassigned	129,708	—	—	—	—	129,708
Total fund balances	821,127	553,174	1,153,562	120,250	384,831	3,032,944
Total liabilities and fund balances	$ 3,929,339	$ 1,034,309	$ 1,183,412	$ 663,625	$ 1,139,639	$ 7,950,324

Figure B-4. Reconciliation of Total Government Fund Balances to Total Net Position of the Governmental Activities, State Government

State of Seabury
Reconciliation of the Governmental Funds Balance Sheet
to the Government-Wide Statement of Net Position
As of June 30, 2017
(dollars in thousands)

Total fund balances—governmental funds		$ 3,032,944
Amounts reported for governmental activities in the statement of net position are different because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. These assets consist of:		
Land	1,080,204	
Infrastructure assets	8,218,393	
Other capital assets	3,853,332	
Accumulated depreciation	(3,313,645)	
Total capital assets		9,838,283
The state has an equity interest in a joint venture. This investment is not a current financial resource and therefore is not reported in the funds.		32,356
Some of the state's revenues will be collected after year-end but are not available soon enough to pay for the current period's expenditures and therefore are deferred in the funds.		249,812
Internal service funds are used by management to charge the costs of certain activities to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the statement of net position.		210,863
Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:		
Bonds and notes payable	(3,194,290)	
Accrued interest on bonds	(426,250)	
Capital leases	(220,014)	
Compensated absences	(451,700)	
Claims and judgments	(781,300)	
Pensions and retiree health insurance	(2,450,987)	
Total long-term liabilities		(7,524,541)
Net position of governmental activities		$ 5,839,717

Figure B-5. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, State Government

State of Seabury
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
for the Year Ended June 30, 2017
(dollars in thousands)

	General Fund	Transportation Fund	Local Aid Fund	School Aid Fund	Other Funds	Total
REVENUES						
Taxes:						
Personal and corporate income	$ 7,049,432	$ —	$ —	$ 918,182	$ —	$ 7,967,614
Sales and use	2,041,046	—	—	5,451,119	—	7,492,165
Tobacco and liquor	312,559		—	394,064	—	706,623
Motor fuels	36,776	1,334,349	—	—	—	1,371,125
Others	355,039	58,187	—	81,502	121,203	615,931
From federal agencies:						
Health and human services	4,648,284	—	—	—	—	4,648,284
Agriculture	1,169,833	—	—	—	—	1,169,833
Education	521,235	—	—	69,691	—	590,926
Transportation	8,787	509,941	—	—	—	518,728
Labor	115,492	106,373	—	—	—	221,865
Others	191,234	—	—	—	4,118	195,352
From local governments	134,769	90,248	—	23	—	225,040
Charges for services	119,229	1,186	—	—	—	120,415
Licenses and permits	189,979	73,700	—	—	89,588	353,267
Special Medicaid reimbursements	598,654	—	—	—	—	598,654
Miscellaneous	512,410	72,386	59,205	5,176	172,013	821,190
Total revenues	18,004,758	2,246,370	59,205	6,919,757	386,922	27,617,012
EXPENDITURES						
Current:						
General government	1,060,940	—	—	—	2,039	1,062,979
Education	1,340,042	—	—	8,312,033	134,838	9,786,913
State aid to universities	567,538	—	—	—	—	567,538
Health and welfare	8,617,712	—	—	—	1,382	8,619,094
Public safety and corrections	1,580,342	—	—	—	3,276	1,583,618
Conservation, recreation, and agriculture	247,168	—	—	—	264,291	511,459
Labor, commerce, and regulatory	560,807	—	—	—	33	560,840
Mental health	1,501,080	—	—	—	—	1,501,080
Transportation	—	877,986	—	—	—	877,986
Intergovernmental—grants and revenue sharing	1,281,089	660,910	—	—	—	1,941,999
Debt service:						
Bond principal retirement	—	—	—	—	145,587	145,587
Bond interest and fiscal charges	—	—	—	—	164,394	164,394
Capital lease principal payments	19,202	200	—	—	—	19,402
Interest on capital leases	24,789	11	—	—	—	24,800
Capital outlay	129,958	553,065	—	—	116,495	799,518
Total expenditures	16,930,667	2,092,172	—	8,312,033	832,335	28,167,207
Excess (deficiency) of revenues over expenditures	1,074,091	154,198	59,205	(1,392,276)	(445,413)	(550,195)
OTHER FINANCING SOURCES (USES)						
Bonds and bond anticipation notes issued	—	—	—	—	109,900	109,900
Refunding bonds issued	—	—	—	—	216,600	216,600
Premiums on bonds issued	—	—	—	—	11,014	11,014
Payment to refunding bond escrow account	—	—	—	—	(206,718)	(206,718)
Capital leases	71,746	63	—	—	—	71,809
Transfers in	327,061	651,359	91,334	1,169,288	938,418	3,177,460
Transfers out	(1,409,292)	(849,100)	—	(19,616)	(248,027)	(2,526,035)
Total other financial sources and uses	(1,010,485)	(197,678)	91,334	1,149,672	821,187	854,030
Net changes in fund balances	63,606	(43,480)	150,539	(242,604)	375,774	303,835
Fund balances—beginning	757,521	596,654	1,003,023	362,854	9,057	2,729,109
Fund balances—ending	$ 821,127	$ 553,174	$ 1,153,562	$ 120,250	$ 384,831	$ 3,032,944

Figure B-6. Reconciliation of Net Changes in Governmental Fund Balances to Governmental Activities Change in Net Position, State Government

State of Seabury
Reconciliation of the Changes in Fund Balances of Governmental Funds
to the Statement of Activities
for the Year Ended June 30, 2017
(dollars in thousands)

Net changes in fund balances—total governmental funds		$ 303,835
Amounts reported for governmental activities in the statement of activities are different because:		
Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:		
Capital outlay	$ 799,518	
Depreciation expense	373,501	
Excess of capital outlay over depreciation expense		426,017
Bond proceeds provide current financial resources to governmental funds; however, issuing debt increases long-term liabilities in the statement of net position. In the current period, proceeds were received from:		
Bonds and bond anticipation notes issued, including a premium of $2,828	(112,728)	
Refunding bonds issued, including a premium of $8,186	(224,786)	
Total bond proceeds		(337,514)
Some capital additions were financed through capital leases. In governmental funds, a capital lease arrangement is considered a source of financing, but in the statement of net position, the lease obligation is reported as a liability.		(71,809)
Repayment of long-term debt is reported as an expenditure in governmental funds, but the repayment reduces long-term liabilities in the statement of net position. In the current year, these amounts consist of:		
Bond principal retirement	145,587	
Capital lease payments	19,402	
Payments to the bond refunding agent	206,718	
Total long-term debt repayment		371,707
Internal service funds are used by management to charge the costs of certain activities to individual funds. The net revenue of the internal service funds is reported with the governmental activities.		9,108
Because some revenues will not be collected for several months after the state's fiscal year ends, they are not considered "available" revenues and are deferred in the governmental funds. Deferred revenues increased by this amount this year.		37,471
Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:		
Net increases in accrued interest	(14,500)	
Interest accreted on capital appreciation debt	(10,500)	
Increase in compensated absences	(3,126)	
Increase in claims and judgments	(53,205)	
Total additional expenditures		(81,331)
Change in net position of governmental activities		$ 657,484

Figure B-7. Proprietary Funds Statement of Net Position, State Government

State of Seabury
Statement of Net Position
Proprietary Funds
As of June 30, 2017
(dollars in thousands)

	Enterprise Funds				
	Lottery Fund	Unemployment Compensation Fund	Other Enterprise Funds	Total	Internal Service Funds
ASSETS					
Current assets:					
Cash and cash equivalents	$ 27,503	$ 87,653	$ 17,510	$ 132,666	$ 186,648
Assessments, interest, and penalties receivable	—	144,836	—	144,836	—
Investments	111,102	1,842,878	—	1,953,980	—
Due from other funds	—	2,716	—	2,716	82,796
Due from federal agencies	—	2,601	—	2,601	—
Due from local units	—	15,740	—	15,740	—
Inventories	3,496	—	28,966	32,462	18,560
Other current assets	43,274	16,477	418	60,169	13,434
Total current assets	185,375	2,112,901	46,894	2,345,170	301,438
Noncurrent assets:					
Investments	869,433	—	—	869,433	—
Capital assets:					
Land	—	—	98	98	—
Buildings and equipment	10,685	—	10,508	21,193	176,090
Less accumulated depreciation	(8,633)	—	(7,082)	(15,715)	(63,874)
Other noncurrent assets	—	—	—	—	65,821
Total noncurrent assets	871,485	—	3,524	875,009	178,037
Total assets	1,056,860	2,112,901	50,418	3,220,179	479,475
LIABILITIES					
Current liabilities:					
Accounts payable and other liabilities	154,562	59,631	34,691	248,884	91,909
Due to other funds	123	2,188	249	2,560	74,745
Unearned revenue	—	1,370	—	1,370	424
Total current liabilities	154,685	63,189	34,940	252,814	167,078
Noncurrent liabilities:					
Prize awards payable	900,486	—	—	900,486	—
Other noncurrent liabilities	1,689	—	3,774	5,463	101,534
Total noncurrent liabilities	902,175	—	3,774	905,949	101,534
Total liabilities	1,056,860	63,189	38,714	1,158,763	268,612
NET POSITION					
Net investment in capital assets	2,052	—	3,524	5,576	112,216
Restricted for unemployment compensation	—	2,049,712	—	2,049,712	—
Unrestricted (deficit)	(2,052)	—	8,180	6,128	98,647
Total net position	$ —	$ 2,049,712	$ 11,704	$2,061,416	$ 210,863

Figure B-8. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, State Government

State of Seabury
Statement of Revenues, Expenses, and Changes in Fund Net Position
Proprietary Funds
for the Year Ended June 30, 2017
(dollars in thousands)

	Enterprise Funds				
	Lottery Fund	Unemployment Compensation Fund	Other Enterprise Funds	Total	Internal Service Funds
OPERATING REVENUES					
Sales and charges for services	$ 1,456,251	$ —	$ 480,020	$ 1,936,271	$ 774,926
Assessments	—	1,231,245	—	1,231,245	—
From federal agencies	—	165,964	—	165,964	—
From local agencies	—	1,301	—	1,301	—
Miscellaneous	—	18,451	—	18,451	—
Total operating revenues	1,456,251	1,416,961	480,020	3,353,232	774,926
OPERATING EXPENSES					
Salaries, wages, and administrative expenses	159,716	—	35,652	195,368	120,433
Depreciation	851	—	1,171	2,022	10,895
Unemployment compensation	—	1,174,657	—	1,174,657	—
Purchases for resale	—	—	34,106	34,106	52,963
Lottery prize awards	826,447	—	—	826,447	—
Premiums and claims	—	—	—	—	547,129
Other operating expenses	—	—	—	—	33,446
Total operating expenses	987,014	1,174,657	70,929	2,232,600	764,866
Operating income	469,237	242,304	409,091	1,120,632	10,060
NONOPERATING REVENUES (EXPENSES)					
Alcoholic beverage taxes	—	—	8,182	8,182	—
Interest and dividends	4,625	115,173	—	119,798	—
Net increase in fair value of investments	75,684	—	—	75,684	—
Other nonoperating revenue	—	—	160	160	170
Interest expense	—	—	(803)	(803)	(429)
Total nonoperating revenues (expenses)	80,309	115,173	7,539	203,021	(259)
Income before transfers	549,546	357,477	110,630	1,017,653	9,801
Transfer to other funds	(549,546)	(18,258)	(98,402)	(666,206)	(693)
Transfer from other funds	—	15,744	—	15,744	—
Change in net position	—	354,693	12,228	366,921	9,108
Total net position—beginning	—	1,695,019	(524)	1,694,495	201,755
Total net position—ending	$ —	$ 2,049,712	$ 11,704	$ 2,061,416	$ 210,863

Figure B-9. Proprietary Funds Statement of Cash Flows, State Government

State of Seabury
Statement of Cash Flows
Proprietary Funds
for the Year Ended June 30, 2017
(dollars in thousands)

	Enterprise Funds				
	Lottery Fund	Unemployment Compensation Fund	Other Enterprise Fund	Total	Internal Service Fund
CASH FLOWS FROM OPERATING ACTIVITIES					
Cash received from assessments	$ —	$ 1,239,640	$ —	$ 1,239,640	$ —
Cash received from federal and local agencies	—	164,896		164,896	—
Cash received from customers	1,456,251	—	480,020	1,936,271	—
Cash received from other funds	—	—	—	—	737,765
Payments to employees	(122,658)	—	(31,791)	(154,449)	(112,989)
Payments to suppliers	(28,199)	—	(348,335)	(376,534)	(96,909)
Payments to prize winners	(781,102)	—	—	(781,102)	—
Claims paid	—	(1,177,535)	—	(1,177,535)	(547,129)
Other receipts (payments)	—	18,451	(3,912)	14,539	4,208
Net cash provided (used) by operating activities	524,292	245,452	95,982	865,726	(15,054)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Interest paid	—	—	(803)	(803)	(429)
Interfund loan or loan repayments received	—	1,991	10,765	12,756	47,541
Interfund loans made or repaid	—	(4,001)	(10,831)	(14,832)	(38,261)
Alcoholic beverage taxes	—	—	8,182	8,182	—
Net transfers to other funds	(549,546)	(2,784)	(98,402)	(650,732)	(693)
Net cash provided (used) by noncapital financing activities	(549,546)	(4,794)	(91,089)	(645,429)	8,158
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Acquisition and construction of capital assets	(665)	—	(136)	(801)	(48,683)
Capital lease payments (and interest)	—	—	—	—	(169)
Proceeds from sale of property, plant, and equipment	—	—	1,935	1,935	1,816
Net cash provided (used) by capital and related financing activities	(665)	—	1,799	1,134	(47,036)
CASH FLOWS FROM INVESTING ACTIVITIES					
Purchase of investments	(64,007)	(363,719)	—	(427,726)	—
Proceeds from sale and maturities of investments	63,401	—	—	63,401	—
Interest and dividends on investments	4,625	115,173	—	119,798	—
Net cash provided (used) by investing activities	4,019	(248,546)	—	(244,527)	—
Net increase (decrease) in cash	(21,900)	(7,888)	6,692	(23,096)	(53,932)
Cash and cash equivalents—beginning	49,403	95,541	10,818	155,762	240,580
Cash and cash equivalents—ending	$ 27,503	$ 87,653	$ 17,510	$ 132,666	$ 186,648
Reconciliation of operating income to net cash provided (used) by operating activities					
Operating income	$ 469,237	$ 242,304	$ 103,091	$ 814,632	$ 10,060
Adjustments to reconcile operating income to net cash provided (used) by operating activities:					
Depreciation	851	—	1,171	2,022	10,895
Net changes in assets and liabilities:					
Inventories	(718)	—	(1,984)	(2,702)	—
Other assets	681	6,026	180	6,887	(45,843)
Current liabilities	8,859	(2,878)	(6,476)	(495)	20,838
Prize awards payable	45,345	—	—	45,345	—
Other liabilities	37	—	—	37	(11,004)
Net cash provided (used) by operating activities	$ 524,292	$ 245,452	$ 95,982	$ 865,726	$ (15,054)

Noncash investing activities: The net increase in the fair value of investments in the Lottery Fund was $75,684 for the year.

Figure B-10. Statement of Fiduciary Net Position, State Government

State of Seabury
Statement of Fiduciary Net Position
Fiduciary Funds
As of June 30, 2017
(dollars in thousands)

	Pension Trust Fund	Private-Purpose Trust Funds	Investment Trust Funds	Agency Funds
ASSETS				
Cash and cash equivalents	$ 155,564	$ 104,747	$ —	$ 87,788
Receivables				
Employee	2,123	—	—	—
Employer	83,004	—	—	—
Interest and dividends	175,402	—	12,166	—
From other funds	28,787	—	—	—
From federal agencies	—	—	—	858
From local units	—	—	—	17
From sale of investments	30,879	—	—	—
Total receivables	320,195	—	12,166	875
Investments at fair value:				
Short-term investments	2,268,960	61,591	241,645	1,811,384
Bonds, notes, mortgages, and preferred stock	14,115,391	187,650	804,576	—
Common stock	20,742,440	520,196	497,848	—
Real estate	3,408,145	—	—	—
International investments	1,723,951	—	342,845	—
Mutual funds	72,315	—	178,046	—
Pooled investment funds	23,128	—	—	—
Total investments	42,354,330	769,437	2,064,960	1,811,384
Securities lending collateral	1,746,544	—	—	—
Other assets	13,519	81,157	181	394,910
Total assets	44,590,152	955,341	2,077,307	2,294,957
LIABILITIES				
Accounts payable and other liabilities	130,846	61,447	1,361	2,294,957
Obligations under securities lending	1,746,544	—	—	—
Other long-term liabilities	1,617	7,870	—	—
Total liabilities	1,879,007	69,317	1,361	2,294,957
NET POSITION				
Held in trust for:				
Employees' pension benefits	29,897,802	—	—	—
Employees' postemployment healthcare benefits	12,813,343	—	—	—
Individuals, organizations, and other governments	—	886,024	2,075,946	—
Total net position	$ 42,711,145	$ 886,024	$ 2,075,946	$ —

Figure B-11. Statement of Changes in Fiduciary Net Position, State Government

State of Seabury
Statement of Changes in Fiduciary Net Position
Fiduciary Funds
for the Year Ended June 30, 2017
(dollars in thousands)

	Pension Trust Fund	Private-Purpose Trust Funds	Investment Trust Funds
ADDITIONS			
Contributions:			
Members	$ 297,846	$ —	$ —
Employers	1,259,384	—	—
Other plans	148,792	—	—
Gifts, bequests, and endowments	—	72,132	—
Total contributions	1,706,022	72,132	—
Investment income:			
Net increase in fair value of investments	1,852,408	98,765	84,663
Interest, dividends, and other	1,416,448	90,378	73,465
Securities lending income	76,075	—	—
Total investment income	3,344,931	189,143	158,128
Less investment expense:			
Investment activity expense	32,281	—	50,236
Securities lending expense	73,642	—	—
Net investment income	3,239,008	189,143	107,892
Capital share and individual account transactions			
Shares sold	—	—	2,817,210
Reinvested distributions	—	—	96,525
Shares redeemed	—	—	(2,811,843)
Net capital share and individual account transactions	—	—	101,892
Miscellaneous	1,130	—	—
Total additions	4,946,160	261,275	209,784
DEDUCTIONS			
Benefits paid to participants or beneficiaries	1,963,047	—	—
Medical, dental, and life insurance for retirees	536,027	—	—
Refunds and transfers to other systems	170,514	—	—
Administrative expense	19,920	—	—
Payments in accordance with trust agreements	—	211,222	—
Distributions to shareholders	—	—	95,525
Total deductions	2,689,508	211,222	95,525
Change in net position held in trust for:			
Employees' pension benefits	2,280,555	—	—
Employees' postemployment healthcare benefits	(23,903)	—	—
Individuals, organizations, and other governments	—	50,053	113,259
Net position—beginning	40,454,493	835,971	1,962,687
Net position—ending	$ 42,711,145	$ 886,024	$ 2,075,946

APPENDIX C

FINANCIAL STATEMENTS FOR A SCHOOL DISTRICT

Page Number

Figure C-1. District-Wide Statement of Net Position, School District C-3

Figure C-2. District-Wide Statement of Activities, School District C-4

Figure C-3. Governmental Funds Balance Sheet, School District C-5

Figure C-4. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, School District C-6

Figure C-5. Reconciliation of Net Changes in Governmental Fund Balances to Governmental Activities Change in Net Position, School District C-7

Figure C-6. Proprietary Funds Statement of Net Position, School District C-8

Figure C-7. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, School District C-9

Figure C-8. Proprietary Funds Statement of Cash Flows, School District C-10

Figure C-9. Statement of Fiduciary Net Position, School District C-11

Figure C-10. Statement of Changes in Fiduciary Net Position, School District C-12

Figure C-1. District-Wide Statement of Net Position, School District

Luna Independent School District
Statement of Net Position
As of June 30, 2017

	Governmental Activities	Business-Type Activities	Total
ASSETS			
Cash and cash equivalents	$ 42,871,042	$ 7,664,712	$ 50,535,754
Investments	61,962,339	163,531	62,125,870
Property taxes receivable (net)	12,182,730	—	12,182,730
Due from other governments	19,968,336	2,002,921	21,971,257
Other receivables	3,688,518	4,081	3,692,599
Internal balances	615,597	(615,597)	—
Inventories	1,537,230	1,949,526	3,486,756
Nondepreciated capital assets	32,272,411	—	32,272,411
Depreciated capital assets	381,428,545	11,549,456	392,978,001
Less: Accumulated depreciation	(98,176,725)	(9,016,026)	(107,192,751)
Total assets	458,350,023	13,702,604	472,052,627
DEFERRED OUTFLOWS OF RESOURCES			
Increases in the net pension liability	2,395,287	126,068	2,521,355
Increases in the total liability for retiree health insurance	5,988,218	315,169	6,303,387
Accumulated decrease in fair value of hedging derivatives	1,754,896	—	1,754,896
Total deferred outflows of resources	10,138,401	441,237	10,579,638
LIABILITIES			
Accounts payable and other current liabilities	36,103,967	1,303,768	37,407,735
Long-term obligations			
Due within one year			
Bonds, capital leases, and contracts	13,446,974	—	13,446,974
Accrued interest	759,880	—	759,880
Other	7,856,000	—	7,856,000
Due beyond one year			
Net liability for employee pensions	15,968,581	840,452	16,809,032
Total retiree health insurance liability	39,921,452	2,101,129	42,022,581
Bonds, capital leases, and contracts	70,958,588	—	70,958,588
Accrued interest	16,014,649	—	16,014,649
Other	23,082,406	—	23,082,406
Total liabilities	224,112,496	4,245,349	228,357,845
DEFERRED INFLOWS OF RESOURCES			
Decreases in the net pension liability	1,117,801	58,832	1,176,632
Decreases in the total liability for retiree health insurance	2,794,502	147,079	2,941,581
Total deferred inflows of resources	3,912,302	205,911	4,118,213
NET POSITION			
Net investment in capital assets	214,344,140	2,533,430	216,877,570
Restricted for:			
Debt service	4,133,180	—	4,133,180
School-based activities	1,396,569	—	1,396,569
Unrestricted	20,589,736	7,159,152	27,748,888
Total net position	$ 240,463,625	$ 9,692,582	$ 250,156,207

Figure C-2. District-Wide Statement of Activities, School District

Luna Independent School District
Statement of Activities
for the Year Ended June 30, 2017

Functions/Programs	Expenses	Program Revenues: Charges for Services	Program Revenues: Operating Grants and Contributions	Program Revenues: Capital Grants and Contributions	Net (Expense) Revenue and Changes in Net Position: Primary Government: Governmental Activities	Net (Expense) Revenue and Changes in Net Position: Primary Government: Business-Type Activities	Net (Expense) Revenue and Changes in Net Position: Primary Government: Total
Governmental activities:							
Instruction and instruction-related services	$ 238,876,955	$ 5,509,719	$ 27,631,301	$ —	$ (205,735,935)		$ (205,735,935)
Instructional and school leadership	34,166,630	—	3,783,490	—	(30,383,140)		(30,383,140)
Support services—student-based	37,963,791	2,986,172	4,203,974	—	(30,773,645)		(30,773,645)
Administrative support services	9,528,781	—	1,055,183	—	(8,473,598)		(8,473,598)
Support services—nonstudent-based	58,382,470	—	5,465,065	—	(52,917,405)		(52,917,405)
Community services	2,801,454	—	131,297	—	(2,670,157)		(2,670,157)
Interest on long-term debt	5,969,465	—	—	—	(5,969,465)		(5,969,465)
Total government activities	387,689,545	8,495,891	42,270,310	—	(336,923,344)		(336,923,344)
Business-type activities:							
Food services	20,596,032	4,750,350	15,849,235	750,000		$ 753,553	753,553
Adult education	1,837,753	936,150	1,102,491	—		200,888	200,888
Total business-type activities	22,433,785	5,686,500	16,951,726	750,000		954,441	954,441
Total school district	$ 410,123,330	$ 14,182,391	$ 59,222,036	$ 750,000	(336,923,344)	954,441	(335,968,903)
General revenues:							
Taxes:							
Property taxes, levied for general purposes					154,108,322	—	154,108,322
Property taxes, levied for debt service					16,860,557	—	16,860,557
State aid—formula grants					176,265,211	—	176,265,211
Investment earnings					7,397,103	312,271	7,709,374
Special item—gain on sale of building					1,367,341	—	1,367,341
Total general revenues and special item					355,998,534	312,271	356,310,805
Change in net position					19,075,190	1,266,712	20,341,902
Net position—beginning					221,388,435	8,425,870	229,814,305
Net position—ending					$ 240,463,625	$ 9,692,582	$ 250,156,207

Figure C-3. Governmental Funds Balance Sheet, School District

Luna Independent School District
Balance Sheet
Governmental Funds
As of June 30, 2017

	General Fund	Debt Service Fund	Other Governmental Funds	Total
ASSETS				
Cash and cash equivalents	$ 37,786,672	$ 3,294,850	$ 1,789,520	$ 42,871,042
Investments	61,059,534	—	902,805	61,962,339
Property taxes receivable, net	10,341,512	1,841,218	—	12,182,730
Due from other governments	15,105,826	—	4,862,510	19,968,336
Accrued interest	504,757	—	—	504,757
Due from other funds	5,170,479	759,359	1,852,454	7,782,292
Other receivables	2,529,130	20,695	508,827	3,058,652
Inventories—supplies and materials	1,537,230	—	—	1,537,230
Other current assets	125,109	—	1,593,237	1,718,346
Total assets	$ 134,160,249	$ 5,916,122	$ 11,509,353	$ 151,585,724
LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND FUND BALANCES				
Liabilities:				
Accounts payable and accrued liabilities	$ 27,526,883	$ 8,740	$ 933,434	$ 28,469,057
Due to other funds	23,589,501	—	5,503,492	29,092,993
Due to other governments	10,093	—	—	10,093
Due to student groups	—	—	256,183	256,183
Grants received in advance	1,668,634	—	—	1,668,634
Total liabilities	52,795,111	8,740	6,693,109	59,496,960
Deferred inflows of resources:				
Unavailable tax revenues	6,267,379	1,774,202	—	8,041,581
Unavailable grant revenues	4,580,022	—	1,243,438	5,823,460
Total deferred inflows of resources	10,847,401	1,774,202	1,243,438	13,865,041
Fund balances:				
Nonspendable: Inventories	1,537,230	—	—	1,537,230
Restricted for:				
Debt service	—	4,133,180	—	4,133,180
Early childhood programs	3,161,173	—	—	3,161,173
Committed to:				
Classroom technology	—	—	333,000	333,000
Athletic facilities	1,000,000	—	250,000	1,250,000
Assigned to:				
New middle school construction	21,222,556	—	—	21,222,556
Extended day program	—	—	2,989,806	2,989,806
Unassigned	43,596,778	—	—	43,596,778
Total fund balances	70,517,737	4,133,180	3,572,806	78,223,723
Total liabilities, deferred inflows of resources, and fund balances	$ 134,160,249	$ 5,916,122	$ 11,509,353	

Amounts reported for governmental activities in the statement of net position are different because:			
Capital assets used in governmental activities are not financial resources and, therefore, are not reported as assets in governmental funds. The cost of the assets is $413,700,956 and the accumulated depreciation is $98,176,725.			315,524,231
Property taxes receivable and amounts due from other governments will be collected this year but are not available soon enough to pay for the current period's expenditures; therefore, they are deferred in the funds. They are not, however, deferred in the governmental activities.			13,865,041
An internal service fund is used by the district's management to charge the costs of the workers' compensation insurance program to the individual funds. The net position of the internal service fund is included with the governmental activities.			8,766,340
Certain deferred outflows of resources ($10,138,401) and deferred inflows of resources ($3,912,302) are reported for governmental activities but not in the governmental funds. The amount by which deferred outflows of resources exceeded deferred inflows of resources was:			6,226,099
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported as liabilities in the funds. Long-term liabilities at year-end consist of:			
	Bonds, capital leases, and contracts	$ 84,405,562	
	Accrued interest	16,774,529	
	Net pension liability	15,968,581	
	Net OPEB liability	39,921,452	
	Other	25,071,685	
			(182,141,808)
Total net position—governmental activities			$ 240,463,625

Figure C-4. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, School District

Luna Independent School District
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
for the Year Ended June 30, 2017

	General Fund	Debt Service Fund	Other Governmental Funds	Total
REVENUES				
Property taxes	$ 153,862,367	$ 16,589,425	$ —	$ 170,451,792
Investment earnings	6,736,986	483,183	176,934	7,397,103
Tuition charges	1,283,778	—	4,225,941	5,509,719
Facility rental fees	2,437,009	—	—	2,437,009
State revenues	188,019,530	—	6,135,833	194,155,363
Federal revenues	2,284,748	—	22,095,410	24,380,158
Other	107,604	—	441,559	549,163
Total revenues	354,732,022	17,072,608	33,075,677	404,880,307
EXPENDITURES				
Current:				
Instruction and instruction-related services	206,958,475	—	25,936,202	232,894,677
Instructional and school leadership	31,485,279	—	1,825,705	33,310,984
Support services—student-based	34,010,001	—	3,003,049	37,013,050
Administrative support services	9,290,149	—	—	9,290,149
Support services—nonstudent-based	55,615,563	—	1,308,415	56,923,978
Community services	1,691,107	—	1,040,189	2,731,296
Debt service:				
Principal	1,160,471	11,985,914	380,561	13,526,946
Interest	378,447	3,908,791	124,107	4,411,345
Capital outlay	922,537	—	8,327	930,864
Total expenditures	341,512,029	15,894,705	33,626,555	391,033,289
Excess (deficiency) of revenues over expenditures	13,219,993	1,177,903	(550,878)	13,847,018
OTHER FINANCING SOURCES (USES)				
Proceeds from capital leases	—	—	692,245	692,245
SPECIAL ITEM				
Proceeds from sale of building	2,601,908	—	—	2,601,908
Net change in fund balance	15,821,901	1,177,903	141,367	17,141,171
Fund balances—beginning	54,695,836	2,955,277	3,431,439	61,082,552
Fund balances—ending	$ 70,517,737	$ 4,133,180	$ 3,572,800	$ 78,223,723

Figure C-5. Reconciliation of Net Changes in Governmental Fund Balances to Governmental Activities in Net Position, School District

Luna Independent School District
Reconciliation of the Governmental Funds Statement of Revenues,
Expenditures, and Changes in Fund Balances with the District-Wide Statement of Activities
for the Year Ended June 30, 2017

Total net changes in fund balances—governmental funds		$ 17,141,171
Amounts reported for governmental activities in the statement of activities are different because:		
Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures. However, for governmental activities, those costs are shown in the statement of net position and allocated over their estimated useful lives as annual depreciation expenses in the statement of activities. This is the amount by which depreciation exceeds capital outlays in the period.		
Depreciation expense	$ (6,555,000)	
Capital outlays	930,864	(5,624,136)
Some of the capital assets acquired this year were financed with capital leases. The amount financed by the leases is reported in the governmental funds as a source of financing. On the other hand, the capital leases are not revenues in the statement of activities but, rather, constitute long-term liabilities in the statement of net position.		(692,245)
Because some property taxes will not be collected for several months after the District's fiscal year ends, they are not considered as "available" revenues in the governmental funds and are instead counted as deferred tax revenues. They are, however, recorded as revenues in the statement of activities.		517,087
In the statement of activities, only the gain on the sale of the building is reported, whereas in the governmental funds, the entire proceeds from the sale increase financial resources. Thus, the change in net position differs from the change in fund balances by the cost of the building sold.		(1,234,567)
In the statement of activities, certain operating expenses—compensated absences (vacations) and special termination benefits (early retirement)—are measured by the amounts earned during the year. In the governmental funds, however, expenditures for these items are measured by the amount of financial resources used (essentially, the amounts actually paid). This year, special termination benefits paid ($10,300,426) exceeded the amounts earned ($7,906,074) by $2,394,352. Vacation used ($261,132) was less than the amounts earned ($327,280) by $66,148. Other expenses incurred exceeded the amounts paid in the governmental funds by $6,553,809.		(4,225,605)
Repayment of bond principal is an expenditure in the governmental funds, but it reduces long-term liabilities in the statement of net position and does not affect the statement of activities.		13,526,946
Interest on long-term debt in the statement of activities differs from the amount reported in the governmental funds because interest is recorded as an expenditure in the funds when it is due and, thus, requires the use of current financial resources. In the statement of activities, however, interest expense is recognized as the interest accrues, regardless of when it is due. The additional interest reported in the statement of activities is the net result of two factors. First, accrued interest on bonds, leases, and contracts payable decreased by $43,380. Second, $1,601,500 of additional accumulated interest was accreted on the District's capital appreciation bonds.		(1,558,120)
An internal service fund is used by the District's management to charge the costs of the workers' compensation insurance program to the individual funds. The net revenue of the internal service fund is reported with governmental activities.		1,224,659
Change in net position of governmental activities		$ 19,075,190

Figure C-6. Proprietary Funds Statement of Net Position, School District

Luna Independent School District
Statement of Net Position
Proprietary Funds
As of June 30, 2017

	Enterprise Funds			
	Adult Education	Food Service	Total	Internal Service Fund
ASSETS				
Current assets:				
Cash and cash equivalents	$ 1,844,430	$ 5,820,282	$ 7,664,712	$ —
Investments	12,781	150,750	163,531	—
Due from other governments	634,808	1,368,113	2,002,921	—
Due from other funds	—	—	—	20,333,061
Other receivables	—	4,081	4,081	—
Inventories—supplies and materials	477,150	1,472,376	1,949,526	—
Total current assets	2,969,169	8,815,602	11,784,771	20,333,061
Noncurrent assets				
Furniture and equipment (net)	—	2,533,430	2,533,430	—
Total assets	2,969,169	11,349,032	14,318,201	20,333,061
DEFERRED OUTFLOWS OF RESOURCES				
Increases in the net pension liability	126,068	—	126,068	—
Increases in the total liability for retiree health insurance	315,169	—	315,169	—
Total deferred outflows of resources	441,237	—	441,237	—
LIABILITIES				
Current liabilities:				
Accounts payable and accrued liabilities	96,579	1,207,189	1,303,768	—
Claims payable	—	—	—	5,700,000
Due to other funds	375,061	240,536	615,597	—
Total current liabilities	471,640	1,447,725	1,919,365	5,700,000
Noncurrent liabilities				
Claims payable	—	—	—	5,886,721
Net pension liability	840,452	—	840,452	—
Total retiree health insurance liability	2,101,129	—	2,101,129	—
Total noncurrent liabilities	2,941,581	—	2,941,581	11,566,721
Total liabilities	3,413,221	1,447,725	4,860,946	11,566,721
DEFERRED INFLOWS OF RESOURCES				
Decreases in the net pension liability	58,832	—	58,832	—
Decreases in the total liability for retiree health insurance	147,079	—	147,079	—
Total deferred inflows of resources	205,911	—	205,911	—
NET POSITION				
Net investment in capital assets	—	2,533,430	2,533,430	—
Unrestricted	(208,726)	7,367,877	7,159,151	8,766,340
Total net position	$ (208,726)	$ 9,901,307	$ 9,692,581	$ 8,766,340

Figure C-7. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, School District

Luna Independent School District
Statement of Revenues, Expenses, and Changes in Fund Net Position
Proprietary Funds
for the Year Ended June 30, 2017

	Enterprise Funds			
	Adult Education	Food Service	Total	Internal Service Fund
Operating revenues:				
User charges	$ 936,150	$ 4,750,350	$ 5,686,500	$ 23,864,586
Total operating revenues	936,150	4,750,350	5,686,500	23,864,586
Operating expenses:				
Payroll costs	888,793	10,494,786	11,383,579	—
Professional and contract services	—	343,439	343,439	—
Supplies and materials	67,228	8,773,317	8,840,545	—
Facility rental	826,746	—	826,746	—
Other operating costs	54,986	984,490	1,039,476	22,639,927
Total operating expenses	1,837,753	20,596,032	22,433,785	22,639,927
Operating income (loss)	(901,603)	(15,845,682)	(16,747,285)	1,224,659
Nonoperating revenues:				
Investment earnings	10,861	301,410	312,271	—
Grants	1,102,491	15,849,235	16,951,726	—
Total nonoperating revenues	1,113,352	16,150,645	17,263,997	—
Income before capital contributions	211,749	304,963	516,712	1,224,659
Capital contributions	—	750,000	750,000	—
Change in net position	211,749	1,054,963	1,266,712	1,224,659
Total net position—beginning	(420,475)	8,846,344	8,425,869	7,541,681
Total net position—ending	$ (208,726)	$ 9,901,307	$ 9,692,581	$ 8,766,340

Figure C-8. Proprietary Funds Statement of Cash Flows, School District

Luna Independent School District
Statement of Cash Flows
Proprietary Funds
for the Year Ended June 30, 2017

	Enterprise Funds			
	Adult Education	Food Services	Total	Internal Service Funds
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from user charges	$ 1,052,578	$ 4,851,104	$ 5,903,682	$ —
Cash received from assessments made to other funds	—	—	—	22,639,927
Cash payments to employees for services	(888,793)	(10,494,786)	(11,383,579)	—
Cash payments for insurance claims	—	—	—	(22,639,927)
Cash payments to suppliers for goods and services	(35,449)	(7,855,737)	(7,891,186)	—
Cash payments for facility use	(826,746)	—	(826,746)	—
Cash payments for other operating expenses	—	(2,593)	(2,593)	—
Net cash used for operating activities	(698,410)	(13,502,012)	(14,200,422)	—
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Grants received	897,983	15,574,568	16,472,551	—
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Capital contributions	—	750,000	750,000	—
Acquisition of capital assets	—	(1,522,918)	(1,522,918)	—
Net cash used for capital and related financing activities	—	(722,918)	(772,918)	—
CASH FLOWS FROM INVESTING ACTIVITIES				
Purchase of investments	(16,271)	(135,217)	(151,488)	—
Proceeds from maturities of investments	14,280	115,625	129,905	—
Interest on investments	10,042	285,446	295,488	—
Net cash provided by investing activities	8,051	265,854	273,905	—
Net increase in cash and cash equivalents	207,624	1,565,492	1,773,116	—
Cash and cash equivalents—beginning	1,636,806	4,254,790	5,891,596	—
Cash and cash equivalents—ending	$ 1,844,430	$ 5,820,282	$ 7,664,712	$ —
Reconciliation of operating income (loss) to net cash provided (used) by operating activities				
Operating income (loss)	$ (901,603)	$ (15,845,682)	$ (16,747,285)	$ 1,224,659
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:				
Depreciation	—	981,897	981,897	—
Commodities used	—	1,684,867	1,684,867	—
Changes in assets and liabilities:				
Receivables	116,428	100,754	217,182	(2,549,089)
Inventories	94,794	210,239	305,033	—
Accrued liabilities	(5,684)	(371,455)	(377,139)	1,324,430
Unearned revenue	(2,345)	(262,632)	(264,977)	—
Net cash provided by operating activities	$ (698,410)	$ (13,502,012)	$ (14,200,422)	$ —

NONCASH NONCAPITAL FINANCING ACTIVITIES

During the year, the District received $1,684,867 of food commodities from the U.S. Department of Agriculture.

NONCASH INVESTING ACTIVITIES

During the year, the District had $16,783 of unrealized gains on its enterprise funds investments.

Figure C-9. Statement of Fiduciary Net Position, School District

Luna Independent School District
Statement of Fiduciary Net Position
As of June 30, 2017

	Private–Purpose Trust	Agency Funds
ASSETS		
Cash and cash equivalents	$ 32,578	$ 101,959
Investments	247,509	—
Due from other governments	—	100,242
Accrued interest	23,853	—
Due from other funds	321,026	1,272,211
Total assets	624,966	$ 1,474,412
LIABILITIES		
Accounts payable	1,450	$ 14,911
Due to student groups	—	1,239,739
Due to other governments	—	219,762
Total liabilities	1,450	$ 1,474,412
NET POSITION		
Held for scholarships	623,516	
Total net position	$ 623,516	

Figure C-10. Statement of Changes in Fiduciary Net Position, School District

Luna Independent School District
Statement of Changes in Fiduciary Net Position
for the Year Ended June 30, 2017

	Private-Purpose Trust
ADDITIONS	
Private donations	$ 24,480
District contribution	5,000
Investment earnings	32,487
Total additions	61,967
DEDUCTIONS	
Scholarships awarded	36,644
Changes in net position	25,323
Net position—beginning	598,193
Net position—ending	$ 623,516

APPENDIX D

FINANCIAL STATEMENTS FOR A PUBLIC COLLEGE OR UNIVERSITY ENGAGED IN BOTH GOVERNMENTAL AND BUSINESS-TYPE ACTIVITIES

Page Number

Figure D-1. Institution-Wide Statement of Net Position, Public College or University D-3

Figure D-2. Institution-Wide Statement of Activities, Public College or University D-4

Figure D-3. Governmental Funds Balance Sheet, Public College or University D-5

Figure D-4. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, Public College or University D-6

Figure D-5. Proprietary Funds Statement of Net Position, Public College or University D-7

Figure D-6. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, Public College or University D-8

Figure D-7. Proprietary Funds Statement of Cash Flows, Public College or University D-9

Figure D-1. Institution-Wide Statement of Net Position, Public College or Univerity

Cozy Community College
Statement of Net Position
As of June 30, 2017

	Governmental Activities	Business-Type Activities	Total
ASSETS			
Cash	$ 5,117,496	$ 490,441	$ 5,607,937
Investments	19,889,916	3,150,000	23,039,916
Property taxes receivable	7,981,008	—	7,981,008
Tuition and fees receivable	758,521	—	758,521
Other receivables	635,039	63,468	698,507
Internal balances	167,692	(167,692)	—
Inventories	—	463,424	463,424
Prepaid items	137,120	—	137,120
Land	4,889,818	—	4,889,818
Capital assets, net of accumulated depreciation	62,975,781	868,750	63,844,531
Total assets	102,552,391	4,868,391	107,420,782
LIABILITIES			
Accounts payable	289,606	1,933	291,539
Accrued payroll	1,435,038	60,974	1,496,012
Tuition and fees received in advance	2,431,551	—	2,431,551
Other payments received in advance	102,868	—	102,868
Bonds payable:			
Due within one year	580,000	—	580,000
Due in more than one year	9,840,000	—	9,840,000
Total liabilities	14,679,063	62,907	14,741,970
NET POSITION			
Net investment in capital assets	57,445,599	868,750	58,314,349
Unrestricted	30,427,729	3,936,734	34,364,463
Total net position	$ 87,873,328	$ 4,805,484	$ 92,678,812

Figure D-2. Institution-Wide Statement of Activities, Public College or University

Cozy Community College
Statement of Activities
for the Year Ended June 30, 2017

Functions/Programs	Expenses	Expense Allocation	Program Revenues: Charges for Services: Tuition and Fees	Program Revenues: Charges for Services: Sales, Services, and Other Revenues	Program Revenues: Operating Gifts, Grants, and Contracts	Net Revenues (Expenses) and Changes in Net Position: Governmental Activities	Net Revenues (Expenses) and Changes in Net Position: Business-Type Activities	Net Revenues (Expenses) and Changes in Net Position: Total
Governmental activities:								
Instruction	$ 13,810,090	$ 6,325,073	$ 12,812,745	$ —	$ 263,899	$ (7,058,519)	$ —	$ (7,058,519)
Academic support	860,032	919,058	—	396,752	—	(1,382,338)	—	(1,382,338)
Student services	3,734,433	2,804,118	23,585	396,950	857,352	(5,260,664)	—	(5,260,664)
Public service	1,368,526	—	15,150	—	270,443	(1,082,933)	—	(1,082,933)
General administration	1,785,692	—	—	296,648	—	(1,489,044)	—	(1,489,044)
Operations and maintenance	3,522,463	(3,522,463)	—	—	—	—	—	—
Institutional support	4,541,687	—	—	—	—	(4,541,687)	—	(4,541,687)
Interest	870,320	(870,320)	—	—	—	—	—	—
Depreciation	5,655,466	(5,655,466)	—	—	—	—	—	—
Total governmental activities	36,148,709	—	12,851,480	1,090,350	1,391,694	(20,815,185)	—	(20,815,185)
Business-type activities:								
College bookstore	2,945,641	—	—	3,083,961	—	—	138,320	138,320
Food service	1,753,369	—	—	2,098,643	—	—	345,274	345,274
Industrial training	321,825	—	—	134,458	14,431	—	(172,936)	(172,936)
Total business-type activities	5,020,835	—	—	5,317,062	14,431	—	310,658	310,658
Total primary government	$ 41,169,544	$ —	$ 12,851,480 ①	$ 6,407,412	$ 1,406,125	$ (20,815,185)	$ 310,658	$(20,504,527)
General revenues:								
Property taxes						$ 15,362,534	$ —	$ 15,362,534
State appropriations						10,959,604	—	10,959,604
Interest						543,360	179,391	724,751
Miscellaneous						—	147,282	147,282
Transfers						370,000	(370,000)	—
Total general revenues and transfers						27,237,498	(43,327)	27,194,171
Change in net position						6,422,313	267,331	6,689,644
Net position—beginning						81,451,015	453,813	85,989,168
Net position—ending						$ 87,873,328	$ 4,805,484	$ 92,678,812

Figure D-2 Note

① A separate column for tuition and fees is not required.

Figure D-3. Governmental Funds Balance Sheet, Public College or University

Cozy Community College
Balance Sheet
Governmental Funds
As of June 30, 2017

	General Fund	Grants and Contracts Fund	Other Governmental Funds	Total Governmental Funds
ASSETS				
Cash	$ 1,491,423	$ —	$ 3,155,721	$ 4,647,144
Investments	9,349,916	—	9,790,000	19,139,916
Property taxes receivable	6,049,682	—	1,931,326	7,981,008
Tuition and fees receivable	758,521	—	—	758,521
Interest receivable	111,895	—	164,055	275,950
Internal receivables	138,995	201,897	—	340,892
Prepaid items	1,395,629	—	—	1,395,629
Total assets	$ 19,433,181	$ 201,897	$ 15,041,102	$ 34,676,180
LIABILITIES				
Accounts payable	$ 81,332	$ 13,991	$ 136,386	$ 231,709
Accrued payroll	1,414,199	9,757	5,035	1,428,991
Tuition and fees received in advance	—	75,281	1,090,115	1,165,396
Other payments received in advance	—	102,868	—	102,868
Total liabilities	3,927,082	201,897	1,231,536	5,360,515
FUND BALANCE				
Assigned	—	—	13,809,566	13,809,566
Unassigned	15,506,099	—	—	15,506,099
Total fund balance	15,506,099	—	13,809,566	29,315,665
Total liabilities and fund balance	$ 19,433,181	$ 201,897	$ 15,041,102	29,315,665

Amounts reported for *governmental activities* in the statement of net position are different because:	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	67,865,599
Internal service funds are used by management to charge the cost of certain activities to individual funds. The assets and liabilities of the internal service funds are included in the statement of net position.	1,112,064
Bonds payable are not due and payable in the period and, therefore, are not reported in the funds.	(10,420,000)
Net position of governmental activities	$ 87,873,328

Figure D-4. Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances, Public College or University

Cozy Community College
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
for the Year Ended June 30, 2017

	General Fund	Grants and Contracts Fund	Other Governmental Funds	Total Governmental Funds
REVENUES				
Tuition and fees	$ 12,851,480	$ —	$ —	$ 12,851,480
Property taxes	11,761,887	—	3,600,647	15,362,534
State appropriations	7,999,822	1,743,130	1,216,652	10,959,604
Federal appropriations	—	1,127,795	—	1,127,795
Interest	237,224	—	289,939	527,163
Other revenues	411,211	16,643	926,395	1,354,249
Total revenues	33,261,624	2,884,568	6,033,633	42,182,825
EXPENDITURES				
Current:				
Instruction	12,683,945	1,571,117	—	14,255,062
Academic support	820,110	39,750	172	860,032
Student services	1,613,935	829,338	1,291,160	—
Public service	1,235,673	8,871	123,982	1,368,526
General administration	1,785,692	—	—	1,785,692
Operations and maintenance	3,380,016	—	142,447	3,522,463
Institutional support	3,387,430	82,519	1,220,062	4,690,011
Debt service:				
Principal	—	—	440,000	440,000
Interest	—	—	870,320	870,320
Capital outlay	1,697,874	355,973	1,293,114	3,346,961
Total expenditures	26,604,675	2,887,568	5,381,257	34,873,500
Excess of revenues over expenditures	6,656,949	—	652,376	7,309,325
OTHER FINANCIAL SOURCES (USES)				
Transfers in	370,000	—	1,000,000	1,370,000
Transfers out	(1,000,000)	—	—	(1,000,000)
Total other financing sources (uses)	(630,000)	—	1,000,000	370,000
Net changes in fund balances	6,026,949	—	1,652,376	7,679,325
Fund balances—beginning	9,479,150	—	12,157,190	
Fund balances—ending	$ 15,506,099	$ —	$ 13,809,566	

Amounts reported for *governmental activities* in the statement of activities are different because:	
Governmental activities report depreciation, whereas governmental funds do not.	(5,655,466)
Governmental funds report capital outlay as an expenditure, whereas governmental activities do not.	3,346,961
Governmental funds report debt principal repayment as an expenditure, whereas governmental activities do not.	440,000
Internal service funds are used by management to bring the costs of certain activities to individual funds. The net revenue of the internal service funds is reported with governmental activities.	611,493
Change in net position of governmental activities	$ 6,422,313

Figure D-5. Proprietary Funds Statement of Net Position, Public College or University

Cozy Community College
Statement of Net Position
Proprietary Funds
As of June 30, 2017

	Enterprise Funds				
	College Bookstore	Food Service	Industrial Training	Total	Service Funds
ASSETS					
Current assets:					
Cash and cash equivalents	$ 158,832	$ 331,609	$ —	$ 490,441	$ 470,352
Investments	3,150,000	—	—	3,150,000	750,000
Interest receivable	63,468	—	—	63,468	18,197
Inventories	388,534	74,890	—	463,424	—
Total current assets	3,760,834	406,499	—	4,167,333	1,238,549
Noncurrent assets:					
Capital assets, net of accumulated depreciation	3,794,430	1,241,653	—	5,036,083	1,238,549
Total assets	7,555,264	1,648,152	—	9,203,416	2,477,098
LIABILITIES					
Current liabilities:					
Accounts payable	—	822	1,111	1,933	57,897
Accrued payroll	22,544	26,081	12,349	60,974	6,047
Internal payables	—	—	167,692	167,692	62,541
Total liabilities	22,544	26,903	181,152	230,599	126,485
NET POSITION					
Net investment in capital assets	3,974,430	1,241,653	—	5,036,083	1,238,549
Unrestricted	3,738,290	379,596	(181,152)	3,936,734	1,112,064
Total net position	$ 3,771,886	$1,214,750	$ (181,152)	$ 4,805,484	$ 2,350,613

Figure D-6. Proprietary Funds Statement of Revenues, Expenses, and Changes in Fund Net Position, Public College or University

Cozy Community College
Statement of Revenues, Expenses, and Changes in Fund Net Position
Proprietary Funds
for the Year Ended June 30, 2017

	Enterprise Funds				
	College Bookstore	Food Service	Industrial Training	Total	Internal Service Funds
OPERATING REVENUES					
Changes for services	$ 3,083,961	$2,098,643	$ 134,458	$ 5,317,062	$ 4,090,216
Total operating revenues	3,083,961	2,098,643	134,458	5,317,062	4,090,216
OPERATING EXPENSES					
Salaries	239,118	797,747	162,616	1,199,481	78,699
Employee benefits	47,480	104,662	28,544	180,686	2,756,956
Contractual services	299,027	326,314	72,059	697,400	225,576
General material and supplies	2,346,368	387,634	55,840	2,789,842	435,689
Conference and meetings	1,204	43,905	2,766	47,875	—
Depreciation	12,444	93,107	—	105,551	—
Total operating expenses	2,945,641	1,753,369	321,825	5,020,835	3,496,920
Operating income (loss)	138,320	345,274	(187,367)	296,227	593,296
NONOPERATING REVENUES (EXPENSES)					
Interest income	179,391	—	—	179,391	18,197
Miscellaneous revenues	140,131	8,346	14,500	162,977	—
Miscellaneous expenses	—	(1,195)	(69)	(1,264)	—
Total nonoperating revenues (expenses)	319,522	7,151	14,431	341,104	18,197
Income before transfers	457,842	352,425	(172,936)	637,331	611,493
TRANSFERS OUT	(370,000)	—	—	(370,000)	—
Changes in net position	87,842	352,425	(172,936)	267,331	611,493
Total net position—beginning	3,684,044	862,325	(8,216)	4,538,153	500,571
Total net position—ending	$ 3,771,886	$1,214,750	$ (181,152)	$ 4,805,484	$ 1,112,064

Figure D-7. Proprietary Funds Statement of Cash Flows, Public College or University

Cozy Community College
Statement of Cash Flows
Proprietary Funds
for the Year Ended June 30, 2017

	College Bookstore	Food Service	Industrial Training	Total	Internal Service Funds
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from customers	$ 3,083,961	$ 2,098,643	$ 134,458	$ 5,317,062	$ 4,090,216
Payments to suppliers	(2,654,610)	(862,515)	(158,242)	(3,675,367)	(3,387,569)
Payments to employees	(234,512)	(797,103)	(161,475)	(1,193,090)	(77,401)
Other receipts	140,131	7,151	14,431	161,713	—
Net cash provided (used) by operating activities	334,970	446,176	(170,828)	610,318	625,246
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Cash repaid by other funds	483,431	191,159	—	674,590	—
Cash borrowed from other funds	—	—	167,692	167,692	62,541
Transfers to other funds	(370,000)	—	—	(370,000)	—
Net cash provided by noncapital financing activities	113,431	191,159	167,692	472,282	62,541
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Acquisition of fixed assets	—	(305,726)	—	(305,726)	—
Net cash used by capital and related financing activities	—	(305,726)	—	(305,726)	—
CASH FLOWS FROM INVESTING ACTIVITIES					
Purchase of investments	(3,150,000)	—	—	(3,150,000)	(750,000)
Sale of investments	2,650,000	—	—	2,650,000	—
Interest on investments	199,226	—	—	199,226	—
Net cash used by investing activities	(300,774)	—	—	(300,774)	(750,000)
Net increase (decrease) in cash and cash equivalents	147,627	331,609	(3,136)	476,100	(62,213)
Balances—beginning of year	11,205	—	3,136	14,341	532,565
Balances—end of year	$ 158,832	$ 331,609	$ —	$ 490,441	$ 470,352
Reconciliation of operating income (loss) to net cash provided (used) by operating activities:					
Operating income (loss)	$ 138,320	$ 345,274	$ (187,367)	$ 296,227	$ 593,296
Adjustments to reconcile operating income to net cash provided (used) by operating activities:					
Cash flows reported in other categories:					
Depreciation expense	12,444	93,107	—	105,551	—
Other income	140,131	8,346	14,500	162,977	—
Other expenses	—	(1,195)	(69)	(1,264)	—
Change in assets and liabilities:					
Inventories	39,482	—	—	39,482	—
Accounts payable	(13)	—	967	954	30,652
Accrued payroll	4,606	644	1,141	6,391	1,298
Net cash provided by operating activities	$ 334,970	$ 446,176	$ (170,828)	$ 610,318	$ 625,246

APPENDIX E

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND OTHER ILLUSTRATIONS

Page Number

Figure E-1. Auditor's Report E-3

Figure E-2. Summary of Significant Accounting Policies E-6

Figure E-3. Schedule of Contractually Required Employer Pension Contributions E-11

Figure E-4. Calculations to Determine Local City's Major Funds E-12

Figure E-5. Schedule of Capital Assets by Function E-13

Figure E-1. Auditor's Report

READUM & WEAPE LLP
5 SOBBING ROAD, SUITE 400
Tearful, WX 00000

Independent Auditor's Report

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Big City, Some State, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

At this point, the auditor states its opinion regarding whether the financial statements are presented in conformity with the accounting standards. If everything is in order, the auditor may present a single overall unqualified opinion. However, if the auditor has identified issues, it will describe the issues and present a qualified or adverse opinion for the specific parts of the financial report that are affected, and present an unmodified opinion for the remainder.

Sample Unqualified Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Big City, Some State, as of June 30, 2017, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Sample Qualified Opinion

In our opinion, except for the possible effects of the matter described in the [description of the issue] paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the aggregate discretely presented component units of Big City, Some State, as of June 30, 2017, and the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Sample Adverse Opinion

In our opinion, because of the significance of the matter described in the [description of the issue] paragraph, the financial statements referred to above do not present fairly the financial position of the governmental activities of Big City, Some State, as of June 30, 2017, or the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis, budgetary comparison information, other employee postemployment benefits information, and employee retirement pension benefits information (collectively, the required supplementary information) on pages XX–XX and XX–XX, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which

consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

If a government has not presented all of the RSI, the preceding paragraph is modified with language identifying the RSI that was omitted.

If a government presents SI with its financial statements, the auditor's report contains paragraphs similar to the following.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Big City's basic financial statements. The combining and individual nonmajor fund financial statements and budgetary schedules on pages XX—XX and XX—XX, respectively, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

This supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Big City's basic financial statements. The introductory and statistical sections are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

[Signature of the auditor]

[City and state of the auditor]

[Date]

Figure E-2. Summary of Significant Accounting Policies

Note 1—Summary of Significant Accounting Policies

A. Reporting Entity

The accompanying financial statements present the activities of the City (the primary government) and its three component units, entities for which the City is financially accountable. Local Public School District and Local City Landfill Authority are displayed in a separate, discrete column in the financial statements (to emphasize their legal separateness from the primary government). Local City Redevelopment Agency, although legally separate, is so intertwined with the City that it is, in substance, one and the same. Accordingly, it is blended with the primary government. The following table describes the City's component units:

Component Unit	Description; Criteria for Inclusion	Reporting Method	For Separate Financial Statements
Local City Redevelopment Agency	Tax increment district redevelopment; Council members comprised the board, and City has operational responsibility for the Agency.	Blended	Not available
Local Public School District	Kindergarten through high school system; separate board appointed by Council; City finances a substantial portion of operations and guarantees payment of debt.	Discrete	Local Public School District 789 Milligan Lane Local City, ST
Local City Landfill Authority	Operation of landfill within City; separate board appointed by Council; rates approved by Council.	Discrete	Landfill Authority 456 Galloway Drive Local City, ST

In addition, the City participates in a joint venture with Sample County for operation of the Metro Zoo. The City Council is responsible for other related organization board appointments to the Local Fine Arts League and the Local Historical Society. See Notes 20 and 21 for more detailed financial information regarding these relationships.

B. Basis of Presentation, Basis of Accounting

Basis of Presentation

Government-Wide Statements: The statement of net position and the statement of activities display information about the City as a whole. These statements include the financial activities of the overall government, except for fiduciary activities. The government-wide statements provide information about the primary government (the City) and its component units without displaying funds. These statements also distinguish between the *governmental* and *business-type activities* of the City and between the City and its discretely presented component units. Eliminations have been made to minimize the double counting of internal activities.

The statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities.

- Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function.
- Indirect expenses—expenses of the general government related to the administration and support of the City's programs, such as personnel and accounting (but not interest on long-term debt)—are allocated to programs based on their percentage of total primary government expenses. Interest expenses are allocated to the programs that manage the capital assets financed with long-term debt.
- Program revenues include charges paid by the recipients of goods or services offered by the programs and grants, and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements: The fund financial statements provide information about the City's funds, including fiduciary funds and blended component units. Separate statements for each fund category—*governmental, proprietary,* and *fiduciary*—are presented. The emphasis of governmental and enterprise fund reporting (enterprise funds are a type of proprietary fund) is on major funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds. Internal service funds and fiduciary funds are aggregated and reported by fund type and fund classification, respectively.

The City has the following major governmental funds:

- *General fund*. This is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- *HUD programs*. This special revenue fund accounts for grants received from the U.S. Department of Housing and Urban Development. Grants are restricted for accomplishing objectives of the Community Development Block Grant Program, rental rehabilitation and related loan activities, and residential redevelopment.

- *Community redevelopment*. This fund accounts for revenue received from tax increment financing. Those revenues are restricted to carrying out redevelopment in the designated area.
- *Route 7 construction*. This fund accounts for grants and bond proceeds restricted to the improvement and construction of Route 7.

④ Proprietary fund *operating* revenues and expenses are related to providing water and sewer services to the residents and businesses of Local City, operating the City's parking garages, and providing the following services to other parts of the City government: casualty, health, and life insurance; fleet management; telecommunications; and data processing. Revenues and expenses arising from capital and noncapital financing activities and from investing activities are presented as nonoperating revenues or expenses.

The City has the following major proprietary funds:

- *Water and sewer fund*. This fund accounts for the activities of the City's water and sewer utility.
- *Parking facilities fund*. This fund accounts for the activities of the City's parking facilities.

Additionally, the City reports the following funds:

- *Internal service funds.* These funds account for the financing of goods and services provided by one department to other departments on a cost-reimbursement basis, including casualty, health, and life insurance; fleet management; telecommunications; and data processing.
- *Pension trust fund.* This fund reports the trust arrangement for the City employee pension plan.
- *Private-purpose trust fund.* This fund reports a trust arrangement under which principal and income benefit individuals and private organizations.
- *Agency fund.* This fund reports resources held for other governments on a short-term basis in a purely custodial capacity.

Basis of Accounting

⑤ The basis of accounting determines when transactions are reported on the financial statements. The government-wide, proprietary funds, and fiduciary funds financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of whe n the related cash flows take place. Nonexchange transactions, in which the City receives value without directly giving equal value in return, include property taxes, grants, entitlements, and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

⑥ Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized

when measurable and available. The City considers all revenues available if they are collected within 60 days after year-end. Expenditures are recorded when the related fund liability is incurred, except for unmatured principal and interest on general long-term debt, which is recognized when due. Claims, judgments, and compensated absences are recognized as expenditures only to the extent they are normally expected to be paid from existing unrestricted fund balance. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term liabilities and acquisitions under capital leases are reported as other financing sources.

⑦ Under the terms of grant agreements, the City funds certain programs by a combination of specific cost-reimbursement grants, categorical block grants, and general revenues. Thus, when program expenses are incurred, there is both restricted and unrestricted net position available to finance the program. It is the City's policy to first apply cost-reimbursement grant (restricted) resources to such programs, followed by general revenues (unrestricted).

C. Budgetary Data

Annual budgets are adopted for the general fund and the HUD fund. The budgetary basis of accounting is modified accrual with the following exceptions:

- Claims and compensated absences are budgeted on the cash basis.
- Encumbrances are budgeted as expenditures in the year the order is placed.

All unencumbered appropriation balances lapse at year-end.

The preceding budgetary disclosure appears in the notes if the budgetary comparison is presented as a basic financial statement. If the budgetary comparison is presented as RSI (as it is for Local City), the disclosure is included in notes to RSI.

D. Assets and Liabilities

Cash and Investments

The City's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. All short-term cash surpluses are maintained in a cash and investments pool, the earnings from which are allocated to each fund based on month-end deposit and investment balances.

Investments are reported at fair value, based on quoted market prices, except for money market investments, which are reported at amortized cost.

Inventories

Inventories are valued at cost using the first in/first out (FIFO) method. Inventories in the general fund are accounted for using the "consumption" method in the governmental fund financial statements.

Capital Assets

Capital assets purchased or constructed are recorded as expenditures in the governmental funds but are capitalized at historical cost or estimated historical cost in the government-wide statements and proprietary funds. Capitalization of infrastructure assets acquired or constructed prior to 2002, the year the City implemented GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* is limited to major capital assets acquired or constructed since 1980. Capital assets are reported at actual or estimated historical cost based on appraisals or deflated current replacement cost. Contributed assets are reported at estimated fair value at the time received. The City does not capitalize works of art, historical treasures, and similar assets that are held for public exhibition, are preserved, and are subject to a City policy that requires the proceeds of sales of collection items to be used to acquire other items for the collection. Net interest expense incurred during construction is capitalized when it can be attributed to a specific project.

Depreciation methods and estimated useful lives of capital assets reported in the government-wide statements and proprietary funds are as follows:

	Depreciation Method	Estimated Useful Life
Buildings and improvements	Straight-line	20–50 years
Equipment	Declining-balance	7–10
Bridges	Straight-line	40–75
Distribution and collection systems	Straight-line	30–40

Depreciation is used to allocate the actual or estimated historical cost of all capital assets (except roads) over their estimated useful lives. For roads and highways the City uses the modified approach, under which the City reports the annual expenses for maintaining and preserving infrastructure assets at a predetermined condition level selected by the City, in lieu of depreciating the assets' historical cost.

Compensated Absences

The City uses the vesting method to compute compensated absences for sick leave.

E. Fund Balance

The City reports fund balance in five categories—nonspendable, restricted, committed, assigned, and unassigned. Restricted fund balance has been limited to specific uses by external parties or individuals, such as the State and federal governments. Committed fund balance has been limited to specific uses by ordinance, the City's highest level of decision-making authority. Assigned fund balance has been identified as intended for specific uses by the City's commissioner of finance, under the authority of the City Council.

When resources are available from more than one category for spending on a particular purpose, it is the City's policy to spend resources in this order: restricted, committed, assigned, and unassigned.

Figure E-3. Schedule of Contractually Required Employer Pension Contributions

① Himalaya Village
Schedule of Pension Contributions
② Past 10 Fiscal Years
(dollars in thousands) ③

	20X9	20X8	20X7	20X6	20X5	20X4	20X3	20X2	20X1	20X0
Contractually required contribution ④	$ 2,095	$ 2,057	$ 1,969	$ 1,649	$ 1,176	$ 898	$ 820	$ 769	$ 880	$ 1,082
Contributions in relation to the contractually required contribution	(2,095)	(2,057)	(1,969)	(1,649)	(1,176)	(898)	(820)	(769)	(880)	(1,082)
Contribution deficiency (excess)	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
District's covered-employee payroll	$ 12,097	$ 10,962	$ 10,063	$ 9,634	$ 9,538	$ 9,410	$ 9,004	$ 8,442	$ 8,042	$ 7,784
Contributions as a percentage of covered-employee payroll	17.32%	18.76%	19.57%	17.11%	12.33%	9.54%	9.10%	9.11%	10.94%	13.90%

Figure E-3 Notes

① If a government has a contractually or statutorily required contribution amount for its OPEB plan, it would present a schedule like this for OPEB as well.

② This sample schedule presents a full 10 years for illustrative purposes. Governments should have all of the information necessary to present all 10 years. However, they may build this schedule prospectively under certain circumstances and, therefore, may present only a few years at this time.

③ Dollar amounts have been rounded off to the nearest thousand.

④ Alternatively, a government's contribution requirement may be established in statute instead of via contract.

Figure E-4. Calculations to Determine Local City's Major Funds

*Numbers **in maroon** show where funds qualify as major because they represent at least 10 percent of all governmental funds AND 5 percent of all government and enterprise funds combined.*

Fund	Assets plus Deferred Outflows	Total Governmental Fund Assets plus Deferred Outflows	Percentage	Liabilities plus Deferred Inflows	Total Governmental Liabilities plus Deferred Inflows	Percentage
General	$ 9,408,550	$51,705,690	18.20%	$7,753,184	$16,812,584	**46.12%**
HUD	7,504,765	51,705,690	14.51%	6,428,389	16,812,584	**38.24%**
Comm. Redev.	13,616,035	51,705,690	**26.33%**	440,548	16,812,584	2.62%
Route 7	10,478,037	51,705,690	20.26%	1,115,632	16,812,584	6.64%

Fund	Assets plus Deferred Outflows	Total Governmental and Enterprise Funds Assets plus Deferred Outflows	Percentage	Liabilities plus Deferred Inflows	Total Governmental and Enterprise Liabilities plus Deferred Inflows	Percentage
General	$9,408,550	$266,141,717	3.54%	$7,753,184	$155,149,158	**5.00%**
HUD	7,504,765	266,141,717	2.82%	6,428,389	98,083,172	**6.55%**
Comm. Redev.	13,616,035	266,141,717	**5.12%**	440,548	98,083,172	0.45%
Route 7	10,478,037	266,141,717	3.94%	1,115,632	98,083,172	1.14%

Fund	Revenues	Total Governmental Revenues	Percentage	Expenditures	Total Governmental Expenditures	Percentage
General	$86,022,165	$97,482,467	**88.24%**	$88,717,173	$121,332,470	**73.12%**
HUD	2,731,473	97,482,467	2.80%	2,954,389	121,332,470	2.43%
Comm. Redev.	549,489	97,482,467	0.56%	2,664,485	121,332,470	2.20%
Route 7	273,100	97,482,467	0.28%	11,298,469	121,332,470	9.31%

Fund	Revenues	Total Governmental and Enterprise Revenues	Percentage	Expenditures	Total Governmental and Enterprise Expenditures/ Expenses	Percentage
General	$86,022,165	$113,960,980	**75.48%**	$88,717,173	$138,413,546	**64.10%**
HUD	2,731,473	113,960,980	2.40%	2,954,389	138,413,546	2.13%
Comm. Redev.	549,489	113,960,980	0.48%	2,664,485	138,413,546	1.93%
Route 7	273,100	113,960,980	0.24%	11,298,469	138,413,546	8.16%

Figure E-5. Schedule of Capital Assets by Function

County of Reesepepper
Schedule of Capital Assets by Function
As of December 31, 2017

	Land	Buildings and Building Improvements	Equipment	Joint Tenancy	Construction in Progress	Total
General government administration	$ —	$ 100,340	$ 258,040	$ —	$ —	$ 358,380
Judicial administration	18,700	5,223	234,291	—	—	258,214
Public safety	636,081	2,269,673	1,279,236	—	1,355,411	5,540,401
Public works	1,388,757	2,598,628	200,549	—	238,948	4,426,882
Health and welfare	—	474,178	—	—	—	474,178
Education	—	—	—	30,373,229	—	30,373,229
Parks, recreation, and culture	—	1,779,958	674,015	—	74,484	2,528,457
Community development	483,600	9,635	89,086	—	—	582,321
Total general capital assets—primary government	$ 2,527,138	$ 7,237,635	$ 2,735,217	$ 30,373,229	$ 1,668,843	$ 44,542,062

APPENDIX F

GLOSSARY OF TERMS

AAL: see **ACTUARIAL ACCRUED LIABILITY**

ABILITY-TO-PAY RATIOS: comparisons of financial and nonfinancial information, such as **DEBT PER CAPITA**, that measure a government's capacity to raise **REVENUE** or issue debt (Parts 4 and 14)

ACCOUNTABILITY: a responsibility to justify your actions to another party

ACCOUNTING CHANGES: a type of **PRIOR-PERIOD ADJUSTMENT** to make a change in the way something is accounted for; there are three types—**CHANGES IN ACCOUNTING PRINCIPLE, CHANGES IN ACCOUNTING ESTIMATE,** and **CHANGES IN THE REPORTING ENTITY** (Part 13)

ACCOUNTING EQUATION: the equation stating the relationship among the elements recorded by financial accounting. For the **GOVERNMENTAL FUNDS**, it is assets + deferred outflows = liabilities + deferred inflows + fund balance; the equation can be rearranged for other funds and the **GOVERNMENT-WIDE FINANCIAL STATEMENTS:** assets + deferred outflows − liabilities − deferred inflows = net position

ACCOUNT POOL: see **CLAIMS-SERVICING POOL**

ACCOUNTS PAYABLE: amounts a government owes to external persons or groups (Part 5, Fig. 14)

ACCOUNTS RECEIVABLE: amounts a government is due to receive (Part 5, Figs. 10 and 11)

ACCRUAL: a **BASIS OF ACCOUNTING** in which all flows of resources (and thus all **CHANGES IN NET POSITION**) during the year are recorded regardless of whether they involved cash flowing in or out of the government (Part 2, UFR pp. 14 and 18)

ACCUMULATED DEPRECIATION: the sum of all annual **DEPRECIATION** expenses to date for a **CAPITAL ASSET**; it is subtracted from **HISTORICAL COST** on a **STATEMENT OF NET POSITION** (Part 4, Fig. 12)

ACTUARIAL ACCRUED LIABILITY (AAL): under prior accounting standards, the estimated value of **OTHER POSTEMPLOYMENT BENEFITS** attributed to service already completed by current and future retirees (Part 5, UFR p. 110)

ACTUARIALLY DETERMINED CONTRIBUTION: amount calculated by an actuary that a government should contribute annually to a pension or **OTHER POSTEMPLOYMENT BENEFITS** plan, which is intended to ensure that sufficient resources are available to make future benefit payments (Part 6, Fig. 30)

ACTUARIAL VALUE OF ASSETS (AVA): under prior accounting standards, the value assigned in an actuarial valuation to cash, investments, and other property held by an **OTHER POSTEMPLOYMENT BENEFITS** plan for the future payment of benefits (Part 5, UFR p. 110)

ADDITIONS: increases in **FIDUCIARY NET POSITION**, including contributions by employers and employees and investment earnings (Part 10, Figs. 79, B-11, and C-10)

ADJUSTMENT EXPENSES: the costs of investigating and settling claims against a **PUBLIC ENTITY RISK POOL** (Parts 5 and 6, Figs. 26 and 33)

ADVANCE REFUNDING: a **DEBT REFUNDING** in which the proceeds of the refunding bonds are placed with an escrow agent and invested, and the regular debt service payments are made from the proceeds in escrow (and sometimes from an additional revenue source) (Part 5, Fig. 17, BTN p. 85)

AGENCY FUND: a category of **FIDUCIARY FUND** that contains resources held by a government on a temporary, purely custodial basis on behalf of others (Part 10, BTN p. 257)

AGENT MULTIPLE-EMPLOYER PLAN: multiple **SINGLE-EMPLOYER** pension or **OTHER POSTEMPLOYMENT BENEFITS** plans aggregated into one plan, with shared administrative and investment functions; separate accounts are maintained for each employer to ensure that each employer's contributions provide benefits only for its employees; see also **COST-SHARING MULTIPLE-EMPLOYER PLAN** (Part 5)

AMORTIZATION: the systematic recognition of original cost or an original amount received as **EXPENSE** or **REVENUE,** respectively, similar to the use of **DEPRECIATION** for tangible **CAPITAL ASSETS** (Part 5)

AMORTIZED COST: the original cost of debt or acquiring an investment plus the annual amortized discount or premium amounts accumulated to date (Part 5, UFR p. 53)

ANNUAL REQUIRED CONTRIBUTION (ARC): under prior accounting standards, an actuarially determined amount that is expected, if contributed to an **OTHER POSTEMPLOYMENT BENEFITS** plan, to be sufficient to fully fund benefit payments as they come due (Part 5, UFR p. 110)

APPROPRIATIONS: legal authorizations to make expenditures, or to enter into obligations to make expenditures, for specific purposes

ARC: see **ANNUAL REQUIRED CONTRIBUTION**

ARO: see **ASSET RETIREMENT OBLIGATION**

ASSESSED VALUE: the value placed on property during a government's assessment process; it often is a percentage of the **ESTIMATED ACTUAL VALUE OF PROPERTY** (Part 8, Fig. 48, KIM pp. 189 and 191)

ASSET NETWORK: a system of related **CAPITAL ASSETS,** such as a state highway system (Part 4, BTN p. 41)

ASSET RETIREMENT OBLIGATION (ARO): a liability resulting from a legal requirement to perform certain activities in order to shut down a tangible **CAPITAL ASSET,** such as a nuclear power plant (UFR p. 112)

ASSET SUFFICIENCY RATIO: a measure of the degree to which resources set aside in a pension or **OTHER POSTEMPLOYMENT BENEFITS** trust cover a government's overall obligation to provide pension benefits or **OPEB** to employees and retirees; it is calculated as follows: **FIDUCIARY NET POSITION** divided by **TOTAL PENSION LIABILITY** (or **FIDUCIARY NET POSITION** divided by **TOTAL OPEB LIABILITY**) (Part 6)

ASSETS: resources controlled by a government that can be used to provide service

ASSIGNED FUND BALANCE: the portion of **FUND BALANCE** that represents resources a government intends to use for a particular purpose; resources in **GOVERNMENTAL FUNDS** other than the **GENERAL FUND** are, at a minimum, assigned (Part 9, Fig. 53)

AUDITOR'S REPORT: a letter accompanying the financial statements that presents a CPA firm's or state auditor's opinion concerning whether the statements are presented fairly in accordance with **GAAP** (Part 3, Fig. E-1)

AVA: see **ACTUARIAL VALUE OF ASSETS**

BALANCE SHEET: a financial statement that compares what an entity owns with what it owes; governments use it to report the **CURRENT FINANCIAL RESOURCES** of the **GOVERNMENTAL FUNDS**, and sometimes to report the **ECONOMIC RESOURCES** of the **PROPRIETARY FUNDS** (Part 9, Figs. 53, B-3, C-3, and D-3)

BANs: see **BOND ANTICIPATION NOTES**

BANKING POOL: a type of **PUBLIC ENTITY RISK POOL** holding resources that can be used to make loans to member governments experiencing losses (Parts 5 and 6, BTN p. 114)

BASIC FINANCIAL STATEMENTS (BFS): the heart of a government's annual financial report, consisting of **GOVERNMENT-WIDE FINANCIAL STATEMENTS**, **FUND FINANCIAL STATEMENTS**, and **NOTES TO THE FINANCIAL STATEMENTS**

BASIS OF ACCOUNTING: the decision standards a government employs to determine when to record the **FINANCIAL STATEMENT** items specified by the relevant **MEASUREMENT FOCUS**; three principal bases used by governments are **ACCRUAL**, **MODIFIED ACCRUAL**, and cash (Part 2, UFR pp. 14 and 18)

BASIS RISK: the risk of losing protection from loss of fair value or cash flows because the variable interest rates on a **DERIVATIVE** and the underlying instrument or agreement are based on different indexes (Part 5, Fig. 21)

BFS: see **BASIC FINANCIAL STATEMENTS**

BLENDED COMPONENT UNITS: COMPONENT UNITS that are aggregated within the **PRIMARY GOVERNMENT**, as opposed to **DISCRETELY PRESENTED COMPONENT UNITS** (Part 12, UFR p. 283)

BOND ANTICIPATION NOTES (BANs): a type of **NOTE** issued in advance of the receipt of proceeds from a bond issue; it is repaid with a portion of those proceeds (BTN p. 80)

BONDS: a form of debt issued by governments that is repaid, generally with **INTEREST**, over periods stretching from a few years to several decades; they typically are issued to finance the acquisition, construction, and rehabilitation of **CAPITAL ASSETS**

BTA: see **BUSINESS-TYPE ACTIVITIES**

BUDGETARY COMPARISON: a comparison of a government's **ORIGINAL BUDGET** and **FINAL BUDGET** with actual results for a given year; a government may present the comparison as one of the **BASIC FINANCIAL STATEMENTS** or as a schedule with the **RSI** (Part 10, Figs. 60–62)

BUSINESS-TYPE ACTIVITIES (BTA): activities primarily financed with fees charged for goods and services and generally reported in **ENTERPRISE FUNDS**, as well as the **GOVERNMENT-WIDE FINANCIAL STATEMENTS** (Parts 4–8 and 11)

CAFR: see **COMPREHENSIVE ANNUAL FINANCIAL REPORT**

CALLS: features of a bond agreement or other financial instrument that allow a government to redeem the bond or instrument prior to its original **MATURITY** (Part 5)

CAPITAL AND RELATED FINANCING CASH FLOWS: cash received and disbursed by a government for the purpose of buying, selling, building, and rehabilitating **CAPITAL ASSETS** (Part 10, Fig. 70)

CAPITAL ASSET DEPLETION RATIO: a **FINANCIAL EFFICIENCY RATIO** that approximates the average remaining **USEFUL LIFE** of a government's **CAPITAL ASSETS;** it is calculated as follows: [(**HISTORICAL COST** – **ACCUMULATED DEPRECIATION**) ÷ historical cost] × 100 (Part 14)

CAPITAL ASSET REPLENISHMENT RATIO: a **FINANCIAL EFFICIENCY RATIO** that measures whether a government's investment in **CAPITAL ASSETS** is keeping pace with physical deterioration; it is calculated as follows: capital **EXPENDITURES** ÷ **DEPRECIATION** (Part 14)

CAPITAL ASSETS: assets used in operations that have initial **USEFUL LIVES** of more than one year, such as land, buildings, improvements to buildings, vehicles, equipment, and **INFRASTRUCTURE** (Parts 4–6, Figs. 12, 32, 35, and E-5, BTN pp. 41 and 70)

CAPITAL GRANTS AND CONTRIBUTIONS: INTERGOVERNMENTAL AID and donations received or provided to finance construction or acquisition of capital assets (Part 7, Fig. 42)

CAPITAL LEASES: contracts under which a government obtains the right to use another entity's **CAPITAL ASSET** and which meet at least one of the following criteria: the government owns the asset when the lease ends, the government can purchase the asset at a significant discount, the lease lasts 75 percent or more of the remaining useful life of the asset, or the value of the lease is close to the value of the asset if purchased (Parts 5 and 8, Fig. 44, UFR p. 42, UFR p. 98)

CAPITAL PROJECTS FUND: a **GOVERNMENTAL FUND** to account for the flows of resources related to the construction, acquisition, and renovation of **CAPITAL ASSETS** (Part 9, BTN p. 194)

CATEGORICAL GRANTS: INTERGOVERNMENTAL AID restricted to a specific purpose

CERTIFICATES OF PARTICIPATION (COPs): an arrangement by which an investor buys a share of a governmental entity's lease payments

CHANGE IN FINANCIAL POSITION: refers to how finances changed as a government was run during the course of a period; most simply defined as a **CHANGE IN NET POSITION** (Part 7)

CHANGE IN FUND BALANCE: the increase or decrease from year to year in **FUND BALANCE,** it is the sum of the flows reported in the **GOVERNMENTAL FUNDS** (Part 9, Fig. 54)

CHANGE IN FUND NET POSITION: the increase or decrease from year to year in the **NET POSITION** of the **PROPRIETARY FUNDS;** it is the sum total of the flows reported in the **STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION** (Part 9, Fig. 69)

CHANGE IN NET POSITION: the increase or decrease from year to year in the **NET POSITION** of the whole government; it is the sum total of the flows reported in the government-wide **STATEMENT OF ACTIVITIES** (Part 7, Fig. 42)

CHANGES IN ACCOUNTING ESTIMATE: a type of **PRIOR-PERIOD ADJUSTMENT** to change an estimated amount in the financial statements or an estimate that is used in calculating a **FINANCIAL STATEMENT** amount (Part 13)

CHANGES IN ACCOUNTING PRINCIPLE: a type of **PRIOR-PERIOD ADJUSTMENT** to implement new accounting standards or select a different accounting method when the standards allow a choice between methods (Part 13)

CHANGES IN THE REPORTING ENTITY: a type of **PRIOR-PERIOD ADJUSTMENT** to reflect the addition of an organization to, or its removal from, the **REPORTING ENTITY** (Part 13)

CHARGES FOR SERVICES: fees and other charges to the users or recipients of the goods and services a government provides (Part 7, Fig. 42)

CLAIMS AND JUDGMENTS: LIABILITIES of a government related to claims for payment (such as from insured employees) and court-imposed awards

CLAIMS-SERVICING POOL: a type of **PUBLIC ENTITY RISK POOL** arrangement that seeks economies of scale from centralized management but does not involve any mixing of participants' resources; separate accounts are managed for each participating government, from which each government's losses are paid (Parts 5 and 6, BTN p. 114)

CLASSIFIED FORMAT: a method of organizing a **STATEMENT OF NET POSITION** or a **BALANCE SHEET** that divides **ASSETS** and **LIABILITIES** between **CURRENT** and **NONCURRENT** (Part 4, Fig. 1)

COMBINING FINANCIAL STATEMENTS: statements that present the finances of multiple similar accounting entities, such as **NONMAJOR GOVERNMENTAL FUNDS** or individual **INTERNAL SERVICE FUNDS;** combining statements for **COMPONENT UNITS** may be presented among the **BASIC FINANCIAL STATEMENTS,** and for other purposes with the **SUPPLEMENTARY INFORMATION** in the **CAFR** (BTN p. 248, Figs. 63, 64, 72–77, 80–82, 91, and 92)

COMMITTED FUND BALANCE: the portion of **FUND BALANCE** that is constrained by a government itself using its highest level of decision-making authority; committed fund balance cannot be used for any other purpose unless a government again uses its highest level of decision-making authority to change or remove the purpose limitation (Part 9, Fig. 53)

COMMON-SIZE RATIOS: calculations that put financial data in a metric that allows comparisons over time and across governments; see **PERCENTAGE CHANGE** and **PERCENTAGE DISTRIBUTION** (Part 14, Figs. 100 and 101)

COMPARATIVE FINANCIAL STATEMENTS: documents presenting the information from a particular statement for more than one year; governments may include them among the supplementary material in the **CAFR** (UFR p. 32, BTN p. 248)

COMPENSATED ABSENCES: unused vacation and other leave time for which employees will be paid when they retire or otherwise cease to work for a government

COMPONENT UNITS: legally separate organizations, often governmental, for which the elected officials of a primary government are financially responsible (Part 12, Figs. 91–93, BTN pp. 248, 282, and 283, UFR p. 283)

COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR): a government's official annual financial report, containing the **BASIC FINANCIAL STATEMENTS** as well as introductory material and additional statements and **STATISTICAL SECTION** schedules with financial, economic, and demographic information

CONCENTRATION OF CREDIT RISK: the risk of loss related to the magnitude of a government's investment in a single issuer (Part 5, Fig. 3)

CONDENSED FINANCIAL STATEMENTS: documents containing a substantially reduced set of information from another complete financial statement; governments may use them rather than **COMBINING STATEMENTS** to report **COMPONENT UNITS** (Fig. 93, BTN p. 248)

CONDUIT DEBT: debt issued by a government to provide capital financing for a third party that is not a part of the government; the third party, not the government, is responsible for repaying the debt through lease or loan payments to the government; examples include bonds issued to finance home mortgages and business expansion (Part 5)

CONTINGENT LIABILITIES: potential future liabilities based on conditions that were unresolved as of the date of the **FINANCIAL STATEMENTS**, such as pending court cases, disputed claims, and unfilled purchase orders (Part 5, UFR p. 121)

COPs: see **CERTIFICATES OF PARTICIPATION**

CORRECTIONS OF ERRORS: a type of **PRIOR-PERIOD ADJUSTMENT** to address mistakes made in the preparation of past years' **FINANCIAL STATEMENTS** (Part 13)

COST-SHARING MULTIPLE-EMPLOYER PLAN: a pooling or cost-sharing arrangement among multiple governments; the costs of providing pensions or **OTHER POSTEMPLOYMENT BENEFITS** to employees are shared by the plan as a whole, rather than attributed to the individual governments; see also **AGENT MULTIPLE-EMPLOYER PLAN** (Part 5, Fig. 29)

COVERAGE: a **FINANCIAL ANALYSIS** concept addressing a government's ability to repay **LONG-TERM DEBT** when payments are due (Parts 4 and 14)

COVERAGE RATIOS: types of **SOLVENCY RATIOS** used to determine a government's ability to repay long-term debts; examples include **INTEREST COVERAGE** and **DEBT SERVICE COVERAGE** (Part 14, UFR p. 320)

COVERED-EMPLOYEE PAYROLL: total employee pay (Part 6, Figs. 28–30 and E-3, BTN p. 127)

COVERED PAYROLL: the portion of employee pay on which contributions to a pension or **OTHER POSTEMPLOYMENT BENEFITS** plan are based (Part 6, Figs. 28–30 and E-3, BTN p. 127)

CREDIT RATING: a grade given by a private credit rating firm to a particular outstanding or pending issue of debt to assist investors and creditors in determining the likelihood that a government will be able to make the **INTEREST** and **PRINCIPAL** payments on time

CROSSOVER REFUNDING: a **DEBT REFUNDING** in which the proceeds of the refunding bonds are placed with an escrow agent and invested, but the regular debt service payments continue to be made from a revenue source for a time before ultimately being made from the proceeds in escrow (Part 5)

CURRENT ASSETS: cash and other assets expected or required to be converted to cash within a year that face no restrictions that would prevent a government from doing so (Part 4)

CURRENT FINANCIAL RESOURCES: MEASUREMENT FOCUS applied to the **GOVERNMENTAL FUNDS** to report on the flows of resources that occurred within or soon after a given year; it does not include **CAPITAL ASSETS** or **LONG-TERM DEBT** (Parts 2 and 9, UFR pp. 14 and 18)

CURRENT LIABILITIES: LIABILITIES that are due now or are expected to become due within a year, and that generally require the use of **CURRENT ASSETS** to satisfy them (Part 4)

CURRENT RATIO: a calculation to determine whether a government has enough liquid **ASSETS** to cover the **LIABILITIES** that are due now or are expected to come due in the next year; calculated as follows: **CURRENT ASSETS ÷ CURRENT LIABILITIES** (Part 14)

CURRENT REFUNDING: a **DEBT REFUNDING** in which the proceeds of the refunding bonds are used to immediately repay the outstanding bonds (Part 5)

CUSTODIAL CREDIT RISK: the risk of another party not returning a government's cash deposits or investments (Part 5, Fig. 2)

DAYS CASH ON HAND RATIO: a **FINANCIAL RATIO** that measures how much cash a government has available for covering operating costs (Part 14)

DAYS INVENTORY RATIO: a **FINANCIAL EFFICIENCY RATIO** that measures how long it takes a government to use its inventory (Part 14)

DAYS PAYABLE RATIO: a **FINANCIAL EFFICIENCY RATIO** that measures how long it takes a government to pay its bills (Part 14)

DAYS RECEIVABLE RATIO: a **FINANCIAL EFFICIENCY RATIO** that measures how long it takes a government to collect on its **ACCOUNTS RECEIVABLE** (Part 14)

DAYS UNPAID CLAIMS RATIO: a **FINANCIAL EFFICIENCY RATIO** that measures how long it takes a government to make payment on its **ACCOUNTS PAYABLE** (Part 14)

DEBT PER CAPITA: LONG-TERM DEBT divided by population (Part 14, Figs. 36 and 37)

DEBT REFUNDING: the sale of new bonds for the purpose of using the proceeds or other resources to repay existing debt, typically in order to lower annual **DEBT SERVICE** payments (Part 5, Fig. 17)

DEBT SERVICE: the payment of **INTEREST** and **PRINCIPAL** on amounts borrowed (Fig. 43)

DEBT SERVICE COVERAGE RATIO: a kind of **COVERAGE RATIO** used to determine a government's ability to pay **INTEREST** on and repay the **PRINCIPAL** of its **LONG-TERM DEBT** (Part 14, Fig. 40, KIM p. 151)

DEBT SERVICE FUND: a **GOVERNMENTAL FUND** to account for the payment of **INTEREST** and **PRINCIPAL** on **LONG-TERM DEBT** (Part 9, BTN p. 194)

DEDICATED TAXES: tax revenues legally limited to a particular purpose (BTN p. 162)

DEDUCTIONS: reductions in **FIDUCIARY NET POSITION,** primarily benefit payments and the costs of general administration (Part 10, Figs. 79, B-10, and C-9)

DEFEASANCE: a circumstance in which **LONG-TERM DEBT** has been satisfied either legally, based on the provisions of the original debt issuance, or in substance because the proceeds of a **DEBT REFUNDING** have been used to acquire qualified securities that have been placed with the escrow agent and are not available to the government (Part 5, Fig. 17, BTN p. 85)

DEFERRED INFLOWS OF RESOURCES: inflows of resources related to a future period (Part 4, UFR pp. 43, 102, and 103)

DEFERRED OUTFLOWS OF RESOURCES: outflows of resources related to a future period (Part 4, UFR pp. 43, 102, and 103)

DEFINED BENEFIT PLANS: pension or **OTHER POSTEMPLOYMENT BENEFITS** plans that, for accounting purposes, do not meet the definition of **DEFINED CONTRIBUTION PLANS;** a government guarantees a specific level of future benefits and then is obligated to provide sufficient resources to pay those benefits (Part 5)

DEFINED CONTRIBUTION PLANS: pension or **OTHER POSTEMPLOYMENT BENEFITS** plans in which a government promises to contribute a specific amount to each employee's individual account and the amount of benefits employees will receive when they retire depends only on how much was contributed and the earnings on those contributions when invested (Part 5)

DEPRECIATION EXPENSE: the systematic allocation of the **HISTORICAL COST** of a **CAPITAL ASSET,** less its **SALVAGE VALUE,** over its **USEFUL LIFE;** it is a proxy for the cost of using a capital asset in the operations of a government or for the gradual wearing out of a capital asset over time (Parts 2 and 4, Fig. 12, TOT p. 26)

DERIVATIVE: a financial instrument or a transaction that a government enters into that is based on some other instrument or agreement, such as an investment or outstanding debt; the value of the derivative is predicated on the performance of the underlying instrument or agreement (Part 5, Figs. 19–21, BTN p. 96)

DERIVED TAX REVENUES: a **NONEXCHANGE TRANSACTION** resulting from taxing a separate **EXCHANGE TRANSACTION,** such as sales tax on a purchase of a car (Part 2, BTN p. 16)

DISBURSEMENTS: outflows of cash, such as when employees are paid

DISCRETELY PRESENTED COMPONENT UNITS: COMPONENT UNITS that are reported separately from the **PRIMARY GOVERNMENT,** as opposed to **BLENDED COMPONENT UNITS** (Part 12, UFR p. 283)

DUE FROM OTHER GOVERNMENTS: amounts a government is owed by other governments; a type of **ASSET**

ECONOMIC CONDITION: a composite of a government's **FINANCIAL POSITION, FISCAL CAPACITY,** and **SERVICE CAPACITY** (Part 14)

ECONOMIC RESOURCES: MEASUREMENT FOCUS applied to all governmental accounting and financial reporting except for the **GOVERNMENTAL FUNDS,** it includes all of the resources of a government, both capital and financial, current and long-term (Part 2, UFR pp. 14 and 18)

EFFECTIVENESS: the degree to which a government achieves its objectives through the provision of services (Part 14)

ENABLING LEGISLATION: a statute or ordinance that creates a revenue source and imposes a legal restriction that the **REVENUE** can be used only for a specific purpose (Parts 4 and 5)

ENCUMBRANCES: amounts set aside to pay for goods and services a government contracted for but did not receive prior to the end of the year

ENTERPRISE FUND: a type of **PROPRIETARY FUND** used to account for a government's **BUSINESS-TYPE ACTIVITIES** (Part 10, Figs. 68–70, BTN p. 236)

ESTIMATED ACTUAL VALUE OF TAXABLE PROPERTY: the **FAIR VALUE** of taxable real or personal property or a surrogate measure if actual fair value information is not available; often referred to as market value (Parts 6 and 8, Figs. 37 and 48, KIM pp. 189 and 191)

ESTIMATED TOTAL CURRENT COST: the cost today for a government to perform the actions that are legally required for closing a municipal landfill and caring for it after its closure (Parts 5 and 8, Fig. 45)

EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES: the difference between **REVENUES** and **EXPENDITURES**; more simply, surplus (deficit) (Part 9, Fig. 54)

EXCHANGE TRANSACTIONS: transactions in which an equal exchange of value takes place between two willing parties; distinguished from **NONEXCHANGE TRANSACTIONS**

EXPENDITURES: the outflow of cash, a promise to pay, or other financial resources in return for goods and services that have been received (Part 9, Fig. 54)

EXPENSE: a decrease in **NET POSITION** resulting from the using up or outflows of **ASSETS** in the course of operating a government and providing goods and services; expenses also result from reductions in accumulated **DEFERRED OUTFLOWS OF RESOURCES** with the passage of time (Part 7, Fig. 42)

EXTERNAL INVESTMENT POOL: an arrangement external to the **REPORTING ENTITY** in which governments pool their resources to invest in a single portfolio to benefit the individual participating governments (Part 5)

EXTRAORDINARY ITEMS: CHANGE IN NET POSITION or **CHANGE IN FUND BALANCE** that is both unusual in nature and infrequent in occurrence; they are reported separately from **REVENUES** and **EXPENSES/EXPENDITURES** (Part 7)

FAIR VALUE: the amount that would be received if an asset were sold or the amount that would be paid to transfer a liability between a willing seller and a willing buyer in an active market (Part 5, Fig. 3)

FIDUCIARY ACTIVITIES: activities in which a government acts as trustee or agent for resources that belong to others, such as employee pension plans; these activities are not included in the **GOVERNMENT-WIDE STATEMENTS** because their resources do not belong to the government and are not available to be used (Part 10, Figs. 78 and 79)

FIDUCIARY FUNDS: funds used to account for **FIDUCIARY ACTIVITIES**; they employ the **ECONOMIC RESOURCES MEASUREMENT FOCUS** and **ACCRUAL BASIS OF ACCOUNTING**; classes of fiduciary funds include **PENSION (AND OTHER EMPLOYEE BENEFIT) TRUST FUND, INVESTMENT TRUST FUND, PRIVATE-PURPOSE TRUST FUND,** and **AGENCY FUND** (Part 10, Figs. 78–82, BTN p. 257, UFR p. 264)

FIDUCIARY NET POSITION: the **NET POSITION** of a pension or **OTHER POSTEMPLOYMENT BENEFITS** plan that is dedicated to providing benefits to the members of the plan; when subtracted from the **TOTAL PENSION LIABILITY,** the remainder is the **NET PENSION LIABILITY** (Parts 4 and 5, Figs. 78–82, B-10, B-11, C-9, and C-10)

FINAL BUDGET: the budget that reflects all legal changes made to the **ORIGINAL BUDGET** subsequent to the start of the year (even those that occur after the end of the year) (Part 9, Figs. 60–62)

FINANCIAL ANALYSIS: the examination and processing of financial statements and other relevant information to draw conclusions about a government's financial health upon which decisions may be based (Part 14)

FINANCIAL CONDITION: see **ECONOMIC CONDITION**

FINANCIAL EFFICIENCY RATIOS: calculations to determine how well a government uses its **ASSETS** and **LIABILITIES** (Part 14)

FINANCIAL POSITION: the status of a government's **ASSETS, DEFERRED OUTFLOWS OF RESOURCES, LIABILITIES, DEFERRED INFLOWS OF RESOURCES,** and **NET POSITION** at a given point in time (Parts 4 and 14)

FINANCIAL RATIOS: numbers calculated from information in **FINANCIAL STATEMENTS** for the purpose of conducting **FINANCIAL ANALYSIS** (Part 14)

FINANCIAL SECTION: the portion of the **CAFR** containing the **BASIC FINANCIAL STATEMENTS** and other supporting **FINANCIAL STATEMENTS** and schedules

FINANCIAL STATEMENTS: documents prepared by a government for the purpose of reporting its finances to the public (Part 2)

FINES RECEIVABLE: fine payments owed to a government; they are **ASSETS**

FISCAL CAPACITY: a government's ability and willingness to meet its financial obligations on an ongoing basis; see **ECONOMIC CONDITION** (Part 14)

FISCAL FUNDING CLAUSES: provisions of lease contracts that allow a government to cancel the lease on an annual basis if funds are not appropriated in the budget to make the lease payments (Part 5)

FISCAL YEAR: the typical period covered by a government's **FINANCIAL STATEMENTS**

FIXED-RATE DEBT: debt that carries an unchanging interest rate until its **MATURITY;** see **VARIABLE-RATE DEBT**

FOREIGN CURRENCY RISK: the risk of loss from changes in exchange rates (Part 5)

FORWARD CONTRACTS: a type of **DERIVATIVE** in which a government agrees to purchase or sell an asset in the future at an agreed-upon price (Part 5)

FRINGE BENEFITS: nonsalary compensation for employees, such as pension contributions and health and life insurance premiums

FULL ACCRUAL: see **ACCRUAL**

FUND BALANCE: the difference between **ASSETS, DEFERRED OUTFLOWS OF RESOURCES, LIABILITIES,** and **DEFERRED INFLOWS OF RESOURCES** in the **GOVERNMENTAL FUNDS**; at present, however, accounting standards do not require reporting of deferred inflows and outflows in the governmental funds (Part 9, Figs. 53 and 65)

FUND FINANCIAL STATEMENTS: statements reporting the finances of a government's **GOVERNMENTAL FUNDS, PROPRIETARY FUNDS,** and **FIDUCIARY FUNDS** (Parts 9 and 10, BTN p. 11)

FUNDS: fiscal and accounting entities created by a government for the purpose of tracking the finances of a particular activity or group of activities

GAAP: see **GENERALLY ACCEPTED ACCOUNTING PRINCIPLES**

GANs: see **GRANT ANTICIPATION NOTES**

GARVEEs: see **GRANT ANTICIPATION REVENUE VEHICLES**

GASB: see **GOVERNMENTAL ACCOUNTING STANDARDS BOARD**

GENERAL FUND: accounts for all activities not reported in the other **GOVERNMENTAL FUNDS** (Part 9, BTN p. 194)

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP): the body of standards promulgated by the **GASB** and its predecessors that govern how state and local governments account for and report their finances externally (Parts 1 and 2)

GENERAL OBLIGATION (GO) DEBT: debt issued by a government (generally long-term **BONDS**) that typically is secured by the full faith and credit of the government—meaning all of its taxing and revenue-raising capability (Figs. 36–39)

GENERAL PURPOSE GOVERNMENTS: governments that provide a variety of services and generally are supported with taxes, such as states, counties, and cities

GENERAL REVENUES: all revenues that are not **PROGRAM REVENUES**; most commonly, taxes (Part 7, Fig. 42)

GO: see **GENERAL OBLIGATION (GO) DEBT**

GOING CONCERN: the concept that a government will be capable of operating and meeting its financial obligations over the course of the 15 months following the date of the financial statements (Part 13)

GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB): the organization that is recognized by the accounting industry as the setter of **GENERALLY ACCEPTED ACCOUNTING PRINCIPLES** for state and local governments (App. G)

GOVERNMENTAL ACTIVITIES: activities generally financed with taxes and unrestricted **INTERGOVERNMENTAL AID** and reported in the **GOVERNMENTAL FUNDS** and **INTERNAL SERVICE FUNDS,** as well as the **GOVERNMENT-WIDE FINANCIAL STATEMENTS** (Parts 4–9, BTN p. 193)

GOVERNMENTAL FUNDS: these funds track the finances of a government's basic services and collectively are virtually synonymous with the **GOVERNMENTAL ACTIVITIES** reported in the **GOVERNMENT-WIDE FINANCIAL STATEMENTS**; they are reported using the **CURRENT FINANCIAL RESOURCES MEASUREMENT FOCUS** and **MODIFIED**

ACCRUAL BASIS OF ACCOUNTING, and include the GENERAL FUND, SPECIAL REVENUE FUND, DEBT SERVICE FUND, CAPITAL PROJECTS FUND, and PERMANENT FUND (Part 9, UFR p. 14, BTN pp. 11, 193, and 194)

GOVERNMENT-MANDATED NONEXCHANGE TRANSACTION: a NONEXCHANGE TRANSACTION, such as a CATEGORICAL GRANT, in which one government provides resources to another government and requires that the resources be used for a particular purpose (Part 2, BTN p. 16)

GOVERNMENT-WIDE FINANCIAL STATEMENTS: statements covering all of a government's activities (except FIDUCIARY ACTIVITIES); they are prepared using the ECONOMIC RESOURCES MEASUREMENT FOCUS and ACCRUAL BASIS OF ACCOUNTING; they are the first to appear among the BASIC FINANCIAL STATEMENTS and include the STATEMENT OF NET POSITION and STATEMENT OF ACTIVITIES (Parts 4–8, Figs. 1 and 42, BTN p. 11)

GRANT ANTICIPATION NOTES (GANs): a type of NOTE issued in advance of the receipt of proceeds from a grant; it is repaid with a portion of the grant (BTN p. 80)

GRANT ANTICIPATION REVENUE VEHICLES (GARVEEs): a type of NOTE issued in advance of receiving federal transportation aid; it is repaid with the grant when received (BTN p. 80)

HEDGING DERIVATIVE INSTRUMENT: a DERIVATIVE that significantly reduces financial risk by substantially offsetting the changes in cash flows or fair values of the item the derivative is associated with; the changes in their fair value are deferred, rather than included in investment income, until they cease to be effective, are terminated, or otherwise end (Part 5, Figs. 19–21, BTN p. 96)

HISTORICAL COST: the original construction cost or acquisition price of a CAPITAL ASSET; it is reported in a STATEMENT OF NET POSITION, less ACCUMULATED DEPRECIATION (Parts 2 and 4, TOT p. 26)

IMPAIRMENT: a substantial and unexpected reduction in the SERVICE CAPACITY of a CAPITAL ASSET (Part 5)

IMPOSED NONEXCHANGE TRANSACTION: a NONEXCHANGE TRANSACTION in which taxes are levied, other than DERIVED TAX REVENUES (Part 2, BTN p. 16)

INFRASTRUCTURE: especially long-lasting CAPITAL ASSETS that are stationary, can be preserved for significantly greater periods than most capital assets, and typically are part of a larger system of capital assets; examples include bridges, tunnels, roads, water mains, and sewers (Part 4, Figs. 12, 32, and 35)

INPUTS: money, labor, CAPITAL ASSETS, and other resources used to provide services (Part 14)

INSURANCE-PURCHASING POOL: a type of PUBLIC ENTITY RISK POOL in which governments combine resources to purchase commercial insurance (Parts 5 and 6, BTN p. 114)

INTANGIBLE ASSET: a type of CAPITAL ASSET without physical form, such as patents, computer software, easements, and rights to use the assets of another entity

INTEREST: the cost of using borrowed money; it typically is a percentage of PRINCIPAL

INTEREST COVERAGE RATIO: a kind of COVERAGE RATIO used to determine a government's ability to pay future INTEREST payments on its LONG-TERM DEBT (Part 14, KIM p. 151)

INTEREST RATE RISK: the risk that changing interest rates will lead to a decline in the fair value of an investment (Part 5, Figs. 3 and 5–7)

INTEREST RATE SWAP: a type of **DERIVATIVE** in which a government essentially turns **VARIABLE-RATE DEBT** into **FIXED-RATE DEBT** by agreeing to make equal payments to another party in return for payments equal to the government's payments on the variable-rate debt (Part 5)

INTEREST RECEIVABLE: interest payments owed to a government

INTERFUND BALANCES: amounts owed from one **FUND** to another at the end of the **FISCAL YEAR** (Part 9, Fig. 56)

INTERFUND ELIMINATIONS: adjustments made when converting individual **FUND** information to government-wide data to avoid counting twice the effect of transfers or other movements of resources among funds

INTERFUND TRANSFERS: amounts moved from one **FUND** to another during the **FISCAL YEAR** (Part 9, Fig. 57)

INTERGOVERNMENTAL AID: grants to or from other governments; for local governments, they typically come from the state and federal governments; see **CAPITAL GRANTS AND CONTRIBUTIONS** and **OPERATING GRANTS AND CONTRIBUTIONS**

INTERNAL SERVICE FUNDS: a type of **PROPRIETARY FUND** that tracks the activities that provide goods or services to the other agencies or programs of a government; generally included with the **GOVERNMENTAL ACTIVITIES** in the **GOVERNMENT-WIDE FINANCIAL STATEMENTS** (Part 10, Figs. 68–70 and 75–77, BTN p. 236)

INTERPERIOD EQUITY: the degree to which a government raises sufficient resources in a year to cover its costs (Part 4)

INTRODUCTORY SECTION: the first part of the **CAFR**, it contains the **LETTER OF TRANSMITTAL**, organizational charts, and other general information about a government (Part 3)

INVESTING CASH FLOWS: the exchange of cash related to the buying and selling of investments, as well as investment earnings (Part 10, Fig. 70)

INVESTMENT TRUST FUND: a category of **FIDUCIARY FUND** to track the portion of a government's investment pools that belongs to other governments (Part 10, BTN p. 257)

JOINTLY GOVERNED ORGANIZATION: a separate governmental entity created by other governments to provide services to their citizens; the governments share control of the entity but, unlike a **JOINT VENTURE**, do not retain an ongoing financial interest in or responsibility for it (Part 12)

JOINT VENTURE: a separate governmental entity created by other governments to provide services to their citizens; the governments share control of the entity and retain an ongoing financial interest in or responsibility for it, unlike a **JOINTLY GOVERNED ORGANIZATION** (Part 12)

LEGAL DEBT LIMIT: the total amount of a particular type of debt, typically **GENERAL OBLIGATION**, that a government is legally allowed to issue (Part 6, Fig. 39)

LEGAL DEBT MARGIN: the amount of a particular type of debt, typically **GENERAL OBLIGATION DEBT**, that a government is legally allowed to issue before reaching its **LEGAL DEBT LIMIT**; it generally is the difference between a government's legal debt limit and the amount of that particular debt currently outstanding (Part 6, Fig. 39)

LETTER OF TRANSMITTAL: a welcoming message to the user of the **CAFR**, presented in the **INTRODUCTORY SECTION**, from a government's executive—the mayor, city manager, or equivalent position—or chief financial officer; it may include information not found in **MD&A**, such as indicators of service performance (Part 3)

LEVERAGE: a **FINANCIAL ANALYSIS** concept addressing the degree to which a government's **ASSETS** are financed with **LONG-TERM DEBT** and other **NONCURRENT LIABILITIES** (Parts 4 and 14)

LEVERAGE RATIOS: calculations to determine the degree to which a government's **ASSETS** are financed through borrowing and other long-term obligations (Part 14)

LIABILITIES: amounts a government is obligated to pay to persons and groups outside the government

LIABILITIES-TO-ASSETS RATIO: a **LEVERAGE RATIO** calculated as follows: **LIABILITIES** ÷ **ASSETS** (Part 14)

LIABILITIES-TO-NET POSITION RATIO: a **LEVERAGE RATIO** calculated as follows: **LIABILITIES** ÷ **NET POSITION** (Part 14)

LIQUIDITY: how quickly an **ASSET** can be exchanged for cash or is expected to be used up, taking into account any restrictions as to when the asset can be used (Parts 4 and 14, KIM p. 318)

LIQUIDITY RATIOS: calculations to determine a government's ability to pay for its most immediate obligations (Part 14)

LONG-TERM DEBT: borrowing that is expected to be repaid over several years to several decades, typically through loans or the sale of **BONDS** (Parts 4–6, Figs. 16–18 and 36–40)

MAJOR FUNDS: a government's most significant **GOVERNMENTAL FUNDS** and **ENTERPRISE FUNDS**, based on specific size criteria; the **GENERAL FUND** always is considered major, and governments can designate other important funds as well; they are displayed individually on the **GOVERNMENTAL FUNDS FINANCIAL STATEMENTS** and **PROPRIETARY FUNDS FINANCIAL STATEMENTS** (Parts 9 and 10, Fig. E-4)

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A): an overview and analysis, prepared by a government's finance officers, of the information in the government's **FINANCIAL STATEMENTS**; it is a form of **RSI**, although it appears before the **BASIC FINANCIAL STATEMENTS** (Part 3 and App. A, KIM p. 31, UFR p. 32)

MARKET-ACCESS RISK: the chance that a government will not be able to issue debt or that doing so will become more expensive (Part 5, Fig. 21)

MATURITY: refers to when (1) a liability is due to be settled or (2) an investment is due to pay off (Parts 4 and 5)

MD&A: see **MANAGEMENT'S DISCUSSION AND ANALYSIS**

MEASUREMENT DATE: the date on which a government measures its **TOTAL PENSION LIABILITY** or **TOTAL OPEB LIABILITY**; the measurement date may be as early as the last day of the prior fiscal year (Part 5)

MEASUREMENT FOCUS: the definition of the kinds of transactions a government should consider when accounting for and reporting its finances (Part 2, UFR pp. 14 and 18)

MINIMUM FUND BALANCE POLICY: a policy mandating that a government end each **FISCAL YEAR** with at least a certain amount of **FUND BALANCE** (Part 9)

MODIFIED ACCRUAL: the **BASIS OF ACCOUNTING** a government uses to account for its **GOVERNMENTAL FUNDS**; it records **EXPENDITURES** rather than **EXPENSES**, and requires that payment on **REVENUES** be received during the year or soon enough thereafter to be used to liquidate the current year's **LIABILITIES** (Parts 2 and 9, UFR pp. 14 and 18)

MODIFIED APPROACH: an alternative method to **DEPRECIATION** for reporting certain general **INFRASTRUCTURE** assets; it involves reporting annual maintenance and preservation **EXPENSES** for assets that a government can show are kept at a predetermined level of physical condition chosen by the government (Parts 4 and 6, Fig. 32, BTN p. 41)

MONEY MARKET INVESTMENTS: short-term investments that are easily converted to cash, such as certain U.S. Treasury debt (Part 5)

NET ASSETS: the difference between **ASSETS** and **LIABILITIES** on an **ACCRUAL** basis of accounting (UFR p. 44)

NET COST: the portion of the cost of providing services—after deducting revenues from **USER FEES** and **CATEGORICAL GRANTS** or donations—that is financed by **GENERAL REVENUES** such as taxes; also called **NET EXPENSE** (Part 7, Fig. 42)

NET (EXPENSE) REVENUE: the remainder after **PROGRAM REVENUES** are subtracted from **EXPENSES**; a functional expense category with a positive number provides net revenue to the government; a functional expense category with a negative number places a net expense on the government that generally is financed with taxes and other **GENERAL REVENUES**; this information is found in the government-wide **STATEMENT OF ACTIVITIES**; see also **NET COST** (Part 7, Fig. 42)

NET INVESTMENT IN CAPITAL ASSETS: the portion of **NET POSITION** represented by **CAPITAL ASSETS** less **ACCUMULATED DEPRECIATION**, less outstanding debts incurred by a government to buy or construct them (Part 4, Fig. 1)

NET OPEB LIABILITY (NOL): the portion of a government's obligation to provide **OTHER POSTEMPLOYMENT BENEFITS** to active and inactive employees and their beneficiaries that is not covered by resources set aside in an **OPEB** trust; it is calculated as follows: **TOTAL OPEB LIABILITY** minus **FIDUCIARY NET POSITION** (Parts 4 and 5)

NET OPEB OBLIGATION: under prior accounting standards, the cumulative difference between actuarially determined contributions to an **OTHER POSTEMPLOYMENT BENEFITS** plan and a government's actual contributions (Part 4, UFR p. 110)

NET PENSION LIABILITY (NPL): the portion of a government's obligation to provide pensions to active and inactive employees and their beneficiaries that is not covered by resources set aside in a pension trust; it is calculated as follows: **TOTAL PENSION LIABILITY** minus **FIDUCIARY NET POSITION** (Parts 4 and 5)

NET POSITION: what remains after **LIABILITIES** and **DEFERRED INFLOWS OF RESOURCES** have been subtracted from **ASSETS** and **DEFERRED OUTFLOWS OF RESOURCES** (Part 4, UFR p. 45)

NETWORK SUBSYSTEM: a portion of an **ASSET NETWORK** of **CAPITAL ASSETS**, such as secondary roadways within a state highway system (Part 5, BTN p. 41)

NOL: see **NET OPEB LIABILITY**

NONCANCELABLE OPERATING LEASES: lease contracts that do not meet the criteria to be considered a **CAPITAL LEASE** and which cannot be terminated unilaterally by the government (Part 8, Fig. 44)

NONCAPITAL FINANCING CASH FLOWS: the exchange of cash related to borrowing for purposes other than purchasing, constructing, or rehabilitating **CAPITAL ASSETS** (Part 10, Fig. 70)

NONCURRENT ASSETS: ASSETS that will be liquidated beyond the coming year, if at all, or that are restricted from being liquidated in the current year (Part 4)

NONCURRENT LIABILITIES: LIABILITIES that come due beyond the coming year (Part 4)

NONEMPLOYER CONTRIBUTING ENTITY: a government or other entity that makes contributions to a pension or **OTHER POSTEMPLOYMENT BENEFITS** plan that is used to provide benefits to the employees of other governments (Part 4, UFR p. 100)

NONEXCHANGE FINANCIAL GUARANTEE: TRANSACTION in which a government provides or receives a guarantee of a financial obligation in return for little or no payment (Part 5, Fig. 27)

NONEXCHANGE TRANSACTION: transaction in which there is an unequal exchange of resources or one of the parties is not a willing participant (Part 2, BTN p. 16)

NONMAJOR FUNDS: FUNDS that do not qualify as **MAJOR FUNDS** (Parts 9 and 10, Figs. 63, 64, 72–74, and E-4)

NONSPENDABLE FUND BALANCE: the portion of **FUND BALANCE** that represents resources that cannot be spent, because they either are not in spendable form or are required by an external individual or organization to be maintained intact (Part 9, Fig. 53)

NOTES: a form of debt issued by governments that is typically repaid within one year; they are commonly used to even out cash flows over the course of a year (BTN, pp. 80 and 196)

NOTES TO FINANCIAL STATEMENTS: note disclosures provide additional information that is essential for **FINANCIAL STATEMENTS** to present fairly the finances of a government; they are considered a component of the **BASIC FINANCIAL STATEMENTS** and therefore are essential to a user's understanding of financial position and the inflows and outflows of resources (Parts 2, 5, and 8–13, BTN p. 21, KIM pp. 23 and 24)

NOTIONAL AMOUNT: the amount—stated in dollars, gallons, shares, and so on—specified in a **DERIVATIVE;** like bond principal, it is the amount upon which payments depend (Part 5, Fig. 19)

NPL: see **NET PENSION LIABILITY**

ON-BEHALF PAYMENTS: direct payments made by a government to a third party, or payments received from another government for the **FRINGE BENEFITS** and salaries of employees of another, legally separate organization or government (Part 8)

OPEB: see **OTHER POSTEMPLOYMENT BENEFITS**

OPERATING CASH FLOWS: the exchange of cash related to a government's provision of services and the production and provision of goods (Part 10, Fig. 70)

OPERATING EXPENSES: the costs of producing and providing goods and services to customers and of collecting payment from them (Part 10, BTN pp. 35 and 169, Fig. 69)

OPERATING GRANTS AND CONTRIBUTIONS: INTERGOVERNMENTAL AID and donations received or provided to finance operating activities (Part 7, Fig. 42)

OPERATING LEASES: lease contracts that do not meet the criteria to be considered a **CAPITAL LEASE** (Parts 5 and 8, Fig. 44)

OPERATING REVENUES: fees and charges generated by a **BTA's** production and provision of goods and services to customers (Part 10, BTN pp. 35 and 169, Fig. 69)

OPTIONS: a type of **DERIVATIVE** that conveys the right to buy or sell an asset at a particular price, by a specific date in the future (Part 5)

ORIGINAL BUDGET: the first legally adopted budget for a given year, including any legal adjustments made to it subsequent to adoption but prior to the start of the year (Part 9, Figs. 60 and 61)

OTHER FINANCING SOURCES: inflows of resources other than **REVENUES** in the **GOVERNMENTAL FUNDS** that increase **FUND BALANCES;** an example is proceeds from **LONG-TERM DEBT** (Part 9, Fig. 54)

OTHER FINANCING USES: outflows of resources other than **EXPENDITURES** in the **GOVERNMENTAL FUNDS** that reduce **FUND BALANCES;** an example is **TRANSFERS** to another fund (Part 9, Fig. 54)

OTHER POSTEMPLOYMENT BENEFITS (OPEB): retirement benefits other than pensions, most notably retiree health insurance (Parts 5 and 6)

OUTCOMES: the results of services provided—what is accomplished—by a government (Part 14)

OUTPUTS: the amount of service provided by a government (Part 14)

OVERALL CREDIT RISK: the risk that an issuer of or counterparty to an investment will not fulfill its obligations (Part 5, Fig. 3)

OVERLAPPING DEBT: a proportion of the outstanding **LONG-TERM DEBT** of other governments that at least partially overlap geographically with the reporting government (Part 6, Fig. 38, BTN p. 146)

OVERLAPPING RATES: tax (or revenue) rates applied to a government's tax (or revenue) base by other governments that at least partially overlap geographically (Part 6, Fig. 49, BTN p. 187)

OWN-SOURCE REVENUES: revenues that are generated by a government itself, such as tax revenues and water and sewer charges; **INTERGOVERNMENTAL AID** and shared revenues are not own-source revenues (Part 8, Figs. 48–52)

PAYABLES: see **ACCOUNTS PAYABLE**

PAYABLES EFFICIENCY RATIO: a **FINANCIAL EFFICIENCY RATIO** that measures how long it takes a government to pay amounts it owes; it is calculated as follows: **PAYABLES** ÷ **EXPENSES** (Part 14)

PAYABLES TURNOVER RATIO: a **FINANCIAL EFFICIENCY RATIO** that measures how long it takes a government to pay amounts it owes; it is calculated as follows: **EXPENSES** ÷ average **PAYABLES** (Part 14)

PENSION (AND OTHER EMPLOYEE BENEFIT) TRUST FUND: a category of **FIDUCIARY FUND** to account for resources held in trust for the members and beneficiaries of employee benefit plans (Part 10, BTN p. 257)

PERCENTAGE CHANGE: a **COMMON-SIZE RATIO** that shows the magnitude of change over time; it is calculated as follows: (most recent year − earlier year) ÷ earlier year (Part 14, Fig. 100)

PERCENTAGE DISTRIBUTION: a **COMMON-SIZE RATIO** for determining the proportions that individual elements represent of a total; it is calculated as follows: individual element ÷ total (Part 14, Fig. 101, UFR p. 310)

PERIOD OF AVAILABILITY: under the **MODIFIED ACCRUAL BASIS OF ACCOUNTING,** the period following the end of the fiscal year when collected **REVENUES** are considered available to pay current-year **LIABILITIES** (Part 2)

PERMANENT FUND: a **GOVERNMENTAL FUND** for reporting resources legally **RESTRICTED** so that only the earnings they generate, and not the resources themselves, may be used to finance operations (Part 9, BTN p. 194)

PLEDGED-REVENUE DEBT: non-**GENERAL OBLIGATION DEBT** that is secured by a pledge of a specific revenue stream (Part 6, Fig. 40)

PREMIUM DEFICIENCY: occurs when the cumulative costs a **PUBLIC ENTITY RISK POOL** expects to have are greater than the premiums that are expected to be received (Part 5)

PRIMARY GOVERNMENT: a state or general purpose local government and all organizations that are legally a part of it; a **SPECIAL-PURPOSE GOVERNMENT** that has a separately elected governing body and is legally separate from and financially independent of other governments also is a primary government (Part 2)

PRINCIPAL: the original amount borrowed via a mortgage, **BONDS, NOTES,** or other debt instrument; or original amounts invested by a government

PRIOR-PERIOD ADJUSTMENTS: changes made to the information in a previous year's **FINANCIAL STATEMENTS** to address **CORRECTIONS OF ERRORS, CHANGES IN ACCOUNTING PRINCIPLE,** or **CHANGES IN THE REPORTING ENTITY** (Part 13)

PRIVATE-PURPOSE TRUST FUND: a category of **FIDUCIARY FUND** to report all trust arrangements not reported in another kind of fiduciary fund (Part 10, BTN p. 257)

PROGRAM REVENUES: REVENUES produced by an activity's fees and charges or received as operating or **CAPITAL GRANTS** specifically for that activity (Part 7, Fig. 42)

PROPRIETARY FUNDS: funds that track a government's activities that charge customers a fee in return for goods or services; there are two kinds—**ENTERPRISE FUNDS** and **INTERNAL SERVICE FUNDS** (Part 10, Figs. 68–70, BTN p. 236)

PUBLIC AUTHORITY: a legally separate organization established in accordance with statutory provisions by a government to provide particular goods or services; typically reported as a **COMPONENT UNIT** of a **PRIMARY GOVERNMENT**

PUBLIC BENEFIT CORPORATION: see **PUBLIC AUTHORITY**

PUBLIC ENTITY RISK POOL: an arrangement by which multiple governments join together to finance activities that involve risk or a liability, such as providing health or life insurance to employees (Parts 5 and 6, Figs. 26, 33, and 34, BTN pp. 114 and 135)

PUT: an OPTION that gives a bondholder the right to demand payment at a particular point in time prior to the ultimate MATURITY of a bond (Part 5)

QUICK RATIO: a LIQUIDITY RATIO calculated as follows: (cash + current investments) ÷ CURRENT LIABILITIES (Part 14)

RAINY-DAY FUNDS: see STABILIZATION ARRANGEMENTS

RANs: see REVENUE ANTICIPATION NOTES

RECEIPTS: inflows of cash, such as the collection of tax payments from homeowners and businesses

RECEIVABLES: see ACCOUNTS RECEIVABLE

RECEIVABLES EFFICIENCY RATIO: a FINANCIAL EFFICIENCY RATIO that measures how long it takes a government to collect amounts owed to it; it is calculated as follows: receivables ÷ REVENUES (Part 14)

RECEIVABLES TURNOVER RATIO: a FINANCIAL EFFICIENCY RATIO that measures how long it takes a government to collect amounts owed to it; it is calculated as follows: REVENUES ÷ average receivables (Part 14)

RECOGNIZED SUBSEQUENT EVENTS: SUBSEQUENT EVENT related to conditions that existed as of the date of the financial statements (Part 13)

RECONCILIATION: schedule to FINANCIAL STATEMENTS that present the adjustments necessary to explain how the BASIS OF ACCOUNTING differs in two sets of statements; governments prepare reconciliations between the GOVERNMENT-WIDE STATEMENTS and GOVERNMENTAL FUNDS STATEMENTS, the enterprise funds STATEMENT OF CASH FLOWS and STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION, and the actual budgetary results and governmental funds STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES (Parts 9 and 10, Figs. 53, 55, 58, 59, 62, 70, B-4, B-6, and C-5)

RECONCILIATION OF CLAIMS LIABILITIES BY CONTRACT: an RSI schedule that presents information about the UNPAID CLAIMS LIABILITIES of a PUBLIC ENTITY RISK POOL (Part 6, Fig. 33)

RELATED ORGANIZATION: an organization in which the majority of its board is appointed by a government, but for which the government is not financially accountable (Part 12)

REPORTING ENTITY: the scope of a government that is covered by the financial statements; it includes GOVERNMENTAL ACTIVITIES, BTAs, and DISCRETELY PRESENTED COMPONENT UNITS (Parts 12 and 13)

REPURCHASE AGREEMENT: an investment in which a government provides cash to an investment firm or other financial institution and receives bonds, stocks, or other securities in exchange, along with a promise that the firm will repay the cash with interest in exchange for the return of the securities; see REVERSE REPURCHASE AGREEMENT (Part 5)

REQUIRED SUPPLEMENTARY INFORMATION (RSI): important additional information that supports and explains the data in the BASIC FINANCIAL STATEMENTS; RSI is not a part of the BFS, but governments are required

by the GASB to provide it together with them; RSI materials follow the NOTES TO FINANCIAL STATEMENTS, with the exception of MD&A, which precedes the BFS (Parts 2, 6, and 8–13, KIM p. 24)

RESTRICTED FUND BALANCE: FUND BALANCE restricted to a particular purpose by organizations or persons external to a government (Part 9, Fig. 53, UFR p. 45)

RESTRICTED NET POSITION: NET POSITION restricted to a particular purpose by organizations or persons external to a government (Part 4, Fig. 1, UFR p. 45)

REVENUE: under the ECONOMIC RESOURCES MEASUREMENT FOCUS, increases in NET POSITION connected with growth in ASSETS as a result of providing goods and services; under the CURRENT FINANCIAL RESOURCES MEASUREMENT FOCUS, inflows of current financial resources that are available during the year or shortly thereafter to cover EXPENDITURES; revenues also result from reductions in accumulated DEFERRED INFLOWS OF RESOURCES with the passage of time (Parts 7 and 9, BTN p. 164)

REVENUE ANTICIPATION NOTES (RANs): a type of NOTE issued in advance of receiving payments of nontax revenues (BTN p. 80)

REVENUE-BACKED DEBT: LONG-TERM DEBT issued by a government that is repaid with resources generated by the activity the debt is financing; for example, a municipal hospital might repay bonds with patient service revenues (Parts 6 and 14, Figs. 36 and 40)

REVENUE DISPERSION: the degree to which a government's REVENUES come from a few sources versus a wide variety of sources (Parts 7 and 14)

REVERSE REPURCHASE AGREEMENT: an investment in which a government provides bonds, stocks, or other securities to an investment firm or other financial institution in exchange for cash, and promises to repay the cash with interest to the firm in exchange for the return of the securities; see REPURCHASE AGREEMENT (Part 5, Fig. 8)

RISK EXPOSURE RATIO: a measure of the property tax increase necessary to cover a 1 percent decrease in INTERGOVERNMENTAL AID and investment income (Part 14)

RISK-SHARING POOL: a type of PUBLIC ENTITY RISK POOL in which governments pool their risk and share the costs of losses by contributing to a central account from which losses are paid (Parts 5 and 6, BTN p. 114)

ROLLOVER RISK: the risk of losing protection from loss of fair value or cash flows because a DERIVATIVE does not last as long as its associated debt is outstanding; after the derivative ends, the government no longer is protected against rising interest rates and may not be able to enter into a new derivative with similar terms (Part 5, Fig. 21)

RSI: see REQUIRED SUPPLEMENTARY INFORMATION

SALVAGE VALUE: theoretically, the value of a CAPITAL ASSET at the end of its USEFUL LIFE; it is subtracted before HISTORICAL COST is allocated over the useful life in DEPRECIATION; also called residual value (Part 2, TOT p. 26)

SCA: see SERVICE CONCESSION ARRANGEMENT

SCHEDULE OF EMPLOYER CONTRIBUTIONS: an **RSI** document comparing (1) a government's actual contribution to its pension or **OTHER POSTEMPLOYMENT BENEFITS** plan with (2) the contribution an actuary calculated it should make or that it was required to make based on statute or contract (Part 6, Figs. 30 and E-3)

SEA: see **SERVICE EFFORTS AND ACCOMPLISHMENTS INFORMATION**

SECURITIES LENDING: a transaction that involves a government transferring securities to a financial firm or other party in exchange for collateral (which may be cash, securities, or letters of credit), while simultaneously agreeing to return the collateral for the same securities in the future; it differs from a **REVERSE REPURCHASE AGREEMENT,** which involves the actual sale and repurchase of securities (Part 5, Fig. 9)

SEGMENTS: individual activities within an **ENTERPRISE FUND** that have revenue sources of their own dedicated to repaying some form of **REVENUE-BACKED DEBT;** governments are required to make disclosures in the **NOTES TO FINANCIAL STATEMENTS** about their segments (Part 10, Fig. 71)

SERVICE CAPACITY: a government's ability and willingness to meet its service commitments on an ongoing basis; see **ECONOMIC CONDITION** (Part 14); or, the amount of service that can be provided with a **CAPITAL ASSET;** see **SERVICE UTILITY** (Part 5)

SERVICE CONCESSION ARRANGEMENT (SCA): a transaction in which a government transfers to another party the rights and responsibilities to operate a capital asset, such as a toll road, and collect fees from users of the **CAPITAL ASSET,** generally in return for payment(s) from the other party; the government retains the right to determine what services are provided with the capital asset, to whom, and for what fee, and at the end of the agreement receives the capital asset back with a significant amount of **SERVICE CAPACITY** remaining (Part 5)

SERVICE COST: the amount of increase in the **TOTAL PENSION LIABILITY** or **TOTAL OPEB LIABILITY** as a result of pension benefits or **OTHER POSTEMPLOYMENT BENEFITS** earned in the year for which the liability is measured (Parts 5 and 6)

SERVICE EFFICIENCY: how much service can be provided or what level of effectiveness can be achieved given a certain level of input (Part 14)

SERVICE EFFORTS AND ACCOMPLISHMENTS (SEA) INFORMATION: information about a government's inputs, outputs, efficiency, and outcomes that measures its service performance; see **SERVICE CAPACITY** (Part 14)

SERVICE UTILITY: the capacity of a **CAPITAL ASSET** to be used to provide services; **DEPRECIATION** allocates the **HISTORICAL COST** of a capital asset over its estimated period of service utility; see also **SERVICE CAPACITY** (Parts 2 and 5, TOT p. 26)

SHORT-TERM LEASES: leases with a maximum possible length of 12 months or less, including any options to extend (UFR p. 98)

SI: see **SUPPLEMENTARY INFORMATION**

SINGLE-EMPLOYER PLAN: a pension or **OTHER POSTEMPLOYMENT BENEFITS** plan that serves the employees and retirees of just one government (and its component units if they participate in the plan); see also **AGENT MULTIPLE-EMPLOYER PLAN** and **COST-SHARING MULTIPLE-EMPLOYER PLAN** (Part 5)

SOLVENCY: a **FINANCIAL ANALYSIS** concept addressing a government's ability to satisfy its **NONCURRENT LIABILITIES**; see **COVERAGE** and **LEVERAGE** (Parts 4 and 14)

SOLVENCY RATIOS: calculations that examine a government's ability to meet long-term obligations (Part 14)

SPECIAL ASSESSMENT: payments levied against a specific group of persons or businesses, often in a particular geographic area of a government's jurisdiction, for the purpose of financing services to those persons or businesses in that area or repaying **SPECIAL ASSESSMENT DEBT** issued to finance capital improvements on behalf of those persons or businesses (Part 5)

SPECIAL ASSESSMENT DEBT: debt issued to finance capital improvements on behalf of specific persons or businesses, often in a particular geographic area of a government's jurisdiction, and repaid with a **SPECIAL ASSESSMENT** levied against those persons or businesses (Part 5)

SPECIAL FUNDING SITUATION: circumstances in which (1) a **NONEMPLOYER CONTRIBUTING ENTITY** is legally responsible for making contributions to a pension or **OTHER POSTEMPLOYMENT BENEFITS** plan that is used to provide benefits to employees of other governments and (2) either the amount of contributions is not dependent on events or factors not related to pensions (or **OPEB**, as appropriate) or the nonemployer entity is the only entity legally required to make contributions directly to the plan (Part 4, UFR p. 100)

SPECIAL ITEMS: nontypical changes in **NET POSITION** or **FUND BALANCES** that are within the control of a government and are either unusual in nature or infrequent in occurrence; they are reported separately from **REVENUES** and **EXPENSES/EXPENDITURES** (Part 7, UFR p. 163)

SPECIAL-PURPOSE GOVERNMENTS: governments that provide a single or a few related services, such as school districts, public colleges and universities, public hospitals, and public utilities (Part 11, BTN p. 268)

SPECIAL REVENUE FUND: a **GOVERNMENTAL FUND** that tracks revenue sources restricted or committed to specific uses (Part 9, BTN p. 194)

SSAP: see **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

STABILIZATION ARRANGEMENTS: formal policies of setting aside resources in advance of unexpected needs or emergencies (Part 9)

STATEMENT OF ACTIVITIES: a **GOVERNMENT-WIDE FINANCIAL STATEMENT** that reports a government's **REVENUES** and **EXPENSES**, as well as other **CHANGES IN NET POSITION** during the year (Part 7, Figs. 42, 84, B-2, C-2, D-2)

STATEMENT OF CASH FLOWS: a **FINANCIAL STATEMENT** comparing the inflows and outflows of cash during a given period for operating and other purposes; governments prepare this statement for their **PROPRIETARY FUNDS** (Part 10, Figs. 70, 90, B-9, C-8, D-7)

STATEMENT OF CHANGES IN FIDUCIARY NET POSITION: a **FINANCIAL STATEMENT** that reports **ADDITIONS** to and **DEDUCTIONS** from the **FIDUCIARY NET POSITION** of **FIDUCIARY FUNDS** during a given period (Part 10, Fig. 79, B-11, C-10)

STATEMENT OF FIDUCIARY NET POSITION: a **FINANCIAL STATEMENT** that reports the **ASSETS, DEFERRED OUTFLOWS OF RESOURCES, LIABILITIES, DEFERRED INFLOWS OF RESOURCES,** and **NET POSITION** of **FIDUCIARY FUNDS** at a given point in time (Part 10, Figs. 78, B-10, C-9)

STATEMENT OF NET POSITION: a **FINANCIAL STATEMENT** that reports **ASSETS, DEFERRED OUTFLOWS OF RESOURCES, LIABILITIES, DEFERRED INFLOWS OF RESOURCES,** and **NET POSITION** at a given point in time; one of a government's **GOVERNMENT-WIDE STATEMENTS,** as well as of the **PROPRIETARY FUNDS** and **FIDUCIARY FUNDS** financial statements (Parts 4–6 and 10, Figs. 1, 68, 83, B-1, C-1, D-1)

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES: a **FINANCIAL STATEMENT** that reports the **REVENUES, EXPENDITURES,** and other inflows and outflows of the **GOVERNMENTAL FUNDS** (Part 9, Figs. 54, B-5, C-5, D-4)

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION: a **FINANCIAL STATEMENT** that reports the **REVENUES, EXPENSES,** and other inflows and outflows of the **PROPRIETARY FUNDS** (Part 10, Figs. 69, 89, B-8, C-7, D-6)

STATISTICAL SECTION: the portion of the **CAFR** that contains additional financial, economic, and demographic information for multiple years relating to the government and its environs (Part 1, BTN p. 141)

STEWARDSHIP: the act of being accountable and demonstrating **ACCOUNTABILITY** to another party

SUBSEQUENT EVENT: an occurrence after the end of the fiscal year that, if known by the reader of the **FINANCIAL STATEMENTS,** would make a difference in their decisions or conclusions based on financial statement information (Part 13)

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (SSAP): NOTES TO FINANCIAL STATEMENTS that explain the general accounting methods and assumptions employed by a government when recording financial information and reporting that information in its **FINANCIAL STATEMENTS,** especially those instances in which a government has a choice among two or more approaches (Part 3, Fig. E-2, BTN p. 35)

SUPPLEMENTARY INFORMATION (SI): SUPPORTING INFORMATION that a government presents voluntarily, it is useful for placing the **FINANCIAL STATEMENTS** and **NOTES TO FINANCIAL STATEMENTS** in context (Parts 2, 6, 8–10, 12, and 13, KIM p. 24)

SUPPORTING INFORMATION: information that is presented following the **NOTES TO FINANCIAL STATEMENTS** for the purpose of placing the **FINANCIAL STATEMENTS** and notes in a context that helps the reader better understand them (Parts 2, 6, 8–10, 12, and 13, KIM p. 24)

TANs: see **TAX ANTICIPATION NOTES**

TAX ABATEMENT: a transaction in which a government agrees to forgo tax revenue in return for an entity or individual performing a beneficial action, such as relocating to the government's geographic area (Part 8, KIM p. 175, Fig. 47)

TAX AND REVENUE ANTICIPATION NOTES (TRANs): a type of **NOTE** issued in advance of receiving payments from taxes and other revenues (BTN p. 80)

TAX ANTICIPATION NOTES (TANs): a type of **NOTE** issued in advance of receiving payments from tax revenues (BTN p. 80)

TAX-BACKED DEBT: LONG-TERM DEBT guaranteed to be repaid with specific tax revenues (Parts 6 and 14, Figs. 36 and 37)

TAXES RECEIVABLE: payments due to a government from taxes

TAX LEVERAGE RATIO: a measure of the property tax increase necessary to cover a 1 percent increase in **EXPENSES** or **EXPENDITURES** (Part 14)

TERMINATION BENEFITS: benefits a government offers to employees to induce them to retire or otherwise voluntarily leave employment, and benefits given to employees who are involuntarily separated from employment (Part 5)

TERMINATION RISK: the risk of losing protection from loss of fair value or cash flows because a **DERIVATIVE** ends early (Part 5, Fig. 21)

TOL: see **TOTAL OPEB LIABILITY**

TOTAL DIRECT RATE: the weighted average of all individual **DIRECT RATES** applied by a government to a particular revenue base (Part 8, Figs. 48 and 49)

TOTAL OPEB LIABILITY (TOL): a government's overall obligation to provide **OTHER POSTEMPLOYMENT BENEFITS** to its active and inactive employees and beneficiaries; it equals the portion of the present value of projected benefit payments that is related to service already provided by employees (Parts 4 and 5)

TOTAL PENSION LIABILITY (TPL): a government's overall obligation to provide pension benefits to its active and inactive employees and beneficiaries; it equals the portion of the present value of projected benefit payments that is related to service already provided by employees (Parts 4 and 5)

TPL: see **TOTAL PENSION LIABILITY**

TRANs: see **TAX AND REVENUE ANTICIPATION NOTES**

TRANSACTIONS: events in which a government provides something of value to another party external to the government, or vice versa, or both

TRANSFERS: shifts of resources from one part of a government to another without receiving something in return, such as from **GOVERNMENTAL ACTIVITIES** to **BUSINESS-TYPE ACTIVITIES**, or from the **GENERAL FUND** to a **DEBT SERVICE FUND** (Parts 7 and 9, Fig. 57)

TRANSMITTAL LETTER: see **LETTER OF TRANSMITTAL**

UAAL: see **UNFUNDED ACTUARIAL ACCRUED LIABILITY**

UNASSIGNED FUND BALANCE: the portion of **FUND BALANCE** that is available for any purpose (Part 9, Fig. 53)

UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL): under prior accounting standards, the portion of the **ACTUARIAL ACCRUED LIABILITY (AAL)** of an **OTHER POSTEMPLOYMENT BENEFITS** plan that is not covered by (or that exceeds) the plan's **ACTUARIAL VALUE OF ASSETS** (Part 5, UFR p. 110)

UNPAID CLAIMS LIABILITIES: claims against a **PUBLIC ENTITY RISK POOL** that have not yet been remitted (Part 6, Figs. 33 and 34)

UNRECOGNIZED SUBSEQUENT EVENTS: SUBSEQUENT EVENTS that are related to conditions that did not exist as of the date of the financial statements (Part 13)

UNRESTRICTED NET POSITION: the portion of **NET POSITION** not **RESTRICTED** or invested in **CAPITAL ASSETS** (Part 4, UFR p. 45, Fig. 1)

USEFUL LIFE: period during which a **CAPITAL ASSET** has **SERVICE UTILITY** for government operations (Parts 2 and 4, TOT p. 26)

USER FEES: see **CHARGES FOR SERVICES**

VARIABLE-RATE DEBT: debt with interest rates that rise and fall with market conditions; see **FIXED-RATE DEBT**

VOLUNTARY NONEXCHANGE TRANSACTION: a **NONEXCHANGE TRANSACTION** resulting from legislative or contractual agreements entered into willingly, other than **EXCHANGE TRANSACTIONS**, such as **UNRESTRICTED** grants and donations (Part 2, BTN p. 16)

ZERO-COUPON BONDS: a type of debt that is repaid at **MATURITY** rather than annually (Part 5)

APPENDIX G

INFORMATION ABOUT THE GASB

WHAT IS THE GASB?

The Governmental Accounting Standards Board (GASB, or "gaz-bee") is the private, nonpartisan, nonprofit organization that works to create and improve the standards U.S. state and local governments follow when accounting for their finances and reporting them to the public. The GASB was founded under the auspices of the Financial Accounting Foundation (FAF), which appoints the GASB members, secures its funding, and oversees its activities. The FAF performs the same functions for the GASB's counterpart for business and nongovernmental not-for-profits, the Financial Accounting Standards Board (FASB).

The GASB was created in 1984 to succeed the National Council on Governmental Accounting (NCGA) by agreement among:

- FAF
- American Institute of Certified Public Accountants (AICPA)
- Council of State Governments
- Government Finance Officers Association
- International City/County Management Association
- National Association of Counties
- National Association of State Auditors, Comptrollers and Treasurers
- National Conference of State Legislatures
- National League of Cities
- National Governors' Association, and
- U.S. Conference of Mayors.

Although the GASB does not have the power to enforce compliance with the standards it promulgates, the authority for its standards is recognized by the AICPA. Also, legislation in many states requires compliance with GASB standards, and governments usually are expected to prepare financial statements in accordance with those standards when they issue bonds or notes or otherwise borrow from public credit markets.

WHO IS THE GASB?

The GASB is composed of a full-time chair and six part-time members drawn from various parts of the GASB's constituency—state and local government finance officers, auditors, comptrollers, the

accounting profession, academia, and the community of persons who use financial statement information.

The GASB has a professional staff drawn from similar constituencies as the Board. The staff works directly with the Board and its task forces, conducts research, analyzes oral and written comments received from the public, and drafts documents for consideration by the Board.

WHAT IS THE GASB TRYING TO ACCOMPLISH?

The mission of the GASB is to:

- Establish and improve accounting and financial reporting standards for state and local governments to provide useful information for users of financial reports
- Educate stakeholders on how to most effectively understand and implement those standards.

The mission is accomplished through a comprehensive and independent process that encourages broad participation, objectively considers all stakeholder views, and is subject to oversight by the FAF's Board of Trustees.

These standards are essential to the efficient and effective functioning of our democratic system of government:

- They improve governments' ability to demonstrate their stewardship to the public, and
- They improve the information available to the public for holding governments accountable.

WHO ARE "USERS"?

The general citizenry is the largest and most diverse portion of the *user community*—the amalgam of people who use governmental financial information, either formally or informally, to make decisions or assess government accountability. A second group is investors and creditors, the people and institutions that buy a government's bonds or to whom a government otherwise is in debt. A third major component is elected legislators—city council members, town supervisors, state senators, and the like—and their staffs, as well as legislative and oversight commissions and similar bodies. The first two broad groups of users are external to government. Though a part of government and considered accountable for it, the third group typically is not in charge of operations and therefore is external to the process of accounting for and reporting governmental finances. But a fourth group may be found solidly *within* government—public employees, managers, and others who do not have access to the same quantity and breadth of information available to government executives (mayors, town managers, governors, and so on) and their staffs.

Clearly, not all of these people read government financial statements. Many find financial information about governments elsewhere, in budgets and other documents, on websites, in newspapers. Most do

not actively search for government financial information at all but, rather, passively use information—whether they realize it or not—that has been gathered, analyzed, and republished by others who *are* intensive users of financial statements. This smaller subset of the user community might be referred to as *intermediate users*—persons and organizations that reprocess governmental information into a form that is digestible to most citizens. Some intermediate users are citizen, taxpayer, and good government groups; think tanks, research organizations, and other academic institutions; the media; and analysts in investment firms and mutual funds.

HOW DOES THE GASB ESTABLISH STANDARDS?

The GASB follows the set of *due process* activities enumerated in its published Rules of Procedure before issuing its standards. Due process is stringent and is designed to permit timely, thorough, and open study of financial accounting and reporting issues by the preparers, attestors, and users of financial reports, in order to encourage broad public participation in the standards-setting process.

For many issues it addresses, the GASB:

- Appoints an advisory task force of outside experts
- Studies existing literature on the subject and conducts or commissions additional research
- Publishes for public comment a discussion document setting forth the issues and possible solutions and seeks public input
- Conducts public hearings and forums of financial statement users, and
- Broadly distributes the Board's Preliminary Views and then an Exposure Draft of proposed standards for public comment.

Significant steps in the process are announced publicly. The GASB's meetings are open to public observation in person or via webcast, and a public record is maintained. The GASB also is advised by the Governmental Accounting Standards Advisory Council, a group appointed by the FAF and representing a wide range of the GASB's constituents.

APPENDIX H

ALPHABETICAL INDEX

Page Number

Ability to pay 323–328
Ability-to-pay ratios 49, 167, 324–328
Accountability 2
Accounting changes 291–292
Accounting equation 37, 195–196
Account pool 113–114
Accounts payable 41, 78–80
Accounts receivable 66–69
Accrual basis of accounting 11
Accumulated depreciation 40–41
Actuarial accrued liability 110
Actuarially determined contributions 129–132
Actuarial valuation 101
Actuarial value of assets 110
Additions 256, 259
Advance refunding 84–85
Agency funds 10, 257, 263
Agent multiple-employer plans 100–108, 110–111, 125–127, 129–132
Alternative measurement method 108
Amortization 53
Amortized cost 53
Annual required contribution 111
Asset retirement obligation 112
Assets 39–41
Asset sufficiency ratio 126–129, 330
Assigned fund balance 198–199
Audit committee letter 29
Auditor's report (opinion) 30–31, E-3
Balance sheet 195–201, 272, B-6, C-5, D-5
Banking pool 113–114
Basic financial statements 3
Basis of accounting 11, 18–19
Basis risk 95–96

Page
Number

Blended component units 282–283
Bonds 81–89
Budgetary comparisons 4, 220–225
Budget variances 223, 225
Business-type activities 8, 19, 179
Calls 90
Capital and related financing cash flows 241–243
Capital asset depletion ratio 335
Capital asset replenishment ratio 336
Capital assets 26, 33–34, 40–41, 335–336
Capital assets, impairment of 71, 74–75
Capital assets, notes about 70–77
Capital assets, required supplementary information about 132–135
Capital assets, supplementary information about 139–141, E-13
Capital grants and contributions 160–161
Capital leases 98
Capital leases, notes about 99
Capital projects funds 9, 194
Change in net position 163–164, 179–183
Changes in accounting estimate 293
Changes in accounting principle 291–292
Changes in fund balance 201–203, 205, 229–230, 232
Changes in the reporting entity 291–292
Charges for services 160
Claims and judgments 113–117
Claims development information, 10-year 137–139
Classified format 37, 237–238
College and university financial statements 275–279
Combining financial statements 24, 248
Combining financial statements, component units 248, 284–286
Combining financial statements, fiduciary funds 248, 261–264
Combining financial statements, individual funds 248
Combining financial statements, internal service funds 248, 252–255
Combining financial statements, nonmajor enterprise funds 246–252
Combining financial statements, nonmajor governmental funds 226–229, 248
Committed fund balance 198
Common-size ratios 46, 309–311

Page
Number

Comparative financial statements 226, 248
Compensated absences 42
Component units 19, 281–287
Component units, combining statements 284–286
Component units, condensed statements 285, 287
Component units, fund financial statements 283
Component units, major 282
Comprehensive annual financial report 4
Concentration of credit risk 58–59
Condensed financial statements 245, 247, 285, 287
Conduit debt 99
Contingent liabilities 121
Corrections of errors 291–292
Cost-sharing multiple employer plans 100, 102–103, 127–129, E-11
Coverage 48, 320–322
Coverage ratios 320–321
Covered-employee payroll 127–129
Covered payroll 126–127, 129–130
Credit risk 58–59, 95, 97
Current assets 39–40
Current financial resources measurement focus 12
Current liabilities 41
Current ratio 318–319
Current refunding 84
Custodial credit risk 52, 58
Days cash on hand ratio 319–320, 329
Days inventory ratio 335
Days payable ratio 334
Days receivable ratio 333
Days unpaid claims ratio 334
Debt capacity 143–154
Debt limitations 149–151
Debt per capita 143
Debt ratios, supplementary information about 142–154
Debt refundings 84–86
Debt service coverage 152–154, 321
Debt service funds 8, 194

Debt service, notes about 170–171
Debt service, supplementary information about 142, 152–154
Debt, supplementary information about 142–154
Deductions 256, 259
Defeasance 84–85
Deferred inflows of resources 42–43
Deferred inflows of resources, notes about 122
Deferred inflows of resources, related to pensions and OPEB 102
Deferred outflows of resources 42–43
Deferred outflows of resources, notes about 122
Deferred outflows of resources, related to pensions and OPEB 102
Deficit 204–205
Demand bonds 87–89
Demographic information, supplementary information about 296–298, 300
Deposits, notes about 51–53
Depreciation 26
Depreciation, notes about 70–72, 169
Derivatives 89–98
Derivatives, risks associated with 96–97
Derived tax revenues 16
Discount rate 106–107
Discretely presented component units 8
Donor-restricted endowments 69–70
Due from other governments 66
Duration 60–61
Economic condition 47
Economic condition analysis 315–328
Economic information, supplementary information about 296–300
Economic resources measurement focus 11
Enabling legislation 44
Enabling legislation, notes about 122–123
Enterprise funds 9, 235–252
Excess (deficiency) of revenues over expenditures 204–205
Expenditures 12, 201–203
Expenditures, trends in 229–230, 232–233
Expenses 157–160
Expenses, notes about 169–175

Page
Number

Expenses, trends in, supplementary information about 179–183
External investment pool, notes about 54
Extraordinary items 162–163, 175
Extraordinary items, notes about 175
Fair value 53, 56–57
Fiduciary activities 3, 179
Fiduciary funds 9–10, 256–265
Fiduciary funds, classes 9–10, 257, 264–265
Fiduciary funds, combining statements 261–264
Fiduciary net position 101
Final budget 220
Finance-related legal and contractual provisions, violations of 295–296
Financial analysis 307–339
Financial condition 47
Financial efficiency ratios 67, 69, 332–336
Financial position 316–317
Financial section (of a CAFR) 4
Financial statements 7–19
Fiscal capacity 318–328
Foreign currency risk 59, 97
Fund balance 196–199, 200
Fund balance, notes about 213–215
Fund balance, trends in 229, 231
Fund financial statements 3, 195–209
General fund 8, 194, 199
Generally accepted accounting principles 3
General obligation debt 143
General obligation debt, supplementary information about 143–146
General purpose governments 4
General revenues 162–163
Going concern 293–294
Governmental Accounting Standards Board 3
Governmental activities 8, 19
Governmental funds 8, 193–233
Governmental funds, combining statements 225–229
Governmental funds, compared with governmental activities 193
Governmental funds, types 8–9, 194

Page
Number

Government employees, supplementary information about 301–303
Government-mandated nonexchange transactions 16
Government-wide financial statements 3, 37–49, 157–167
Hedging derivative instruments 91–97
Historical cost 40
Impairment of capital assets 71, 74–75
Imposed nonexchange revenues 16
Inflation, adjusting for 312
Infrastructure 4, 132–135
Inputs 336–337
In-substance defeasance 84–85
Interest coverage ratios 320–321
Interest rate risk 59–62, 95, 97
Interest rate swaps 90
Interfund balances, notes about 209–211
Interfund transfers, notes about 209–210, 212
Internal service funds 9, 235–245
Internal service funds, combining statements 248, 252–255
Interperiod equity 43
Introductory section (of a CAFR) 4, 27–29
Inventory 26
Investing cash flows 241–243
Investments, notes about 53–65
Investment trust funds 9, 257
Jointly governed organizations 288–289
Joint ventures 288–289
Landfills, notes about 112–113, 172–174
Leases 42, 98–99
Leases, notes about 99, 171–172
Legal and contractual provisions, finance-related 295–296
Legal debt limit 149–151
Legal debt margin 149–151
Letter of transmittal 27–29
Leverage 48, 320
Leverage ratios 320
Liabilities 41–42
Liabilities, notes about 77–121

Page
Number

Liquidity 47–48, 318–320
Long-term liabilities, changes in 34, 81–84
Major funds 195, E-12
Management's discussion and analysis 3, 31–35, A-1
Market-access risk 96
Maximum annual debt service coverage 329
Measurement date 103
Measurement focus 12, 18–19
Minimum fund balance policy 214
Modified accrual basis of accounting 12
Modified approach 40–41
Modified approach, required supplementary information about 132–135
Net assets 44
Net asset value (NAV) per share 57–58
Net cost 161–162
Net (expense) revenue 161–162, 180
Net investment in capital assets 44
Net OPEB liability 101, 105, 107–108, 110–111, 330
Net OPEB liability, changes in 108, 110–111, 125–127, 129
Net OPEB obligation 111
Net pension liability 101, 105–108, 110–111, 330
Net pension liability, changes in 108, 110–111, 125–127, 129
Net position 44–45
Net position held in trust 256
Net position, notes about 122–123
Net position, supplementary information about 154–155
Noncapital financing cash flows 241–243
Noncurrent assets 40
Noncurrent liabilities 41–42
Nonexchange financial guarantees 118–121
Nonexchange transactions 13–16
Nonmajor funds, enterprise, combining statements 246–252
Nonmajor funds, governmental 195
Nonmajor funds, governmental, combining statements 226–228, 248
Nonoperating expenses 239–240
Nonperating revenues 239–240
Nonspendable fund balance 196

Page
Number

Notes (short-term debt) 80–81
Notes to financial statements 3, 20–23
On-behalf payments 174–175
Operating cash flows 240–241, 242–243
Operating expenses 239–240
Operating grants and contributions 160–161
Operating indicators, supplementary information about 301, 303–304
Operating information, supplementary information about 301–305
Operating leases 98–99
Operating revenues 239–240
Original budget 220
Other financing sources and uses 201–202
Other postemployment benefits 100–111, 125–132
Other postemployment benefits, analysis 330
Other postemployment benefits, defined contribution plans 100, 109
Other postemployment benefits, multiple-employer plans 100–101
Other postemployment benefits, notes about 103–111
Other postemployment benefits, required supplementary information about 125–132
Outcomes 337
Outputs 337
Overall credit risk 58
Overlapping debt 146–149
Overlapping rates 185, 187, 189
Own-source revenues 181–192
Payables 41, 78–80, 333–334
Payables efficiency ratio 333
Payables turnover ratio 334
Pension (and other postemployment benefit) trust funds 9, 102, 105, 257
Pensions 100–111, 125–132
Pensions, analysis 330
Pensions, defined benefit plans 100–111, 125–132
Pensions, defined contribution plans 100, 109
Pensions, multiple-employer plans 100–101
Pensions, notes about 103–111
Pensions, required supplementary information about 125–132
Percentage change 46–47, 309–314
Percentage distribution 46, 165, 310–311, 313–315

Page
Number

Period of availability 13
Permanent funds 9, 194
Pledged-revenue coverage 151–154
Primary government 8
Principle employers, supplementary information about 299–300
Principle revenue payers 186, 188–189
Prior-period adjustments 291–292
Private-purpose trust funds 10, 257
Program revenues 160–161
Property tax calendar 218, 318
Property tax levies and collections 190–191
Property values 143, 145–146, 149–150, 181, 184, 189–191
Property values, supplementary information about 181, 184
Proprietary funds 9, 235–245
Proprietary funds, segments 245–247
Proprietary funds, supplementary information about 246–255
Proprietary funds, types 9, 236
Public entity risk pools, notes about 113–117
Public entity risk pools, required supplementary information about 135–139
Puts 87, 90
Quick ratio 318–319
Rainy-day funds, notes about 213–214
Receivables 66–69, 332–333
Receivables efficiency ratio 332
Receivables turnover ratio 333
Recognized subsequent events 294–295
Reconciliation of cash and accrual 243–244
Reconciliation of claims liabilities by contract 135–136
Reconciliation of fund balance to net position 199–200, 215–218, B-7, C-5, D-5
Reconciliation of net change in fund balance to changes in net position 205–207, 215–216, 218–219, B-9, C-7, D-6
Refundings 84–86
Related organizations 288–289
Repurchase agreements 61–62
Required supplementary information 3
Reserved fund balance 200
Restricted fund balance 196, 214

Restricted net position 44
Revenue availability 13
Revenue-backed debt, analysis 328–330
Revenue-backed debt, supplementary information about 143–144, 146, 151–154
Revenue base, supplementary information about 181, 184
Revenue capacity 181–192
Revenue dispersion 165–166
Revenue rates, supplementary information about 185, 187, 189
Revenues 12–13, 160–164
Revenues, notes about 169, 174–179
Revenues, trends in, supplementary information about 179–183, 229–230, 232–233
Reverse repurchase agreements 62–63
Risk, analysis 330–332
Risk exposure ratio 331
Risk, related to derivatives 95–97
Risk, related to investments 57–61
Rollover risk 95–96
Schedule of employer contributions 129–131, E-11
Securities lending 63–65
Segments, notes about 245–247
Service capacity 316, 336–338
Service concession arrangements 75–77
Service cost 102
Service efficiency 337
Service efforts and accomplishments 336–338
Short-term debt 80–81, 196, 245
Single-employer plans 100–108, 110–111, 125–127, 129–132
Solvency 48–49, 320–322
Solvency ratios 320–322
Special assessment debt 86–87, 152–154
Special funding situations 100–101
Special items 162–163, 175
Special items, notes about 175
Special-purpose governments 4, 267–279, 325–327
Special revenue funds 8, 194, 218
Special revenue funds, notes about 218
Stabilization arrangements 213–214

Statement of activities 157–167, 271, 273, B-4–B-5, C-4, D-4
Statement of activities, notes about 169–179
Statement of activities, supplementary information about 179–192
Statement of cash flows 238, 240–245, 278, B-12, C-10, D-9
Statement of changes in fiduciary net position 256, 259, B-14, C-12
Statement of fiduciary net position 256, 258, B-13, C-11
Statement of net position, government wide 37–49, 270, 276, B-3, C-3, D-3
Statement of net position, proprietary funds 235–238, B-10, C-8, D-7
Statement of revenues, expenditures, and changes in fund balances 201–209, 274, B-8, C-6, D-6
Statement of revenues, expenses, and changes in fund net position 235–239, 277, B-11, C-9, D-8
Statistical section (of a CAFR) 4
Subsequent events 294–295
Summary of significant accounting policies 35, 70, E-6
Supplementary information 24
Supporting information 24–25
Surplus 204–205
Tax abatements 175–179
Tax leverage ratio 331–332
Ten-year claims development information 137–139
Termination benefits 112
Termination risk 95–96
Times-interest-earned 321
Total OPEB liability 101
Total pension liability 101
Transfers 162, 209–210, 212
Unassigned fund balance 199
Unfunded actuarial accrued liability 110
Unrecognized subsequent events 294–295
Unreserved fund balance 200, 214
Unrestricted net position 44–45
Variable-rate debt 90
Voluntary nonexchange transactions 16
Weighted average maturity 59–60