

## GOVERNMENT-WIDE FINANCIAL STATEMENTS

STATEMENTS REQUIRED - GASB 34 mandates the presentation of two basic government-wide financial statements:

- A. The Statement of Net Position
- B. The Statement of Activities

The scope of the new government-wide financial statements is to include all governmental and business-type activities, but NOT fiduciary activities. That means that Fiduciary Funds will not be included on the government-wide statements. Governmental activities and business-type activities are to be reported in separate columns, with a consolidated total column being presented for the primary government. To the right of the total column will be a column for reporting component units such as the Housing and Redevelopment Commissions.

STATEMENT OF NET POSITION – Although GASB 34 allows for a variety of layouts, local governments in South Dakota will use the balance sheet format for the government-wide statement of net position. The balance sheet format provides a “balancing effect” whereby total assets should equal total liabilities and net position.

What was previously referred to as the “equity” section should now be called “net position”. Net position follow the following formula:

$$\text{Total Assets} - \text{Total Liabilities} = \text{Net Position}$$

Although GASB 34 allows for alternative methods of presentation, South Dakota counties should report the balance sheet accounts on the statement of net position in the order of their relative liquidity. For example, cash is more liquid than inventories, inventories are more liquid than capital assets, etc... GASB 34 prescribes that net position be classified into the following three categories:

- 1. Net Investment in Capital Assets
- 2. Restricted
- 3. Unrestricted

The first category should reflect the cost of capital assets, adjusted for any accumulated depreciation, as well as for any debt associated with their acquisition, construction or improvement.

The “restricted net position” category is designed to reflect net position that are subject to restrictions that are beyond the government’s control. Qualifying restrictions for this purpose include the following:

- a. Restrictions that are externally imposed (e.g., by creditors, grantors or contributors)
- b. Restrictions imposed by law through constitutional provisions or enabling legislation.

Most of the net position of special revenue funds would constitute “restricted net position”. For example, the assets of the Sales Tax and 911 Funds are restricted by statute.

The enabling legislation part of the definition covers situations when the government passes a law that gives them the ability to levy a tax or otherwise raise revenues, and in that law, the

government commits to using those resources for a particular purpose. That arrangement is tantamount to a legally binding agreement between the government and the taxpayers establishing limitations on how those funds can be used. The government generally cannot unilaterally decide to do something else with those resources. This is different from situations when a government “earmarks” a portion of an existing revenue source. (Capital outlay accumulations) In that situation the government does not obtain funds under restrictive conditions; thus, the limitations imposed indicate assignments, not restrictions.

Any remaining balance of net position is to be reported as “unrestricted.” GASB 34 does not permit the reporting of designations or assignments on the face of the government-wide statement of net position.

**POLICY FOR USE OF RESTRICTED RESOURCES** – Under the new governmental financial reporting model, net position is broken into three categories. In practice, it is common for governments to have the option of using either restricted or unrestricted resources to liquidate a particular expense. Accordingly, governments must select a flow assumption to determine in such cases which assets (restricted or unrestricted) are being used first, when both restricted and unrestricted assets are available for the same purpose. GASB 34 requires that this flow assumption (policy) be disclosed in the notes to the financial statements.

For example, within a Capital Projects Fund there may be assets that are restricted because the derived from a bond issue and there may be unrestricted local dollars committed to the project. Each county should adopt a policy to stipulate whether restricted on unrestricted dollars (or a percentage of each) will be used first to pay for the capital project.

**INTERNAL SERVICE FUNDS** – As a general rule, the assets and liabilities of internal service funds will be eliminated, for the most part, in the process of consolidation. Any remaining balances that are not eliminated normally will be reported in the “governmental activities” column of the statement of net position (rather than the “business-type activities” column), even though internal service funds are proprietary funds rather than governmental funds. The GASB reasons that this treatment is appropriate because the activities accounted for in internal service funds are usually more governmental than business-type in nature. (self insurance coverage for employees of governmental activities). Conversely, in situations where enterprise funds are, in fact, the predominant participants in internal service fund activities, residual balances should be reported in the “business-type activities” column of the government-wide statement of net position.

A key goal of consolidating internal service funds is to eliminate duplication. The revenues and expenses between the internal service fund and the entity fund it serves should not double up on reporting the revenues and expenses. For example, the charge to a General Fund function for health insurance and the payment of a claim from the internal service fund would essentially double up on reporting the same expenditure.

For purposes of consolidation, it is presumed that an internal service fund operates on a strictly break-even basis within the primary government. Accordingly, any profit on internal activity is presumed to indicate that participating functions have been overcharged. Likewise, any loss on internal activity is presumed to indicate that participating functions have been undercharged. Therefore, consolidation is accomplished by reducing (if there is a profit) or increasing (if there is a loss) the amount of expense reported in the participating functions.

Assume the following facts at year end for a particular self-insurance internal service fund:

Charges for services	\$800,000
Cost of services	700,000
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Increase in net position	\$100,000
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Further assume that this internal service fund provides goods and services to individual functions at the following levels:

General Government	30%	\$ 30,000
Public Safety	20%	20,000
Public Works	50%	50,000
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Totals	100%	\$100,000
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Since the internal service fund operated at a profit for the year the profit should be posted to the functions noted above during the year end “reconciliation process”.

CONSOLIDATION – The new statement requires that the total column for the primary government presented on the government-wide statement of net position be fully consolidated. That is to say balances (of interfund loans, etc) between “governmental activities” and “business-type activities” are to be eliminated from the total column.

Rather than reporting “due to” and “due from” accounts, GASB suggests the use of an account called internal balances. The internal balances account will be reported as an asset account. Any “due from” amounts are to be reported as a positive internal balance amount. A “due to” amount would be reported as a negative internal balance amount. If you add across to arrive at the total internal balance for the primary government, the balance would be zero.

Bear in mind that the preceding internal balances approach should only be used for interfund activity between governmental and business-type activities. If there are interfund accounts solely within the governmental activities column, then those amounts should be eliminated. For example, an interfund loan from the Sales Tax Fund to the General Fund would be eliminated because both of those funds are reported within the governmental activities column.

GOVERNMENT-WIDE STATEMENT OF ACTIVITIES – The other basic government-wide financial statement in the new financial reporting model is the statement of activities. The format of this new statement differs profoundly from the formats now used to report the activities of governmental, proprietary and fiduciary funds.

Governments, unlike businesses, do not ordinarily provide services as a means to an end (i.e., profit), but rather as an end in themselves. In principle then, governments make their financial plans by first determining the types and levels of services they need or wish to provide, and then determining how these services are to be financed. Some services are partially financed from sources outside the government itself (i.e., charges for services, grants and contributions). In that case, a government will naturally wish to isolate and focus its attention on the portion of the cost of services that it will need to finance from its own resources. The “net program expense” format mandated by GASB 34 is designed precisely to reflect this unique governmental perspective.

PROGRAM REVENUES - Under the net program cost format, program expenses are netted against program revenues. Program revenues include the following:

- amounts received from those who purchase, use or directly benefit from a program; (rubble sites, swimming pools, airports, etc)  
Charges for services should also include revenues from licenses and permits (they directly benefit by paying for the privilege), liquor

licenses and building permits.

- amounts received from parties outside the county's citizenry (e.g., grants and contributions) that are restricted to one or more specific programs.
- earnings on investments that are legally restricted for a specific program

Charges for services should be reported separately from grants and contributions. Likewise, operating grants and contributions should be reported separately from capital grants and contributions. A grant or contribution that may be used for either operating or capital purposes should be treated as an operating grant or contribution.

Fines and forfeitures should be reported as program revenues. As a rule, charges for services should be reported as a program revenue of the function that generates them. In the case of fines and forfeits, one function (e.g., police, health department) often will issue a citation for an alleged legal or regulatory infraction, which is then subject to adjudication by the courts. Another way to look at reporting fines with the police department is that if there were no police department there would be no fines.

To qualify as program revenue, a grant or contribution must be restricted to one or more specific functions. In the case of multi-purpose grants, the amount associated with each particular function must be specified either in the grant contract or in the underlying application form. However, multi-purpose grants of the reimbursement variety always will meet the test of restriction because such a grant, for accounting and financial reporting purposes, is only considered to occur when all eligibility requirements have been met (including the incurrence of qualifying expenditures in a particular function).

**GENERAL REVENUES** – All revenues that do not qualify as program revenues should be reported as general revenues. General revenues are to be presented immediately below the totals for “net (expense) revenue and changes in net position.”

All taxes, even those that are levied for a specific purpose, are general revenues and should be reported by type of tax—for example, property taxes and sales taxes. All other nontax revenues that do not meet the criteria to be reported as program revenues should also be reported as general revenues.

General revenues are not always discretionary revenues. For example, even though motor vehicle revenues cannot be used for other than “road” purposes, they are still general revenues. Program revenues derive directly from the program itself or from parties outside the county's taxpayers or citizenry, as a whole; they reduce the net cost of the function to be financed from the government's general revenues. Motor vehicle revenues do not derive directly from the public works program itself, but rather they are restricted general revenues provided by law to finance the cost of specific programs.

The gain or loss on the sale of a fixed asset should be netted into general revenues as a miscellaneous revenue. Consideration should also be given to reporting the sale of a fixed asset as a special or extraordinary item if it fits the relevant criteria.

**REPORTING EXPENSES BY FUNCTION** – GASB 34 mandates that governments report their activities at least by function. That is to say, in the case of governmental activities, the level of detail required is that currently found in the governmental fund operating statement (e.g., “general government,” “public safety,” “public works”). For business-type activities, each segment (enterprise fund) is considered to be a function. (water, sewer, liquor, electric).

Each function should report all expenses that are clearly identified with it (i.e., direct expenses). Direct expenses include depreciation related to capital assets that can be specifically identified with a given function. This means that equipment should be sorted by function with the respective depreciation expense coded to each related function.

Interest on long-term debt is NOT a direct expense and should be reported as a separate function.

Depreciation expense that does not qualify as a direct cost (primarily buildings) should be reported as a separate line item in its own right. If a separate line is used, it should be made clear on the face of the statement that only unallocated amounts are included in that line.

Depreciation on infrastructure assets should be reported as a direct expense of the function normally associated with the acquisition and maintenance of infrastructure, or alternatively, as a separate line item.

PERMANENT FUND CONTRIBUTIONS – Contributions to permanent fund principal are to be reported as a separate revenue line in the general revenue section of the government-wide statement of activities. (cemetery perpetual care fund contributions)

GOVERNMENT-WIDE CONCLUSION – Perhaps the most striking feature of the new financial reporting model is the introduction of government-wide reporting. The new government-wide statement of net position will feature, among other things, the reporting of assets and liabilities previously reported in account groups, the reporting of infrastructure assets and a new classification structure for net position. The government-wide statement of activities will focus readers' attention on the net expense of a government's various functions, with a new line item for "special items" and the elimination of the traditional distinction between types of transfer accounts.

Depreciation expense will play a key role in the new government-wide statement of activities, consistent with the GASB's adoption of the economic resources measurement focus and the accrual basis of accounting for government-wide reporting.