

= Fund accounting =

Fund accounting is an accounting system emphasizing accountability rather than profitability, used by non @-@ profit organizations and governments. In this system, a fund is a self @-@ balancing set of accounts, segregated for specific purposes in accordance with laws and regulations or special restrictions and limitations.

The label, fund accounting, has also been applied to investment accounting, portfolio accounting or securities accounting? all synonyms describing the process of accounting for a portfolio of investments such as securities, commodities and / or real estate held in an investment fund such as a mutual fund or hedge fund. Investment accounting, however, is a different system, unrelated to government and nonprofit fund accounting.

= = Overview = =

Nonprofit organizations and government agencies have special requirements to show, in financial statements and reports, how money is spent, rather than how much profit was earned. Unlike profit oriented businesses, which use a single set of self @-@ balancing accounts (or general ledger), nonprofits can have more than one general ledger (or fund), depending on their financial reporting requirements. An accountant for such an entity must be able to produce reports detailing the expenditures and revenues for each of the organization 's individual funds, and reports that summarize the organization 's financial activities across all of its funds.

A school system, for example, receives a grant from the state to support a new special education initiative, another grant from the federal government for a school lunch program, and an annuity to award teachers working on research projects. At periodic intervals, the school system issues a report to the state about the special education program, a report to a federal agency about the school lunch program, and a report to another authority about the research program. Each of these programs has its own unique reporting requirements, so the school system needs a method to separately identify the related revenues and expenditures. This is done by establishing separate funds, each with its own chart of accounts.

= = State and local government funds = =

State and local governments use three broad categories of funds : governmental funds, proprietary funds and fiduciary funds.

Governmental funds include the following.

General fund. This fund is used to account for general operations and activities not requiring the use of other funds.

Special revenue (or special) funds are required to account for the use of revenue earmarked by law for a particular purpose. State and federal fuel tax revenues require special revenue funds, because federal and state laws restrict these taxes to transportation uses.

Capital projects funds are used to account for the construction or acquisition of fixed assets, such as buildings, equipment and roads. Depending on its use, a fixed asset may instead be financed by a special revenue fund or a proprietary fund. A capital project fund exists only until completion of the project. Fixed assets acquired and long @-@ term debts incurred by a capital project are assigned to the government 's General Fixed Assets and Long @-@ Term Debts.

Debt service funds are used to account for money that will be used to pay the interest and principal of long @-@ term debts. Bonds used by a government to finance major construction projects, to be paid by tax levies over a period of years, require a debt service fund to account for their repayment. The debts of permanent and proprietary funds are serviced within those funds, rather than by a separate debt service fund.

Permanent funds should be used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government? s programs? that is, for the benefit of the government or its citizenry.

Proprietary funds include the following .

Internal service funds are used for operations serving other funds or departments within a government on a cost @-@ reimbursement basis . A printing shop , which takes orders for booklets and forms from other offices and is reimbursed for the cost of each order , would be a suitable application for an internal service fund .

Enterprise funds are used for services provided to the public on a user charge basis , similar to the operation of a commercial enterprise . Water and sewage utilities are common examples of government enterprises .

Fiduciary funds are used to account for assets held in trust by the government for the benefit of individuals or other entities . The employee pension fund , created by the State of Maryland to provide retirement benefits for its employees , is an example of a fiduciary fund . Financial statements may further distinguish fiduciary funds as either trust or agency funds ; a trust fund generally exists for a longer period of time than an agency fund .

== Fixed assets and long @-@ term debts ==

State and local governments have two other groups of self @-@ balancing accounts which are not considered funds : general fixed assets and general long @-@ term debts . These assets and liabilities belong to the government entity as a whole , rather than any specific fund . Although general fixed assets would be part of government @-@ wide financial statements (reporting the entity as a whole) , they are not reported in governmental fund statements . Fixed assets and long @-@ term liabilities assigned to a specific enterprise fund are referred to as fund fixed assets and fund long @-@ term liabilities .

== Basis of accounting ==

The accrual basis of accounting used by most businesses requires revenue to be recognized when it is earned and expenses to be recognized when the related benefit is received . Revenues may actually be received during a later period , while expenses may be paid during an earlier or later period . (Cash basis accounting , used by some small businesses , recognizes revenue when received and expenses when paid .)

Governmental funds , which are not concerned about profitability , usually rely on a modified accrual basis . This involves recognizing revenue when it becomes both available and measurable , rather than when it is earned . Expenditures , a term preferred over expenses for modified accrual accounting , are recognized when the related liability is incurred .

Proprietary funds , used for business @-@ like activities , usually operate on an accrual basis . Governmental accountants sometimes refer to the accrual basis as " full accrual " to distinguish it from modified accrual basis accounting .

The accounting basis applied to fiduciary funds depends upon the needs of a specific fund . If the trust involves a business @-@ like operation , accrual basis accounting would be appropriate to show the fund 's profitability . Accrual basis is also appropriate for trust funds using interest and dividends from invested principle amounts to pay for supported programs , because the profitability of those investments would be important .

== Financial reporting ==

State and local governments report the results of their annual operations in a comprehensive annual financial report (CAFR) , the equivalent of a business 's financial statements . A CAFR includes a single set of government @-@ wide statements , for the government entity as a whole , and individual fund statements . The Governmental Accounting Standards Board establishes standards for CAFR preparation .

Governments do not use the terms profit and loss to describe the net results of their operations . The difference between revenues and expenditures during a year is either a surplus or a deficit .

Since making a profit is not the purpose of a government , a significant surplus generally means a choice between tax cuts or spending increases . A significant deficit will result in spending cuts or borrowing . Ideally , surpluses and deficits should be small .

= = Federal government funds = =

Federal government accounting uses two broad groups of funds : the federal funds group and the trust funds group .

= = = Federal funds group = = =

General fund . Technically , there is just one general fund , under the control of the United States Treasury Department . However , each federal agency maintains its own self @-@ balancing set of accounts . The general fund is used to account for receipts and payments that do not belong to another fund .

Special funds are similar to the special revenue funds used by state and local governments , earmarked for a specific purpose (other than business @-@ like activities) .

Revolving funds are similar to the Proprietary funds used by state and local governments for business @-@ like activities . The term , revolving , means that it conducts a continuing cycle of activity . There are two types of revolving funds in the Federal Funds Group : public enterprise funds and intragovernmental revolving funds. Public enterprise funds are similar to the enterprise funds used by state and local governments for business @-@ like activities conducted primarily with the public . The Postal Service Fund is an example of a public enterprise fund .

Intragovernmental revolving funds are similar to the internal service funds used by state and local governments for business @-@ like activities conducted within the federal government .

= = = Trust funds group = = =

Trust funds are earmarked for specific programs and purposes in accordance with a statute that designates the fund as a trust . Its statutory designation distinguishes the fund as a trust rather than a special fund . The Highway Trust Fund is an example of trust funds .

Trust Revolving Funds are business @-@ like activities , designated by statute as trust funds . They are , otherwise , identical to public enterprise revolving funds .

Deposit funds are similar to the agency funds used by state and local governments for assets belonging to individuals and other entities , held temporarily by the government . State income taxes withheld from a federal government employee 's pay , not yet paid to the state , are an example of deposit funds .

= = = Accounting basis and financial reporting = = =

The United States government uses accrual basis accounting for all of its funds . Its consolidated annual financial report uses two indicators to measure financial health : unified budget deficit and net operating (cost) / revenue .

The unified budget deficit , a cash @-@ basis measurement , is the equivalent of a checkbook balance . This indicator does not consider long @-@ term consequences , but has historically been the focus of budget reporting by the media . Except for the unified budget deficit , the federal government 's financial statements rely on accrual basis accounting .

Net operating (cost) / revenue , an accrual basis measurement , is calculated in the " Statements of Operations and Changes in Net Position " by comparing revenues with costs . The federal government 's net operating (cost) / revenue is comparable with the net income / (loss) reported on an income statement by a business , or the surplus / (deficit) reported by state and local governments .

= = Nonprofit organizations = =

Nonprofit organizations generally use the following five categories of funds .

Current fund ? unrestricted . This fund is used to account for current assets that can be used at the discretion of the organization 's governing board .

Current funds ? restricted use current assets subject to restrictions assigned by donors or grantors .

Land , building and equipment fund . Cash and investments reserved specifically to acquire these assets , and related liabilities , should also be recorded in this fund .

Endowment funds are used to account for the principal amount of gifts the organization is required , by agreement with the donor , to maintain intact in perpetuity or until a specific future date or event .

Custodian funds are held and disbursed according to the donor 's instructions .

= = = Basis of accounting and financial reporting = = =

The Report of Consolidated Financial Statements , used for annual financial reporting by nonprofit organizations , is similar to the CAFR used by state and local governments . However , nonprofit organizations use accrual basis accounting for their funds . A nonprofit 's financial statements generally include the following .

Statement of financial position or balance sheet . Similar to the balance sheet of a business , this statement lists the value of assets held and debts owed by the organization at the end of the reporting period .

Statement of activities or statement of support , revenue and expenses . This statement resembles the income statement of a business , but uses the terms excess or deficit rather than profit or loss . It shows the net results , by each fund , of the organization 's activities during the fiscal year reported . The excess or deficit is applied as a change in fund balances , rather than an increase or decrease in owner 's equity .

Statement of functional expenses distributes each expense of the organization into amounts related to the organization 's various functions . These functions are segregated into two broad categories : program services and supporting services . Program services are the mission @-@ related activities performed by the organization . Non @-@ program supporting services include the costs of fund @-@ raising events , management and general administration .

Statement of Cash Flows identifies the sources of cash flowing into the organization and the uses of cash flowing out during the reported fiscal year .

Standards for nonprofit financial statements are set by the Financial Accounting Standards Board . The Board 's most recent proposal , announced to the public on April 22 , 2015 , could establish new standards for financial performance and liquidity information available to donors and lenders .

= = Fund accounting fiscal cycle (fictitious example) = =

The following is a simplified example of the fiscal cycle for the general fund of the City of Tuscany , a fictitious city government .

= = = Opening entries = = =

The fiscal cycle begins with the approval of a budget by the mayor and city council of the City of Tuscany . For Fiscal Year 2009 , which began on July 1 , 2008 , the Mayor 's Office estimated general fund revenues of \$ 35 million from property taxes , state grants , parking fines and other sources . The estimate was recorded in the fund 's general ledger with a debit to Estimated Revenues and a credit to Fund Balance .

An appropriation was approved by the city council , authorizing the city to spend \$ 34 million from the general fund . The appropriation was recorded in fund 's general ledger with a debit to Fund Balance and a credit to Appropriations .

In subsidiary ledgers , the appropriation would be divided into smaller amounts authorized for various departments and programs , such as :

The complexity of an appropriation depends upon the city council 's preferences ; real @-@ world appropriations can list hundreds of line item amounts . An appropriation is the legal authority for spending given by the city council to the various agencies of the city government . In the example above , the city can spend as much as \$ 34 million , but smaller appropriation limits have also been established for individual programs and departments .

= = = Recording revenues = = =

During Fiscal Year 2009 , the city assessed property owners a total of \$ 37 million for property taxes . However , the Mayor 's Office expects \$ 1 million of this assessment to be difficult or impossible to collect . Revenues of \$ 36 million were recognized , because this portion of the assessment was available and measurable within the current period .

= = = Payroll expenditures = = =

The city spent a total of \$ 30 million on its employee payroll , including various taxes , benefits and employee withholding . A portion of the payroll taxes will be paid in the next fiscal period , but modified accrual accounting requires the expenditure to be recorded during the period the liability was incurred .

= = = Other expenditures = = =

The Public Works Department spent \$ 1 million on supplies and services for maintaining city streets .

= = = Closing entries = = =

At the end of the fiscal year , the actual revenues of \$ 36 million were compared with the estimate of \$ 35 million . The \$ 1 million difference was recorded as a credit to the fund balance .

The city spent \$ 31 million of its \$ 34 million appropriation . A credit of \$ 3 million was applied to the fund balance for the unspent amount .

When the current fiscal period ended , its appropriation expired . The balance remaining in the general fund at that time is considered unexpended . City government agencies are not allowed to spend the unexpended balance , even if their expenditures during the now @-@ ended fiscal period were less than their share of the expired appropriation . A new appropriation is necessary to authorize spending in the next fiscal period . (Liabilities incurred at the end of the fiscal period for goods and services ordered , but not yet received , are usually considered expended , allowing payment at a later date under the current appropriation . Some jurisdictions , however , require the amounts to be included in the following period 's budget .)

Instead of re @-@ applying the unspent balance from the general fund to the same programs , the city council may choose to spend the money on other programs . Alternatively , they may use the balance to cut taxes or pay off a long @-@ term debt . With a large surplus , reducing the tax burden will normally be the preferred choice .