



**HILLIARD
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*Certified Public Accountants * Certified Internal Auditors
Certified Government Auditing Professionals*

All Things Governmental

(An FYI Newsletter)

3rd Quarter 2010

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Fund Balance - GASB Statement No. 54

Statement of Governmental Accounting Standards No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, will significantly change the reporting of fund balance in the balance sheets of governmental type funds. Fund balance information provides one of the most widely used information in a government's financial reporting. The fund balance not only provides for crucial information for bond analysts, but is also used as an indicator of available liquid resources that can be used to pay long-term debt, reduce property taxes and expand government services.

GASB No. 54 represents a significant improvement in the reporting of fund balance by the five governmental funds which is composed of 1) the General Fund, 2)

Special Revenue Funds, 3) Capital Project Funds, 4) Debt Service Funds and 5) Permanent Funds.

Governmental funds are currently required to report fund balance in two categories:

- **Reserved Fund Balance** - reports appropriated dollars for which resources have already been committed.
- **Unreserved Fund Balance** - reports the residual amount that is still available for further expenditure and is sometimes further split into designated and undesignated.

The limitations of these definitions created confusion as well as inconsistencies in financial reporting. The issuance of GASB 54 will provide for improved trans-

parency and disclosures that will greatly benefit users of governmental financial statements.

Under GASB No. 54, fund balance will be divided into the following five classifications:

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Hilliard & Milton, LLC's mission is

To provide accounting, consulting, tax and attest services that distinguish us from our competition through our commitment to excellence as consistently reflected in timely personal attention to the well-being of our clients, respect for our clients and uncompromising integrity in client relations throughout every aspect of our practice.



Fund Balance - GASB Statement No. 54

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Nonspendable – reports funds which are not in a spendable form or are legally or contractually required to be maintained intact. Funds not in a spendable form include those associated with inventories, prepaid items and long term receivables. Principal of permanent funds is an example of an amount that is legally or contractually required to be maintained intact.

Restricted – reports funds that are restricted to specific purposes pursuant to the definition of restricted in GASB No. 34 relative to net assets. Fund balances are restricted when constraints are placed on their use by external creditors or parties, enabling legislation, or constitutional provisions.

Committed – reports funds which are committed for a particular purpose through a form of action of law of the government itself. The form or action should be imposed by the government's highest level of decision making such as the governing board. Funds remain committed until the government changes, or removes the commitment in the same form of action previously imposing the commitment.

Assigned – reports funds which

the governing body or delegated body or official have established to be used for a particular purpose. The assignment cannot exceed the total fund balance less its nonspendable, restricted and committed components. With the exception of the General Fund, other governmental fund's fund balances will be treated as assigned. Less formality is required to assign fund balance versus committing fund balance.



Unassigned – reports funds that do not meet any of the above definitions and represent fund balance that is available for any purpose. A positive balance is possible only in general funds. Deficit balances are possible in any governmental funds.

Not all governments will have all five components of fund balance. Governments should review their current policies and procedures to determine if resources would meet the definition of committed or as-

signed. Additional policies may need to be adopted or revised to be consistent with the new definitions.

Note Disclosures

Governments will be required to disclose more information about amounts reported in fund balance:

- Description of authority and actions that lead to committed and assigned fund balance.
- The government's policy regarding order of spending regarding restricted and unrestricted fund balance and the order of spending for committed, assigned and unassigned.
- For any stabilization arrangements, the authority for establishing, requirements for additions, and the conditions under which amounts may be used. If not reported on the face of the financial statements, the stabilization balance.
- Description of any formally adopted minimum fund balance policies.
- The purpose of each major special revenue fund and which revenues or other sources are reported in each of those funds.

- Encumbrances, if significant, are reported in conjunction with other disclosures of significant commitments.

Balance Reporting

Governments can choose where to disclose information about constraints placed on the different classifications of fund balance.

The information can be displayed on the face of the balance sheet, or only aggregate amounts can be reported with the constraints disclosed in the notes to financial statements.

For nonspendable fund balance, the amount not in spendable form and the amount that must be maintained intact must be disclosed separately. For restricted fund bal-

ance, major restricted purposes should be disclosed. Major specific purposes should also be disclosed on committed and assigned fund balance.

GASB 54 is effective for financial statements for periods beginning after June 15, 2010 with early implementation encouraged.

Common Errors in Financial Reporting

The Government Finance Officers Association's (GFOA) Certificate of Achievement for Excellence in Financial Reporting Program (CAFR Program) was started in 1945. The CAFR Program promotes the preparation of annual financial reports which go above and beyond the minimum requirements of generally accepted accounting principles. States and local governments that accomplish that goal are recognized with a certificate. As part of the CAFR Program the GFOA has published some common mistakes in financial reporting as follows:



Letter of transmittal

The date of the letter of transmittal should be no earlier than the date of the independent auditor's report as the CAFR is not ready to be transmitted until it has been audited.

Independent auditor's report

The independent auditor's report should offer an opinion on the fair presentation of the budgetary comparison if it is presented as a basic financial statement. Governments must present a budget to actual comparison for the general fund and major special revenue funds, either as required supplementary information (RSI) or as a basic financial statement.

Management's discussion and analysis (MD&A)

- The scope of the analysis provided in MD&A should be comprehensive and address all

of the following:



- Governmental activities and business-type activities
- The general fund and *other major funds*
- Variances between the final amended budget and actual and variances between the original budget and the final amended budget.

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Expertise, Peace of Mind. Courtesy of Hilliard & Milton, LLC

Our focus is and always has been on the success and potential of our clients and team. Our involvement with the community, our personal touch, and our passion for excellence are important aspects of our firm as we strive to help our clients succeed.



We offer a special **thank you** to our clients for allowing us to be of service to them and their continued trust. If you are pleased with our services we are grateful for any referrals you provide.

Hilliard & Milton, LLC

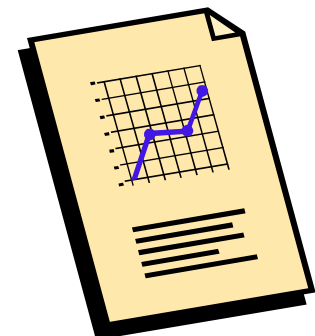
Our governmental services include:

- Financial audits, compilations and reviews
- Internal control reviews/recommended practices
- Policy and procedure development
- Single audits
- Financial statement preparation
- Corrective Action Plans
- Rpt of Local Government Finances preparation
- Grant Certification compliance
- Bond issuance services and compliance
- Audits of SPLOST revenues and expenditures
- Agreed-upon procedures
- Operational reviews and consulting
- Direct or Indirect Cost Allocation Plans
- Budgetary analysis and preparation
- Capital asset accounting and reporting
- Arbitrage tax information
- Payroll tax services
- Retirement plans
- Financial forecasting services
- Computer software and systems
- Financial planning and cash flow management
- Risk assessments
- Education and training

Common Errors in Financial Reporting

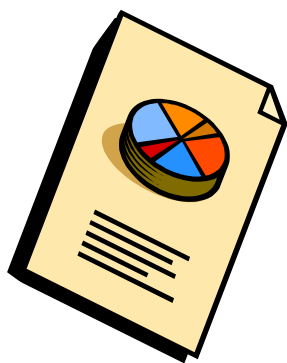
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- Provide analysis for significant changes from the prior year, not simply the amounts or percentages of change.
- Provide three years of condensed financial data if comparative financial statements are presented. Likewise, analysis needs to address not only changes between the current year and the prior year, but also changes between the prior year and the year preceding the prior year.
- Discuss significant capital asset and long-term debt activity during the year.



Government-wide statement of net assets

- Employers that fail to fully fund the annual cost of pension or other postemployment benefits (OPEB) must report an accounting liability for their cumulative under-funding of benefits (net pension/OPEB obligation).
- Accounting liabilities for pension benefits or OPEB should be reflected as long-term rather than current if the government presents a classified statement of net assets. If the government presents assets and liabilities based on their relative order of liquidity, the net pension obligation/net OPEB obligation should be reported as part of the subcategory due in more than one year within the appropriate liability category.



- Report debt net of related premiums and discounts.
- Calculate net assets invested in capital assets, net of related debt correctly. In calculating

this amount it is important to *exclude* all of the following:

- Unexpended bond proceeds
- Bond issuance costs
- Internal borrowings

The amount *should* however, include the following:

- Intangible capital assets
- Refunding bonds

Government-wide statement of activity

- Classify shared taxes correctly. Taxes raised by one government and then "shared" with another is only a tax from the perspective of the government that raised it. The government that obtains the shared tax revenue is, in substance, receiving a grant (i.e., a government-mandated or voluntary nonexchange transaction). If restrictions accompany the grant, as is often the case, it typically should be reported as program revenue rather than as general revenue.
- Report significant revenues on separate lines.
- Refrain from using the term capital outlay. Capital outlay expenditures are properly reported only in funds that use the current financial resources measurement focus and the modified accrual basis of ac-



counting.

- Report intergovernmental expenses in the appropriate functional category and not as a separate line item because they do not constitute a function.
- Ensure all major funds are reported correctly. GASB Statement No. 34, paragraph 76, sets a minimum threshold (based on two tests) at which a given governmental fund or enterprise fund must be reported as a major fund based on its relative size.
- Be sure that any reconciliations to the government-wide statement of activities focus on changes during the period.

Notes to the financial statements

- Describe the criteria used for identifying component units and discuss how component units are reported (blending or discrete presentation).

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Common Errors in Financial Reporting (Continued from Page 5)

- Properly disclose investment policies for each type of investment risk that is relevant in a particular government's circumstances or state that it has no such policy. For this purpose, the term policy is understood to apply solely to policies that have been formally adopted.
- Report changes in long-term liabilities gross rather than net. Reporting the net change (e.g., net increase in the amount owed for compensated absences) is not sufficient.
- Provide newly required pension disclosures in accordance with GASB Statement No. 50, Pension Disclosures. Disclosures must include all of the following in the notes to the financial statements:
 - The current year's data from the schedule of funding progress
 - A reference to the full schedule of funding progress
 - Actuarial assumptions used.
- Distinguish pension/OPEB cost from the annual required contribution. If an employer

reports a net pension/OPEB obligation, pension/OPEB cost will differ from the annual required contribution (ARC). Required note disclosures focus on pension/OPEB cost, whereas the schedule of employer contributions focuses on the ARC.

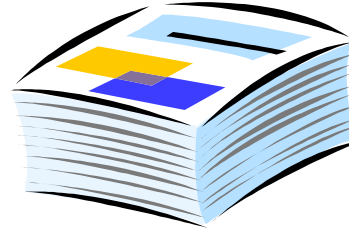
- Provide required note disclosure for pollution remediation in accordance with GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*.

Required supplementary information (RSI)

- Be sure the scope of budgetary comparisons is comprehensive but not excessive. Governments are required to present a budgetary comparison for the general fund and all major special revenue funds.
- Disclosures related to budgetary comparisons presented as RSI should be included in RSI as well, rather than within the notes to the financial statements. However, if there is

over-spending of an appropriation and the overspending is considered to be a significant "violation of finance-related legal provisions," appropriate disclosure should be made in the notes to the financial statements, even if the budgetary comparison itself is presented as RSI.

- Be sure the schedules of funding progress for pensions and OPEB contain all required data elements. The schedule must present both the actuarial value of plan assets and the actuarial accrued liability, not just the net unfunded actuarial accrued liability.



Let Us Know! : If you feel anyone would benefit from our newsletter, please let us know their contact information and we will be happy to add them to our mailing list!

Common Control Deficiencies

The information provided in this newsletter is for informational purposes only and should not be acted upon without first gathering additional information or obtaining professional assistance.

In accordance with Statement on Auditing Standards (SAS) No. 112, *Communicating Internal Control Related Matters Identified in an Audit* auditors are to communicate to those charged with governance *control deficiencies* categorized as **material weaknesses**, **significant deficiencies**, and **other matters**.

A **control deficiency** exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. Deficiencies can exist either in the design or operation of internal controls.

A **significant deficiency** is a control deficiency, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likeli-

hood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected.

A **material weakness** is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.

The following are examples of circumstances that may be deficiencies, significant deficiencies, or material weaknesses:

Deficiencies in the Design of Controls

- Inadequate design of controls over the preparation of the financial statements being audited.
- Inadequate design of controls over a significant account or process.
- Inadequate documentation of the components of internal control.
- Insufficient control consciousness within the organization; for example, the tone at the top and the control environment.
- Absent or inadequate segregation of duties within a significant account or process.

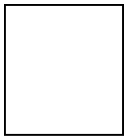
- Absent or inadequate controls over the safeguarding of assets (this applies to controls that the auditor determines would be necessary for effective internal control over financial reporting).
- Inadequate design of IT general and application controls that prevent the information system from providing complete and accurate information consistent with financial reporting objectives and current needs.
- Employees or management who lack the qualifications and training to fulfill their assigned functions. For example, in an entity that prepares financial statements in accordance with generally accepted accounting principles (GAAP), the person responsible for the accounting and reporting function lacks the skills and knowledge to apply GAAP in recording the entity's financial transactions or preparing its financial statements.

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www.hilliardmilton.com/governmental.htm

Common Control Deficiencies

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- Inadequate design of monitoring controls used to assess the design and operating effectiveness of the entity's internal control over time.
- The absence of an internal process to report deficiencies in internal control to management on a timely basis.

Failures in the Operation of Internal Control

- Failure in the operation of effectively designed controls over a significant account or process; for example, the failure of a control such as dual authorization for significant disbursements within the purchasing process.
- Failure of the information and communication component of internal control to provide complete and accurate output because of deficiencies in timeliness,

completeness, or accuracy; for example, the failure to obtain timely and accurate consolidating information from remote locations that is needed to prepare the financial statements.

- Failure of controls designed to safeguard assets from loss, damage, or misappropriation. This circumstance may need careful consideration before it is evaluated as a significant deficiency or material weakness.

