

*Manual of Accounting and Financial Reporting for  
Pennsylvania Public Schools*

**CHAPTER 3**  
**TABLE OF CONTENTS**

<b>Chapter 3</b>	<b>3.1</b>
Measurement Focus and Basis of Accounting	3.1
❖ Measurement Focus	3.2
❖ Basis Of Accounting	3.4

# Chapter 3

---

## Measurement Focus and Basis of Accounting

---

**\*\* Updated 1/3/05 \*\***

As shown in Chapter 2, a government uses different fund types to account for their government-type, business type, and fiduciary type activities. The objectives of the three fund classifications differ from one another with respect to each fund type's "measurement focus" and "basis of accounting." This Chapter will examine these differences and their effect on the financial statements.

❖ **Measurement Focus**

“Measurement focus” determines (1) which assets and which liabilities are included on a government’s balance sheet, and (2) whether an operating statement presents information on the flow of financial resources (revenues and expenditures) or information on the flow of economic resources (revenues and expenses).

For example, the operating statement of a proprietary fund is designed to answer the question “Is the fund better or worse off economically as a result of events and transactions of the period?” Events and transactions that improve the economic position of a proprietary fund are reported as “revenues” or “gains” in the operating statement. Those that diminish the economic position of a proprietary fund are reported as “expenses” or “losses.”

Governmental funds use a “flow of current financial resources” measurement focus. The operating statement of a governmental fund answers the question “Are there more or less resources that can be spent in the near future as a result of events and transactions of the period?” Increases in spendable resources are reported in the operating statement as “revenues” or “other financing sources.” Decreases in spendable resources are reported as “expenditures” or “other financing uses.”

<b>MEASUREMENT FOCUS</b>		
	<u>Governmental Funds</u>	<u>Proprietary &amp; Fiduciary Funds</u>
Measurement Focus	Flow of current financial resources	Flow of economic resources
Fundamental Question	More or less resources to spend in the near future?	Better or worse off economically?
Terminology for Increases	Revenues/Other Financing Sources	Revenues/Gains
Terminology for Decreases	Expenditures/Other Financing Uses	Expenses/Losses

**Chapter 3**

*Measurement Focus and Basis of Accounting*

**3.2**

**PRACTICAL EFFECTS OF THE DIFFERENCE OF MEASUREMENT  
FOCUS BETWEEN GOVERNMENTAL AND PROPRIETARY FUNDS**

<u>Transaction</u>	<u>Governmental Funds</u>	<u>Proprietary &amp; Fiduciary Funds</u>
Does the fund report the receipt of proceeds from long-term borrowings in the operating statement?	Yes	No
Does the fund report capital outlay in the operating statement?	Yes	No
Does the fund report the repayment of the principal of debt in the operating statement?	Yes	No
Does the fund report a charge for consumption of capital assets (i.e., depreciation)?	No	Yes
Does the fund defer and amortize disbursements over the benefiting period?	No *	Yes

\* *Exceptions are prepaid items and inventories accounted for using the "consumption" method.*

❖ **Basis Of Accounting**

Basis of accounting refers to the timing of when transactions are recognized in the accounts and reported in the financial statements. The basis of accounting is used to determine WHEN an accounting entry should be made. Different funds use different bases of accounting, in accordance with governmental accounting standards. The three recognized bases of accounting are:

<b>THREE BASES OF ACCOUNTING</b>			
	<u>Accrual Basis</u>	<u>Modified Accrual Basis</u>	<u>Cash Basis *</u>
<b>Timing of Revenue Recognition</b>	When earned, or in the case of unearned revenue, when the entity becomes entitled to it.	When measurable and available. **	When received in cash.
<b>Timing of Expenditure/Expense Recognition</b>	When the cost is incurred.	When the expenditure is incurred, if measurable. Interest on debt is recognized when it is due. Claims, judgments and compensated absences are recognized in the year they are liquidated from expendable available resources.	When paid in cash.

\* NCGA Statement 1 concludes that this is not an appropriate basis of accounting and reporting for governmental organizations.

\*\* “Measurable” means subject to reasonable estimation. “Available” means revenues are subject to collection within the current period or after the end of the period, but in time to pay liabilities outstanding at the end of the current period.

**PLEASE NOTE:**

Determining when revenues are available has caused some confusion for LEAs in the past. "Available" has been interpreted as one year, 90 days, 60 days, as well as other time frames. Codification Section P70 provides some guidance when recording property taxes and states that amounts collected within 60 days after the year-end which are used to finance current-period expenditures be recorded as available. Unfortunately, this guidance only applies to property taxes. It is the LEA's responsibility, therefore, to examine their revenues and corresponding liability if applicable, to determine whether the revenue is "available" at year end and susceptible to accrual. The LECS Comptroller's Office recommends that your LEA adopt a revenue policy to determine the "available" time period. The policy should be applied consistently in each period, but should also consider unusual and extraordinary items.

**Example:**

LEAs receive the fourth quarter retirement reimbursement in September (three [3] months after the year-end). However, this payment is received in time to pay the liability to PSERS and corresponds with salaries earned during the fiscal year. Therefore, the September retirement payment should be accrued as of June 30.

**NOTE:**

- Governmental Funds use modified accrual accounting.
  - Revenues are recognized when measurable and available to liquidate liabilities of the current period.
  - Expenditures are recognized when an event or transaction is expected to draw upon current spendable (not future) resources.
- Proprietary, Agency and Fiduciary funds use full accrual accounting.
  - Transactions and events are recognized when they occur, regardless of the timing of related cash flows.

A complete understanding of these concepts must be gained to recognize the differences in the manner events and transactions are accounted for in governmental funds and proprietary funds. In a later chapter of this manual, there will be detailed examples of specific events and transactions. These examples will include the accounting entries and the related explanations.

<b>MEASUREMENT FOCUS AND BASIS OF ACCOUNTING</b>		
	<u>Measurement Focus</u>	<u>Basis of Accounting</u>
Governmental Funds: <ul style="list-style-type: none"> <li>▪ General</li> <li>▪ Special Revenue</li> <li>▪ Capital Projects</li> <li>▪ Debt Service</li> <li>▪ Permanent</li> </ul>	Flow of Current Financial Resources	Modified Accrual
Proprietary Funds: <ul style="list-style-type: none"> <li>▪ Enterprise</li> <li>▪ Internal Service</li> </ul>	Flow of Economic Resources, i.e., Net Income	Accrual
Fiduciary Funds	Flow of Economic Resources	Accrual
Agency Funds	No Measurement	Accrual

<p>✓ <b>NOTE:</b> Agency funds do not have fund equity nor measurement focus.</p>
---

**GOVERNMENTAL FUND STRUCTURE, ACCOUNTING, AND REPORTING**

FUND CATEGORY	FUND TYPE	DEFINITION	EXAMPLE TRANSACTIONS EXPENDITURE REVENUE/EXPENSE	MEASUREMENT FOCUS	BASIS OF ACCOUNTING	FINANCIAL STATEMENTS REQUIRED
Governmental	General	To account for all governmental resources except those required to be accounted for elsewhere.	Taxes      Salaries	Current financial resources flow (revenues and expenditures)	Modified Accrual	Basic Financial Statements (BFS) Statement of Net Assets Statement of Activities Governmental Fund Balance Sheet Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balance Notes Reconciliation Statements
	Special Revenue	To account for proceeds of revenue sources legally restricted to expenditure for specified purposes.	Special Tax      Building Renovation See Section 690 of PA School Code, Sec. 1401 of PA Municipal Code and Accounting Manual.			
	Capital Projects	To account for financial resources to be used for acquisition of major capital facilities.	Bond Proceeds      Building Construction			
	Debt Service	To account for accumulation of resources for general long-term debt repayment.	Property Taxes      Bond Interest and Principal Repayment See Local Government Unit Debt Act, Act 1978-52.			
	Permanent Fund	To report resources that are legally restricted to the extent that only earnings and not principal may be used for the benefit of the government				
Proprietary	Enterprise	To account for operations financed and operated similar to businesses-services rendered to general public on a fee basis.	Food Service Revenue      Salaries	Economic resources flow (capital maintenance) (revenues and expenses).	Accrual	Statement of Net Assets Statement of Revenues, Expenses and Changes in Net Assets Statement of Cash Flows
	Internal Service	To account for the financing of goods or services provided by one department or unit to another department or to other governmental units on a cost reimbursement basis.	Computer Time Charges      Expenses of Operating Data Processing Center			
Fiduciary	Trust and Agency	To account for assets held by a governmental unit in a trustee capacity or as agency.	Endowment      Scholarship Award	Depends on objectives of fund.  Either: (1) Governmental or (2) Proprietary	Accrual or modified accrual, as appropriate.	As appropriate for governmental or proprietary type fiduciary funds. Statement of Fiduciary Net Assets Statement of Changes in Fiduciary Net Assets

GASB Statement #33, issued December 1998, establishes accounting and financial reporting standards for nonexchange transactions involving financial or capital resources (for example, most taxes, grants and private donations). The principal issue addressed in the statement is the *timing of recognition* of nonexchange transactions – that is, *when* (in which fiscal year) should an LEA recognize them in the financial statements?

LEAs receive a large portion of their revenues through nonexchange transactions, including property taxes, grants, and private donations. Until now, there has only been limited guidance as to how to report nonexchange transactions. GASB Statement #33 establishes more uniform recognition criteria to promote consistency and comparability in financial reporting.

In an *exchange* transaction, each party receives and gives up essentially equal values. Revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions should be recognized when the exchange takes place.

In an *nonexchange* transaction, an LEA gives (or receives) value without directly receiving (or giving) equal value in return. Revenues, expenses, assets and liabilities resulting from nonexchange transactions should be recognized in accordance with GASB *Codification* Section N590, “Nonexchange Transactions.” There are four (4) classes of nonexchange transactions:

1. *Derived tax revenues* resulting from assessments imposed on exchange transactions (for example, income taxes, other assessments on earnings or consumption).
2. *Imposed nonexchange revenues* result from assessments imposed on nongovernmental entities, including individuals, other than assessments on exchange transactions (for example, property taxes and fines).
3. *Government-mandated nonexchange transactions*, which occur when a government at one level provides resources to a government at another level and requires the recipient to use the resources for a specific purpose (for example, federal programs that state or local governments are mandated to perform).
4. *Voluntary nonexchange transactions*, which result from legislative or contractual agreements, other than exchanges, entered into willingly by the parties to the agreement (for example, certain grants and private donations).

GASB Statement #33 contains many examples on the application of accrual accounting to nonexchange transactions. Copies of GASB Statement #33 are available from the GASB.

The following chart from GASB Statement #33 summarizes the four (4) classes of nonexchange transactions and the timing of recognition required for each class.

## **Chapter 3**

### *Measurement Focus and Basis of Accounting*

#### **3.8**

## CLASSES AND TIMING OF RECOGNITION OF NONEXCHANGE TRANSACTIONS

<u>CLASS</u>	<u>RECOGNITION</u>
<p style="text-align: center;"><b>Derived Tax Revenues</b></p> <p>Examples: sales taxes, personal and corporate income taxes, motor fuel taxes, and similar taxes on earnings or consumption</p>	<p><b>Assets *</b></p> <p>Period when <i>underlying exchange has occurred</i> or when resources are received, whichever is first.</p> <p><b>Revenues</b></p> <p>Period when <i>underlying exchange has occurred</i>. (Report advance receipts as deferred revenues.) When modified accrual accounting is used, resources <i>also</i> should be “available.”</p>
<p style="text-align: center;"><b>Imposed Nonexchange Revenues</b></p> <p>Examples: property taxes, most fines and forfeitures</p>	<p><b>Assets *</b></p> <p>Period when an <i>enforceable legal claim has arisen</i> or when resources are received, whichever is first.</p> <p><b>Revenues</b></p> <p>Period when <i>resources are required to be used</i> or first period that use is permitted (for example, for property taxes, the <i>period for which levied</i>). When modified accrual accounting is used, resources <i>also</i> should be “available.” (For property taxes, apply NCGA Interpretation 3, as amended.)</p>
<p style="text-align: center;"><b>Government-Mandated Nonexchange Transactions</b></p> <p>Examples: federal government mandates on state and local governments</p> <p style="text-align: center;"><b>Voluntary Nonexchange Transactions</b></p> <p>Examples: certain grants and entitlements, most donations</p>	<p><b>Assets * and Liabilities</b></p> <p>Period when <i>all eligibility requirements have been met</i> or (for asset recognition) when resources are received, whichever is first.</p> <p><b>Revenues and Expenses or Expenditures</b></p> <p>Period when <i>all eligibility requirements have been met</i>. (Report advance receipts or payments for use in the following period as deferred revenues or advances, respectively. However, when a provider precludes the sale, disbursement, or consumption of resources for a specified number of years, until a specified event has occurred, or permanently [for example, permanent and term endowments], report revenues and expenses or expenditures when the resources are, respectively, received or paid and report resulting net assets, equity, or fund balance as restricted.) When modified accrual accounting is used for revenue recognition, resources <i>also</i> should be “available.”</p>

Printed with permission of the GASB, 401 Merritt 7,  
P.O. Box 5116, Norwalk, CT 06856-5116.