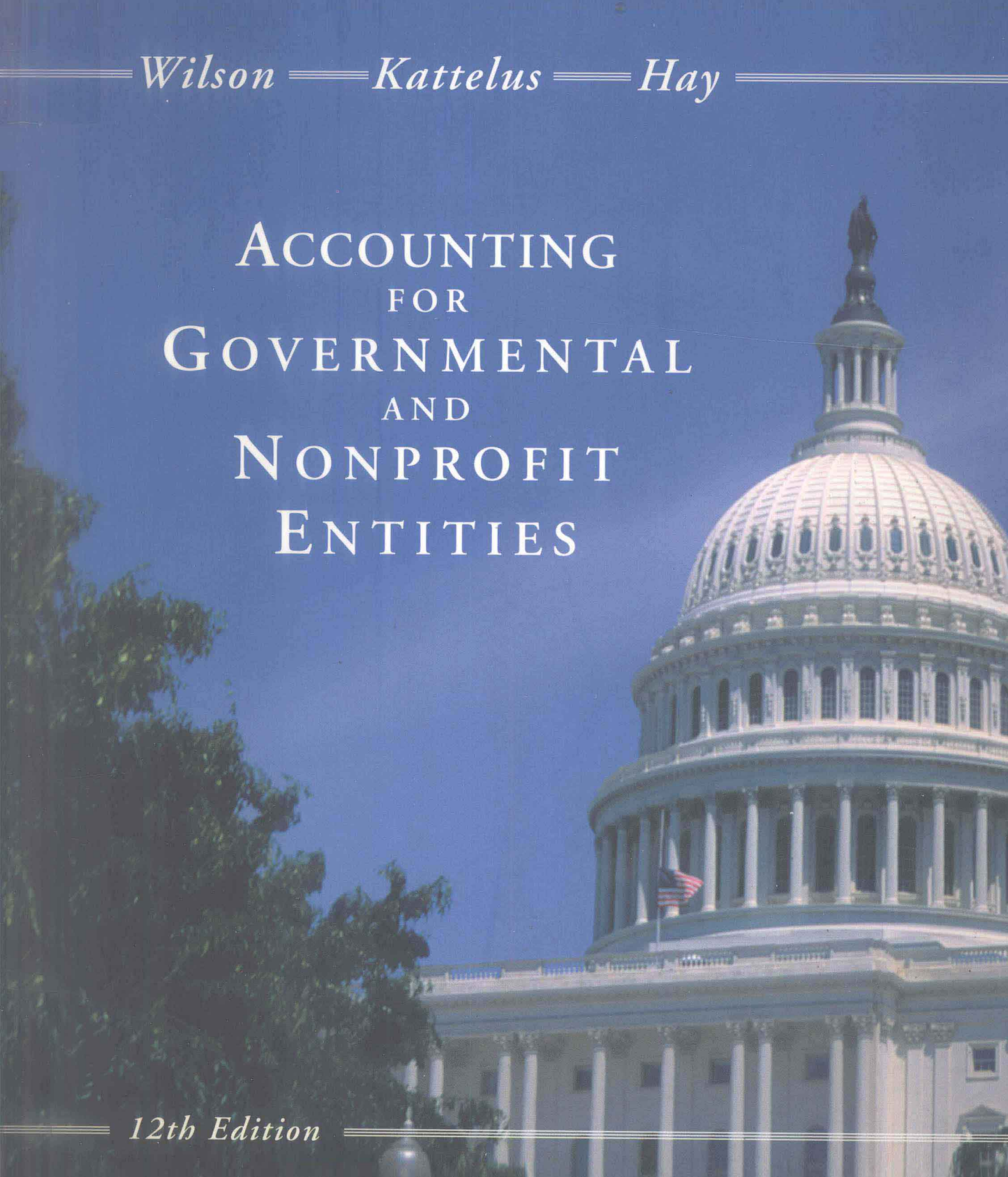


Wilson Kattelus Hay

ACCOUNTING
FOR
GOVERNMENTAL
AND
NONPROFIT
ENTITIES

12th Edition



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EDITION

Accounting for Governmental and Nonprofit Entities

Earl R. Wilson, Ph.D., CPA

*KPMG/Joseph A. Silvos
Distinguished Professor
University of Missouri–Columbia*

Susan C. Kattelus, Ph.D., CPA, CGFM

*Associate Professor
Eastern Michigan University*

Leon E. Hay, Ph.D., CPA, CGFM

*Distinguished Professor Emeritus
~~University of Arkansas–Fayetteville~~*



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Sponsoring editor: Steve Hazelwood

Editorial assistant: Angela Jacobs

Marketing manager: Richard Kolasa

Project manager: Scott Scheidt

Production supervisor: Rose Hepburn

Senior supplement coordinator: Cathy L. Tepper

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Preface

Honoring this book's tradition as the oldest and most comprehensive text on governmental and nonprofit accounting, we offer this revision as the first to fully integrate the GASB's new financial reporting models (GASB *Statement Nos.* 34 and 35, 1999). Educators and professionals have made this the leading text on the subject since 1951 because they can rely on it to be accurate and thorough and to incorporate the most effective pedagogy in teaching this complex topic. In this edition, we use "dual-track" accounting throughout the book to capture information necessary to prepare both government-wide and fund financial statements.

Professor R. M. Mikesell of Indiana University–Bloomington set the standard of excellence with the first two editions (1951, 1956). Dr. Leon E. Hay, then at Indiana University and later at the University of Arkansas–Fayetteville, joined Professor Mikesell in 1961 and continues through this edition to ensure that the text is the most accurate in the field. Dr. Earl R. Wilson of the University of Missouri–Columbia joined Dr. Hay with the ninth edition (1992). As a former member of the Governmental Accounting Standards Advisory Council and several task forces of the GASB and other professional organizations, he provides insight for the most up-to-date coverage in the field. Dr. Susan C. Kattelus of Eastern Michigan University joined with the 11th edition (1999) and adds her expertise in the area of nonprofit accounting as well as pedagogical tools, such as cases and Internet resources.

This edition incorporates changes in FASB, GASB, FASAB, AICPA, OMB, GAO, and other authoritative sources through the spring of 2000. The authors will continue the service of issuing to adopters of this text Update Bulletins that describe changes after the book is in print. These bulletins can be downloaded from Dr. Wilson's website, <http://www.missouri.edu/~accterw>. The authors welcome technical inquiries about the text, preferably by e-mail.

Many professors who were thanked by name in the Prefaces to earlier editions have continued to give generously of their time and effort in improving explanations in chapters of the text and improving the wording of questions, exercises, problems, and solutions. The authors gratefully acknowledge the following individuals who were particularly helpful with this edition of the text: Dr. Kenneth W. Brown of Southwest Missouri State University for Chapter 10 on the evaluation of financial performance; Robert Bramlett and Dr. James Patton of the Federal Accounting Standards Advisory Board, Bruce K. Michelson of the U.S. General Accounting Office, and J. Thomas Luter, formerly of the U.S. Department of the Treasury, for Chapter 12 on federal government accounting; and Dr. Mary L. Fischer of the University of Texas at Tyler and David Smarr of the University of Missouri–Columbia for Chapter 16 on colleges and universities. We gratefully acknowledge the support of our spouses, Florence J. Wilson, John T. Kattelus, and Bobbye S. Hay, CPA, who have contributed greatly to this and previous editions, both technically and personally.

The authors appreciate the courtesy of the Governmental Accounting Standards Board in giving permission to quote their pronouncements and reproduce illustrations from their publications. We are grateful to the Government Finance Officers Association, American Institute of Certified Public Accountants, and International City/County Management Association who granted permission for use of their materials.

Ancillary materials that accompany this text (also available on CD-ROM) include:

- Instructor's Guide and Solutions Manual (including teaching and case analysis tips)
- Power Point lecture presentations (which include 20 to 60 slides for each chapter)
- Test Bank (including a computerized version)
- City of Smithville Computerized Continuous Problem

Although we are extremely careful in checking the text and end-of-chapter material, it is probable that errors, inconsistencies, and ambiguities remain in this edition. As readers encounter errors of omission or commission in this text, we urge them to let us know so that corrections can be made. Additionally, every user of this edition who has suggestions or comments about the material in the chapters is invited to share them with either of the following two coauthors, either by regular mail or e-mail.

Dr. Earl R. Wilson
School of Accountancy
University of Missouri–Columbia
Columbia, MO 65211
wilsonea@missouri.edu
<http://www.missouri.edu/~accterw>

Dr. Susan C. Kattelus
Department of Accounting
Eastern Michigan University
Ypsilanti, MI 48197
susan.kattelus@emich.edu
http://www.online.emich.edu/~acc_kattelus

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CHAPTER

1

Financial Reporting for Governmental and Not-for-Profit Entities

Learning Objectives

After studying this chapter, you should be able to:

- ≈ Identify and explain the characteristics that distinguish governmental and not-for-profit entities from for-profit entities.
- ≈ Identify the authoritative bodies responsible for setting financial reporting standards for (1) state and local governments, (2) the federal government, and (3) not-for-profit organizations.
- ≈ Contrast and compare the objectives of financial reporting for (1) state and local governments, (2) the federal government, and (3) not-for-profit organizations.
- ≈ Distinguish management's discussion and analysis (MD&A), basic financial statements, and required supplementary information of state and local governments from their comprehensive annual financial reports.
- ≈ Explain the different objectives, measurement focus, and basis of accounting of the government-wide financial statements and fund financial statements of state and local governments.
- ≈ Explain why analysis of the financial performance of governmental and not-for-profit entities differs from that of for-profit entities.

What Are Governmental and Not-for-Profit Organizations?

Governmental and not-for-profit organizations are vast in number and diversity. In the United States, governments exist at the federal, state, and local levels and serve a wide variety of functions. The most recent census of governments reports 87,453 local governmental units, in addition to the federal government and 50 state governments. These 87,453 local governments consist of 3,043 counties, 19,372 municipalities, 16,629 towns and townships, 13,726 independent school districts, and 34,683 special district governments.¹

States, counties, municipalities (for example, cities and villages), and townships are **general purpose governments**—governments that provide many categories of services to their residents (such as police and fire protection; sanitation; construction and maintenance of streets, roads, and bridges; and health and welfare). Independent school districts, public colleges and universities, and special districts are **limited or special purpose governments**—governments that provide only a single function, or a limited number of functions (such as education, drainage and flood control, irrigation, soil and water conservation, fire protection, and water supply). Special purpose governments have the power to levy and collect taxes and to raise revenues from other sources as provided by state laws to finance the services they provide.

Not-for-profit organizations also exist in many forms and serve many different functions. Estimates of the number of not-for-profit organizations range from several hundred thousand to more than 1 million.² These include private colleges and universities, various kinds of health care entities, some libraries, museums, professional and trade associations, fraternal and social organizations, and religious organizations.

Distinguishing Characteristics of Governmental and Not-for-Profit Entities

Governmental and not-for-profit organizations differ in important ways from business organizations. Moreover, as you will soon learn, accounting and financial reporting for governmental and not-for-profit organizations are markedly different from accounting and financial reporting for businesses. An understanding of how governmental and not-for-profit organizations differ from business organizations is

¹U.S. Department of Commerce, Bureau of the Census, *1997 Census of Governments*, vol. 1, no. 1 (Washington, DC: U.S. Government Printing Office), p. v.

²The U.S. Bureau of the Census (1992 *Census of Service Industries*, SC92-S-1, Table 1b) reports that in 1992 there were 208,911 tax-exempt service organizations. This does not include, however, numerous other not-for-profit organizations such as religious organizations, labor unions, and political organizations. The total of tax-exempt not-for-profits numbers more than 1 million (1996–97 *Nonprofit Almanac: Dimensions of the Independent Sector*, Washington, DC).