



Municipal Technical Advisory Service
INSTITUTE *for* PUBLIC SERVICE

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Governmental Funds-Measurement Focus

Dear Reader:

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We hope this information will be useful to you; reference to it will assist you with many of the questions that will arise in your tenure with municipal government. However, the *Tennessee Code Annotated* and other relevant laws or regulations should always be consulted before any action is taken based upon the contents of this document.

Please feel free to contact us if you have questions or comments regarding this information or any other MTAS website material.

Sincerely,

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Governmental Funds-Measurement Focus

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To understand the procedures for accounting for capital assets in government, one should first understand the model used for the general fund and the different model used for enterprise funds.

The traditional model of governmental accounting is based on two concepts: the measurement focus and the basis of accounting. Notes to financial statements in all governmental audits detail these two concepts as they apply to the government unit being audited.

The general fund operating statement measures the flow of the government's current financial resources. Revenues in the form of taxes, fees and charges for services are recognized because they increase resources available for the budget year. Expenditure transactions are recognized on the operating statement because they decrease current financial resources available for spending in the budget year.

In the general fund, the focus is on current year revenues (resources) used to provide services through current year expenditures. This measurement focus is called the "current financial resources" focus simply because it recognizes transactions that increase or decrease the resources available for spending during the budget year. The general fund budget is based on this model.

In contrast to the current financial resources measurement focus, there is an economic resources measurement focus model that is used with enterprise funds. It is similar to the model used in private sector businesses. Examples of enterprise funds include water and sewer funds, natural gas funds and solid waste funds. These funds are not as concerned with available resources as they are with changes in net position (total assets minus total liabilities). Operating statements for these funds recognize transactions that increase or decrease the funds' total economic resources during the fiscal year.

This boils down to some significant accounting differences between the annual operating statements (income statements) produced by the two measurement focus models. The economic resources measurement focus model for enterprise funds does not report the issuance of debt in its operating statement. When debt (liability) is issued, an offsetting cash (asset) amount is received resulting in no change to net assets. With the current financial resources measurement focus of the general fund, the issuance of debt increases current resources available and, therefore, is recorded on the operating statement as an Other Financing Source.

Principal debt repayment is not shown on the operating statement of the enterprise fund. The principal portion of debt repayment does not change net position because the reduction in the amount of outstanding debt (liability) is offset by a reduction in cash (asset). In the general fund, a principal repayment is a decrease in current financial resources (decrease in assets) and is shown as an expenditure on the operating statement.

Spending for capital items does not change net position because cash is reduced (or debt is incurred) while another asset is increased by an offsetting amount. Hence, there is no recognition in the enterprise fund operating statement for acquiring assets. However, the same expenditure in the general fund is a reduction in cash (current resource) and is recognized in the general fund operating statement as an expenditure.

Depreciation is used to measure the degree to which an asset is used up over time and is shown on the operating statement of the enterprise fund. It is a non-cash expense derived by dividing the cost of an asset by its anticipated length of service. Depreciation does not affect the current financial resources of the general fund and, therefore, is not shown on its operating statement.

Now, under GASB 34, there are two financial presentations of the general fund in the annual financial report (audit), two balance sheets and two income statements. The difference in the two methods is reflected in the method of accounting for long-term assets and liabilities. Prior to GASB 34, under the general fund model all long-term assets were maintained "off the books" in something called a "general fixed asset account group." Likewise, long-term liabilities were recorded in a separate account group called "general long-term debt account group." These account groups were custodial in nature and not part of the audited financial statements.

Under GASB 34, a new *government-wide* financial report was created to convert the general fund current resources measurement to the economic resources measurement. Basically, this means adding

the long-term assets and liabilities of the local government to the current items, thereby creating new financial reports.

Since the traditional general fund current financial resources focus records only current revenues and expenditures, the balance sheet for these government funds does not include a provision for long-term assets or liabilities.

General fund expenditures for land, equipment, roads, buildings, and infrastructure are recorded simply as “capital outlay” expenditures. This is in agreement with the budget process. Conversely, payments for these items in an enterprise fund would be capitalized as land, equipment or other capital assets.

Under GASB 34, local governments now capture capital outlays in the capital asset accounting system (CAAS). This is not a fund, nor is it the old and very limited general fixed asset account group. It is a permanent addition to the financial records that enables tracking of capital assets. This long-term data is used in the government-wide financial reports.

Having two completely different financial statements for the general fund is confusing. A reconciliation must be included in the financial statements that shows how the governmental reports are related to the government-wide statements of net position and statement of activities.

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