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MEMORANDUM

TO: County Mayors/County Executives
Highway Superintendents
Directors of Schools
Finance Directors

FROM: James R. Arnette
Director

SUBJECT: Impact of Accounting Standard No. 54 on Fund Balance Reporting and Fund Type Definitions

We are issuing this memorandum to ensure that Tennessee county governments are aware of the issuance of Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions by the Governmental Accounting Standards Board (GASB), which is effective for the fiscal year beginning July 1, 2010. The GASB sets accounting and financial statement reporting standards that state and local governments must follow. This new statement establishes criteria for classifying fund balances of governmental funds into defined classifications and clarifies definitions for governmental fund types. This memorandum is divided into two sections: Fund Balance Reporting and Fund Type Definitions.

1. Fund Balance Reporting

Prior to Statement No. 54, the difference between assets and liabilities in governmental funds was referred to as "fund balance", which was divided into reserved and unreserved (designated and undesignated) portions. With the implementation of Statement No. 54, fund balance will be divided into nonspendable, restricted, committed, assigned, and unassigned portions. The various components of the new fund balance reporting are designed to indicate the extent to which a government is bound to honor constraints on the specific purposes

for which amounts in the fund can be spent. A brief description of the new fund balance components is noted below:

1. Nonspendable Fund Balance – includes amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact. Examples: inventories, prepaids, long-term amount of loans and notes receivable, and endowments.
2. Restricted Fund Balance – includes amounts restricted to specific purposes that are (a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or (b) imposed by law through constitutional provisions or enabling legislation.
3. Committed Fund Balance – includes amounts that can only be used for specific purposes pursuant to constraints imposed by formal action of the government's highest level of decision-making authority.
4. Assigned Fund Balance – includes amounts that are constrained by the government's intent expressed by the government's governing body or a body delegated by the governing body.
5. Unassigned Fund Balance – includes amounts that are not restricted, committed, or assigned to specific purposes. In other words, funds which may be spent for any purpose; however, this designation may only appear in the county's General Fund.

In summary, the new fund balance reporting will require the government to classify the equity section of their governmental funds' balance sheets into the above-noted components. The Division of County Audit has released a revision to the state mandated County Uniform Chart of Accounts to accommodate these revisions.

2. Fund Type Definitions

Statement No. 54 clarifies the definitions for governmental fund types, which include the General Fund, special revenue funds, capital projects funds, debt service funds, and permanent funds. A brief definition of the various governmental fund types is noted below:

1. General Fund – should be used to account for and report all financial resources not accounted for and reported in another fund.
2. Special Revenue Funds – should be used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects. This means the fund should have one or more specific restricted or committed revenues that are the foundation for the special revenue fund.
3. Capital Projects Fund – should be used to account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays.
4. Debt Service Funds – should be used to account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest.
5. Permanent Funds – should be used to account for and report resources that are restricted to the extent that only earnings, and not principal, may be used

for purposes that support the reporting government's programs that are for the benefit of the government or its citizenry.

In summary, the new fund type definitions restrict the use of a particular fund type by how its revenues are limited as to use. As governments begin their 2010-11 budget process, officials should analyze the funds they are maintaining and determine if the funds meet the definition of the fund types as defined by Statement No. 54. For example, in instances where a special revenue fund does not meet the new definition, the special revenue fund should be closed into the General Fund and accounted for through specific revenue/expenditure codes or accounted for as a separate department within the General Fund.

For a copy of Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, contact the Governmental Accounting Standards Board at www.gasb.org. Also, the Government Finance Officers Association issued a report entitled The New Fund Balance, which can be obtained from their office at www.gfoa.org.

Purchase of Capital Assets with Debt Service Funds

We have noted that some county governments have purchased capital assets directly from their debt service funds in-lieu-of issuing debt for the capital assets. The direct purchase of capital assets from debt service funds is not in conformance with GASB Statement No. 54. If a county government plans to purchase capital assets directly from the debt service fund please contact our office for an explanation of the guidance on how to handle this transaction. Counties should be cautious about the use of their debt service funds and the total of accumulated balances in their debt service funds since bond rating agencies include these as criteria as part of their rating analysis.

If you have questions, please contact the Division of County Audit, County Technical Assistance Services, or your public accounting firm.