

## **Chapter 2**

### **Fund Accounting**

#### **TRUE/FALSE (CHAPTER 2)**

1. A fund is a separate fiscal and accounting entity with a self-balancing set of accounts.
2. Fund accounting promotes control and accountability over restricted resources.
3. The basis of accounting determines what transactions and events are recognized.
4. An entity's measurement focus determines when transactions and events are recognized.
5. If an entity adopts a full accrual basis of accounting, its measurement focus will automatically be on all economic resources.
6. If an entity adopts a modified accrual basis of accounting, its measurement focus will automatically be on current financial resources.
7. A government may report some of its funds on a full accrual basis.
8. A government may have as many general funds as it deems necessary.
9. Funds divide a government into functional departments.
10. General funds are established to account for resources legally restricted for specified purposes.
11. Fiduciary activities only benefit parties other than the government itself.
12. The Financial Accounting Standards Board requires all nongovernmental not-for-profit entities to use fund accounting.

## MULTIPLE CHOICE (CHAPTER 2)

1. What is the primary reason that governmental entities use fund accounting?
  - a) Fund accounting is required by law.
  - b) Fund accounting is required by GAAP.
  - c) Fund accounting promotes control and accountability over restricted resources.
  - d) Fund accounting promotes better control over operating activities.
  
2. Basis of accounting determines which of the following?
  - a) When transactions and events are recognized.
  - b) What transactions and events will be reported.
  - c) Where transactions and events will be reported.
  - d) Why transactions and events will be reported.
  
3. A fund is
  - a) A separate legal entity.
  - b) A separate fiscal and accounting entity.
  - c) A separate self-balancing set of accounts for inventory purposes.
  - d) None of the above.
  
4. Which of the following funds is a fiduciary fund?
  - a) Permanent fund.
  - b) Agency fund.
  - c) Capital project fund.
  - d) Debt service fund.
  
5. When a governmental entity adopts a basis of accounting other than full accrual and a measurement focus that excludes long-lived assets and liabilities in its governmental fund types:
  - a) It is in violation of the law.
  - b) It is in violation of GAAP.
  - c) It has recorded transactions in accordance with standards for presentation in the fund financial statement required by the new GASB reporting model.
  - d) It has the ability to better measure the results of operations.
  
6. A city receives a donation from a citizen who specifies that the principal must be invested and the earnings must be used to support operations of a city-owned recreational facility. The principal of this gift should be accounted for in which of the following funds?
  - a) Trust fund.
  - b) Special revenue fund.
  - c) Permanent fund.
  - d) Internal service fund.
  
7. Which of the following is NOT a governmental fund?
  - a) City Hall Debt Service Fund.
  - b) City Utilities Enterprise Fund.
  - c) Gasoline Tax Special Revenue Fund.
  - d) City Hall Capital Project Fund.

8. Which of the following accounts would you least expect to see in a debt service fund?
  - a) Principal payments.
  - b) Interest charges.
  - c) Interest earned.
  - d) Outstanding balance of the debt being serviced.
  
9. Which of the following funds is a proprietary fund?
  - a) Internal service fund.
  - b) Special revenue fund.
  - c) Capital project fund.
  - d) Permanent fund.
  
10. Which of the following funds is a governmental fund?
  - a) Enterprise fund.
  - b) Debt service fund.
  - c) Internal service fund.
  - d) Agency fund.
  
11. Which of the following activities should the City of Highland account for in a trust fund?
  - a) General fund contributions received by the City pension plan.
  - b) Greens fees received from golfers at the City-owned golf course.
  - c) Grants received from the Federal government to purchase buses to be used for public transit.
  - d) Proceeds of bonds issued to construct a new city hall building.
  
12. The state collects a gasoline tax that must be used to support highway construction and maintenance. The gasoline tax should be accounted for in which of the following funds?
  - a) General fund.
  - b) Special revenue fund.
  - c) Debt service fund.
  - d) Internal service fund.
  
13. The City of San Jose built a new city hall and financed construction by issuing bonds due in installments over the next 30 years. The bond principal and interest will be paid by a special tax levied on property in the City. The money received from this special tax should be accounted for in which of the following funds?
  - a) General fund.
  - b) Special revenue fund.
  - c) Capital project fund.
  - d) Debt service fund.
  
14. Riverside Golf Course is a City-owned golf course that collects greens fees in amounts sufficient to cover its expenses. Riverside Golf Course should be accounted for in which of the following funds?
  - a) Internal service fund.
  - b) Enterprise fund.
  - c) General fund.
  - d) Special revenue fund.

15. To fulfill the printing needs of its various departments and agencies, the City has established a Central Print Shop which bills the various departments and agencies of the city for printing services rendered. The Central Print Shop should be accounted for in which of the following funds.
- a) Internal service fund.
  - b) Enterprise fund.
  - c) General fund.
  - d) Special revenue fund.
16. Which of the following funds is accounted for on the modified accrual basis of accounting?
- a) General fund.
  - b) Internal service fund.
  - c) Proprietary fund.
  - d) Pension trust fund.
17. Which of the following assets would NOT be found in the fund balance sheet of the General Fund of the City of Harrison?
- a) Cash.
  - b) Capital assets.
  - c) Receivable from Special Revenue Fund.
  - d) Receivable from State.
18. Which of the following liabilities would NOT be found in the fund balance sheet of the General Fund of the City of Marmaduke?
- a) Accounts payable.
  - b) Payable to the special revenue fund.
  - c) Deferred revenue.
  - d) Bonds payable, due in 5 years.
19. For which of the following entities is fund accounting mandated?
- a) American Hospital Association.
  - b) City of New York.
  - c) Grace Lutheran Church.
  - d) United Way.
20. Governments most commonly separate resources into funds to assure that they adhere to restrictions placed on them by
- a) legislators.
  - b) grantors.
  - c) donors.
  - d) all of the above.

## PROBLEMS (CHAPTER 2)

1. Assume that the City of Ft. Smith maintains its books and records in a manner that facilitates the preparation of the fund financial statements. For each of the following events indicate in which fund(s) of the City of Ft. Smith the event would be recorded and justify your fund selection.
  - a. The City collected property taxes levied for the general operations of the City.
  - b. The City collected property taxes levied to pay principal and interest on bonds issued several years in the past to construct a new fire station.
  - c. The City collected property taxes levied on a specific area of the City for the purposes of providing more frequent snow removal than is enjoyed by the rest of the City.
  - d. The City sold bonds to finance the construction of a new City Hall.
  - e. The City sold bonds to finance major renovations at the city-owned electric utility.
  
2. Assume that the City of Amber maintains its books and records in a manner that facilitates the preparation of the fund financial statements. Amber City maintains a general fund, a capital project fund, and a special revenue fund. During 2002, the City engaged in the following transactions. Record all transactions. Be sure to clearly indicate the fund in which the entry is made.
  - a. The City sold bonds, face value \$26 million, at par to finance the construction of a new City Hall.
  - b. The City purchased two new police cars at a total cost of \$50,000.
  - c. The City collected \$8,000 in taxes dedicated for the eradication of noxious weeds.
  - d. The City spent \$6,000 on pesticides for noxious weeds.
  - e. The City acquired a new tractor for \$75,000. The City paid \$20,000 in cash, and signed a \$55,000 note which is due in three years.
  
3. Assume that the Blackfoot County maintains its books and records in a manner that facilitates the preparation of the fund financial statements. Blackfoot County engaged in the following transactions during the current month. Prepare journal entries in the general fund to record these events.
  - a. Paid salaries to County employees, \$100,000.
  - b. Borrowed \$35,000 at a local bank to use to buy a County car.
  - c. Purchased an automobile for the use by County administrative officials, \$35,000.
  - d. Made a \$7,000 payment on the outstanding accounts payable.
  - e. Collected \$3,500,000 of the current property tax lavy.
  - f. Received a \$50,000 grant from the State to support general government activities.
  
4. For each of the following funds list the basis of accounting it should use, either modified accrual or full accrual.
  - a. General fund
  - b. Debt service fund
  - c. Internal service fund
  - d. Investment trusts
  - e. Private purpose trusts
  
5. For each of the following funds list the measurement focus it should use, either current financial resources or economic resources.

- a. General fund
- b. Special revenue funds
- c. Capital projects funds
- d. Enterprise funds
- e. Pension trusts

## **ESSAYS (CHAPTER 2)**

1. Why do governments and not-for-profit entities use fund accounting?
2. Governments use the modified accrual basis of accounting and a current financial resources measurement focus when presenting the fund financial statements of the governmental funds, but they use the accrual basis of accounting and the flow of economic resources for the government-wide financial statements. What is a basis of accounting? What is measurement focus? How does the selection of one affect the selection of the other?
3. For what purposes do governmental and not-for-profit entities use agency funds? What are the distinguishing characteristics of agency funds?
4. Briefly describe the three broad categories of activities that most general-purpose governments engage in.

## ANSWERS TO TRUE/FALSE (CHAPTER 2)

1. True
2. True
3. False
4. False
5. True
6. True
7. True
8. False
9. False
10. False
11. True
12. False



## ANSWERS TO MULTIPLE CHOICE (CHAPTER 2)

1. C
2. A
3. B
4. B
5. C
6. C
7. B
8. D
9. A
10. B
11. A
12. B
13. D
14. B
15. A
16. A
17. B
18. D
19. B
20. D

## ANSWERS TO PROBLEMS (CHAPTER 2)

### Problem 1

- a. General Fund. The general fund is used to account for the general activities of a governmental entity.
- b. Debt Service Fund. The debt service fund is used to account for payments of principal and interest on debt incurred to finance general government activities.
- c. Special Revenue Fund. The proceeds may only be used for snow removal. By accounting for these proceeds in a special revenue fund and accounting for the expenditures of the proceeds the entity can demonstrate compliance with the requirement and demonstrate accountability.
- d. Capital Project Fund. A new City Hall is a general government asset. The Capital Project Fund is used to account for the amassing of assets for the purpose of construction and/or acquisition of general government assets. It is also used to account for the construction and/or acquisition of those assets.
- e. Enterprise Fund. Normally, governments use enterprise funds to account for activities for which there are comparable activities in the private sector. If the electric utility is accounted for in an enterprise fund, all fixed assets and all long-term debt associated with those activities will be accounted for in the enterprise fund.

### Problem 2

- a. GENERAL FUND

Cash	\$26 million	
Bond proceeds		\$26 million
- b. GENERAL FUND

Expenditures	\$ 50,000	
Cash		\$ 50,000
- c. SPECIAL REVENUE FUND

Cash	\$ 8,000	
Revenue		\$ 8,000
- d. SPECIAL REVENUE FUND

Expenditures	\$ 6,000	
Cash		\$ 6,000
- e. GENERAL FUND

Expenditures	\$75,000	
Proceeds of note		\$ 55,000
Cash		20,000

Problem 3

a.	Expenditures	\$100,000	
	Cash		\$100,000
b.	Cash	\$ 35,000	
	Proceeds of notes		\$ 35,000
c.	Expenditures	\$ 35,000	
	Cash		\$ 35,000
d.	Accounts Payable	\$ 7,000	
	Cash		\$ 7,000
e.	Cash	\$3,500,000	
	Revenue or		\$3,500,000
	Property Tax Receivable		
f.	Cash	\$ 50,000	
	Revenue		\$ 50,000

Problem 4

- a. Modified Accrual
- b. Modified Accrual
- c. Accrual
- d. Accrual
- e. Accrual

Problem 5

- a. Current Financial Resources
- b. Current Financial Resources
- c. Current Financial Resources
- d. Economic Resources
- e. Economic Resources

## ANSWERS TO ESSAYS (CHAPTER 2)

1. Governmental and not-for-profit entities use fund accounting to demonstrate accountability. By segregating the assets, entities are able to demonstrate clearly that the assets were used for the intended purposes. By segregating certain activities, governments can better control the revenues and expenditures/expenses of these activities. It would not be uncommon for governments and not-for-profit entities to segregate assets whose use is restricted by outside donors, nor would it be uncommon for these entities to segregate the revenues and expenses of activities that are supposed to be self-supporting.
2. Basis of accounting determines WHEN transactions and events are recognized. Measurement focus determines WHAT is being reported upon. If an entity selects the cash basis of accounting, its measurement focus will necessarily be upon the flow of cash. If an entity selects full accrual accounting its measurement focus will, of course, be upon flow of economic resources. An entity must first decide WHAT assets and liabilities it wants to display and choose a basis of accounting that will then enable the entity to display those assets and liabilities.
3. Agency funds are used to account for assets that the government or not-for-profit entity holds temporarily for other parties. Agency funds are mechanisms for segregating, on financial reports, assets held for others to demonstrate accountability and stewardship. Because agency funds are merely lists of assets held for others, with a corresponding obligation to those parties, agency funds have no operating accounts and no equity accounts. Assets = liabilities is the accounting equation.
4. *Governmental activities* are those financed predominantly through taxes and intergovernmental grants.

*Business-type activities* are those financed predominantly through user charges.

*Fiduciary activities* are those for which the government acts as a trustee or agent for individuals, external organizations, or other governments.