



NORTH CAROLINA
DEPARTMENT OF STATE TREASURER
STATE AND LOCAL GOVERNMENT FINANCE DIVISION
AND THE LOCAL GOVERNMENT COMMISSION

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Memorandum #2010-23 **REVISED**

TO: Local Government Officials and Their Independent Auditors

FROM: Sharon Edmundson, Director, Fiscal Management

SUBJECT: GASB Statement No. 54 *Fund Balance Reporting and Governmental Fund type Definitions - Part 1 – Fund Type Definitions*

DATE: March 3, 2010, original issue date, September 29, 2010, revision date

Governmental Accounting Standards Board (GASB) has issued GASB Statement No. 54 *Fund Balance Reporting and Governmental Fund Type Definitions* that will be effective for fiscal periods that begin after June 15, 2010, meaning fiscal year ending June 30, 2011 for North Carolina governments. The statement has two major areas of discussion: Fund balance classifications and fund type definitions. The Fiscal Management section of the State and Local Government Finance Division is still having conversations with GASB on the fund balance classifications section of this statement; however, due to the potential impact on units of government's 2011 budget structure and/or systems, the staff of the LGC wanted to issue guidance on the Fund Type definitions portion of Statement No. 54 in time for 2011 budget preparation. This memo has been revised to include several interpretations based on questions generated by local governmental units.

Following are key phrases from statement no. 54 on fund type definitions that use bold to emphasize various points, followed by our assessment of the potential impact on units of government and their fiscal reporting.

General Fund

“The General Fund is used to account for and report all financial resources not accounted for and reported in another fund.”

We do not believe that this definition will have any significant impact on current definitions and reporting of the General Fund in North Carolina.

Special Revenue Funds

“Special revenue funds are 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.**” Currently units of government classify funds as special revenue if they have a specific revenue source and/or the funds are required to be spent for specific purposes. GASB Statement No. 54 states that Special Revenue Funds must have a specific **revenue source** that is the foundation for the fund. Funds that have only specific expenditure requirements but don’t have a specific revenue source may no longer be classified as special revenue funds.

Further clarification from GASB has helped us resolve some issues with certain funds, Emergency Telephone System Funds and Occupancy and Food Tax Funds in particular. These funds are discussed individually later in this memo. As a general rule, what we now believe is that the primary revenue source in a fund now classified as a Special Revenue Fund must be restricted or committed specifically for debt service or capital outlay before a fund must be reported as a Debt Service Fund or Capital Projects Fund, respectively.

North Carolina has two statutory funds for which the reporting will be affected by the new definition of Special Revenue Funds: the capital reserve fund and tax revaluation fund. A discussion of how each of these funds will be reported under the new statement follows. Additionally, units of government should review special revenue funds unique to their government to ensure they comply with the new special revenue definitions

Capital Reserve Funds

The new definition for Special Revenue Funds specifically prohibits funds that account for specific revenue sources that are restricted or committed to expenditures for debt service or capital projects. Under GASB Statement No. 54 a capital reserve fund will be reclassified to and reported as either a capital projects fund for capital outlay or to a fund where capital-related debt service is being paid. Reclassification as a Capital Project Fund will be the most common approach. The statute does allow the use of capital reserve funds for debt service so a few units will need to reclassify their capital reserve funds to either the General Fund or a Debt Service Fund depending on where they actually service their debt. It should be noted that nothing in GASB Statement No. 54 requires a unit of government to set up a debt service fund. Units are still allowed to pay debt out of the General Fund or the Debt Service Fund.

GASB Statement No. 54 does not prohibit the use of capital reserve funds; our General Statutes authorize the use of these funds. Statement No. 54 only provides guidance on how to classify and report these funds according to fund type. Under previous guidance they were reported as special revenue fund types; under new guidance they will be reported as capital projects, as part of the general fund or as a debt service based depending on how the moneys in the capital reserve fund are used.

Tax Revaluation Funds

Counties are required by G.S. 153A-150 to set aside funds for their tax revaluations. Most counties currently record these funds in a Special Revenue Fund in their financial reports and on their accounting systems. Units that currently show their tax revaluation fund as a Special Revenue Fund will have to meet two criteria in GASB Statement No. 54 to continue presentation as a special revenue fund: 1) **proceeds** must be from “**specific revenue sources**” and 2) resources must meet the definition of restricted or committed. By statute the governing board must take action for approval or amendments for these funds. The statute also limits use of these funds to revaluation purposes; therefore, a tax revaluation fund meets the GASB’s definition of committed. In order for units to meet the “proceeds of specific revenue sources” language in Statement No. 54 the governing board must name the specific source of funds to be used for tax revaluation. This is almost always property tax revenues; however the board must name the source in its budget resolution. If these two criteria are met, then units who currently classify this fund as a Special Revenue Fund may continue to do so. Tax revaluation funds that don’t meet both criteria will need to be combined with the General Fund for reporting purposes. The fund balance in the tax revaluation fund will be presented as committed in the General Fund balance. If the tax revaluation fund does meet the new Special Revenue Fund criteria, the unit of government needs to make sure that the property tax revenue or other specified revenue source is recorded directly into the tax revaluation fund as revenue and not recorded as a transfer from another fund. Special Revenue funds may have other resources in the fund; however, the restricted or committed proceeds of specific revenue sources are expected to comprise a substantial portion of revenue in the fund. Transfers in do not qualify as restricted or committed proceeds.

Attachment A provides an example of sections of a budget ordinance that has been modified to incorporate language that will allow the tax revaluation fund to remain a Special Revenue fund for reporting purposes.

Emergency Telephone System Fund (911)

We have had several requests for specific guidance about the fund classification of Emergency Telephone System Funds (ETS) under GASB Statement Number 54. Current statutory requirements dictate that these monies be used for specific purposes in the provision of 911 services. The statutes do not restrict the monies to capital outlay or debt service. Because the monies, while restricted to 911 use, can be used for capital and non capital purposes, the Fund does pass the test to remain a Special Revenue Fund. The fact that the unit chooses through their budget process to use funds for capital purposes does not mean that the Fund has to be reported as a capital outlay fund. We believe that all units should report their ETS Fund as a Special Revenue Fund.

Prepared Food and Occupancy Funds

A similar logic that was used to evaluate the Emergency Telephone System Funds also would apply to Prepared Food and Occupancy Funds. If a unit’s authorizing legislation allows for both capital and noncapital expenditures/expenses for prepared food and/or occupancy funds then these

funds can be classified as Special Revenue. The fact that a unit budgets this money for capital outlay and/or debt service does not dictate that the Fund be reported as a capital project or debt service fund.

Capital Projects Funds

“Capital projects funds are used to account for and report **financial resources** that are restricted, committed, or assigned to expenditure for **capital outlays**, including the acquisition or construction of **capital facilities** and **other capital assets**.”

Under the new definition, GASB clearly allows for the purchase or construction of capital facilities as well as other capital assets and also allows for the accumulation of funds to either purchase or construct capital assets.

Conclusion

GASB Statement No. 54 will change the way North Carolina governments report certain parts of their financial statements. GASB Statement Number 54 requires presentation changes. Units of government are not required to change how they budget for their funds. Many units desire to change their budget so that it will flow to their financial statements. Other units will prefer to continue to budget their funds as they currently exist, and simply report them as required by GASB Statement No. 54 in the financial statements. Any reclassifications that are made should be note disclosed and should not be considered prior period adjustments that predicate findings under SAS 115 and SAS 117. Further guidance will be issued on the effects of the Statement on reporting fund balance. If you have any questions or comments please contact Melinda Canady at (919) 807-2384 or via email at Melinda.canady@nctreasurer.com

ATTACHMENT A

SAMPLE BUDGET ORDINANCE
 (Outlines Modifications Necessary to Maintain Special Revenue Classification)

BE IT ORDAINED by the Board of Commissioners of Carolina County, North Carolina Section 1: The following amounts are hereby appropriated in the General Fund for the operation of the county government and its activities for the fiscal year beginning July 1, 20X1, and ending June 30, 20X2, in accordance with the chart of accounts heretofore established for this County:

General Government	6,278,901
Public Safety	7,090,414
Environmental Protection	1,017,860
Transportation	123,656
Economic and Physical Development	1,316,992
Human Services	23,776,951
Cultural and Recreational	2,312,261
Education	41,418,016
Debt Service	1,311,070
Transfer to Revaluation Fund	68,816
Residual Equity Transfer to Water and Sewer Fund	100,000
Total Appropriations	=84,814,937-68,816

In the General Fund the transfer to the Tax Revaluation Fund is eliminated. The result is that the total expenditures for the General Fund is reduced by the eliminated transfer.

Section 2. It is estimated that the following revenues will be available in the General Fund for the fiscal year beginning July 1, 20X1, and ending June 30, 20X2.	
Current year's real property taxes	=51,690,663-68,816
Current year's motor vehicle taxes	522,128
Prior years' real property taxes	1,957,860
Prior years' motor vehicle taxes	19,776
Penalties and interest on real property taxes	546,451
Penalties and interest on motor vehicle taxes	5,520
Local Option Sales Tax	12,482,335
Real estate transfer taxes	131,095
Privilege licenses	145,203
Payments in lieu of taxes	76,147
Beer and wine excise tax	690,363
Senior citizen tax exemption refunds	19,840
Food stamp tax reimbursement	3,128
State grants	7,351,288
Federal grants	5,114,584
Court facilities fees	1,421,584
Building permits and inspection fees	23,158
Register of Deeds	330,911
Rents, concessions, and fees	713,316

The General Fund revenue source is also reduced by amount of revenue that will now be recorded directly in the Special Revenue Fund; which in this example is property taxes. Under the new GASB guidance for Special Revenue Funds the core revenue source must be recorded directly in the special revenue fund and not be recorded as a transfer-in.

Jail fees	28,716
Ambulance fees	110,678
Recreation department fees	185,990
Investment earnings	1,032,500
Sale of materials	68,366
Miscellaneous	143,337
Total estimated revenues	=84,814,937-68,816
<p>Section 3. The following amounts are hereby appropriated in the Fire District fund for the operation of fire protection services for the fiscal year beginning July 1, 20X1, and ending June 30 20X2, in accordance with the chart of accounts heretofore established for this county:</p>	
Public safety - Fire District 1	9,800
Public safety - Fire District 2	11,000
Total appropriations	20,800
<p>Section 4. It is estimated that the following revenues will be available in the Fire District Fund for the fiscal year beginning July 1, 20X1, and ending June 30, 20X2:</p>	
Current Year Taxes	19,200
Prior years' taxes	1,500
Investment earnings	100
Total estimated revenues	20,800

It is the intent of the Board of Commissioners that Property Tax Revenues will be used to Fund the Tax Revaluation Fund for this fiscal year, all future fiscal years and has been the source for all past fiscal years.

Section 5. The following amounts are hereby appropriated in the Tax Revaluation Fund for the revaluation of property in Carolina County during the fiscal year beginning July 1, 20X1, and ending June 30, 20X2, in accordance with the chart of accounts heretofore established for this county:

General Government - Tax Revaluation

Section 6. It is estimated that the following revenues will be available to the Revaluation Fund for the fiscal year beginning July 1, 20X1, and ending June 30, 20X2:

Investment Earnings

~~Transfer from General Fund~~ Property tax

Appropriated Fund Balance

Total estimated revenues

	559,100
	9,600
	68,816
	480,684
	559,100

The transfer-in is changed to property taxes in this example as the source of revenue is recorded directly in the Special Revenue Fund under GASB 54.