1700—The Budget and Budgetary Accounting

References

Sources:

NCGAS 1, NCGAI 10, GASBS 34, GASBIG 2015-1, AICPA SLG 2002

See also:

Section 1200, "Generally Accepted Accounting Principles and Legal Compliance"
Section 1800, "Classification and Terminology"
Section 2400, "Budgetary Reporting"
Section 2900, "Interim Financial Reporting"

Standards

Statement of Principle

Budgeting and Budgetary Control

a. An annual budget(s) should be adopted by every governmental unit.
b. The accounting system should provide the basis for appropriate budgetary control.
c. A common terminology and classification should be used consistently throughout the budget, the accounts, and the financial reports of each fund or activity.

[NCGAS 1, ¶76; NCGAS 1, ¶123, as amended by GASBS 34, ¶15]

Introduction

.101 Budgeting is an essential element of the financial planning, control, and evaluation processes of governments. Every governmental unit should prepare a comprehensive budget covering all governmental, proprietary, and fiduciary funds for each annual (or, in some states, biennial) fiscal period. [NCGAS 1, ¶77]

.102 The manner in which budgetary control should be achieved and reported on differs significantly as between proprietary and governmental funds and, to a lesser extent, among the several types of governmental funds. [NCGAS 1, ¶78]

.103 In most states and complex municipalities, agencies and departments submit budget requests to the chief executive or the budget officer. The chief executive, at a prescribed time, delivers an executive budget to the legislative body. Subject to a variety of limitations and procedures, the legislative body acts on the budget through the passage of appropriation bills or ordinances. The chief executive may have varying amendatory or veto powers, but ultimately, appropriation bills or ordinances when signed into law establish expenditure and obligation authority. Such authority may subsequently be subject to allocation, allotment, transfer, modification, or supplementation. [NCGAI 10, ¶7]

.104 The budget commonly refers to the documents issued by the chief executive and/or the budget officer. However, the appropriated budget is the substance of the appropriation bills or ordinances enacted into law. There may be differences between the executive budget and the substance of the appropriations beyond those revisions that occur during the appropriation process. The executive budget may include organizations, programs, activities, and functions not subject to appropriation. Conversely, there may be governmental organizations, programs, activities, and functions subject to appropriation that are not included in the executive budget. [NCGAI 10, ¶8]

.105 On adoption, the expenditure estimates in the annual budget, as modified by the legislative body, are enacted into law through the passage of an appropriation act(s) or ordinance(s). The appropriations constitute maximum expenditure authorizations during the fiscal year, and cannot legally be exceeded unless subsequently amended by the legislative body. Unexpended and/or unencumbered appropriations may lapse at the end of a fiscal year or may continue as authority for subsequent period expenditures, depending on the applicable legal provisions. [NCGAS 1, ¶86]

Types of Budgets

Time Span of Budgets

.106 Defined in its most general sense, a budget is a plan of financial operation for a given period of time. Two types of budgets in terms of time span, annual budgets and long-term budgets, are commonly found in contemporary public financial administration. [NCGAS 1, ¶79]

.107 The *annual* budget authorizes, and provides the basis for control of, financial operations during the fiscal year. This is the type of budget recommended, whether or not required by law, and that should be appropriately controlled through the accounting system to assure effective budgetary control and accountability. [NCGAS 1, ¶80]

.108 *Long-term* budgets present estimates of revenues and expenditures or expenses (as appropriate) for a period of several years—usually four to six—and the proposed means of financing them. They are *planning* documents that typically emphasize major program or capital outlay plans, the latter being referred to as capital improvement programs or capital budgets. [NCGAS 1, ¶81]

Fixed and Flexible Budgets

.109 Budgets may also be categorized as either “fixed” or “flexible.” *Fixed* budgets embody estimates of specific (fixed) dollar amounts. *Flexible* budgets embody dollar estimates that vary according to demand for the goods or services provided. [NCGAS 1, ¶82]

Governmental Fund Budgeting and Budgetary Control

.110 The primary emphasis of the annual budgetary and appropriations process of most governmental units is on planning and controlling the financial operations of the governmental funds. For this reason, and because proprietary fund budgeting parallels that of business enterprises, this section addresses primarily governmental fund budgeting and budgetary control. [NCGAS 1, ¶83]

.111 Whereas the demand for goods and services largely determines the revenues available to finance proprietary funds, this is not the case with most activities financed and accounted for through governmental funds. To the contrary, the financial resources available to the governmental funds (through taxes, licenses, and so forth) during the period are substantially unrelated to the demand for the goods and services financed through them. [NCGAS 1, ¶84]

.112 The planning process involves determining the types and levels of services to be provided and allocating available resources among various government departments, programs, or functions. Fixed budgeting is found more often in practice than flexible budgeting, and the financial control and evaluation processes typically focus on assuring that these fixed expenditure limitations are not exceeded and on comparing estimated and actual revenues. [NCGAS 1, ¶85]

Levels of Budgetary Control and Authority

.113 The three possible levels of budgetary control and authority to which organizations, programs, activities, and functions may be subject are:

a. “Appropriated budget”; or
b. Legally authorized “nonappropriated budget” review and approval process, which is outside the “appropriated budget” process; or
c. Nonbudgeted financial activities, which are not subject to “appropriated budget” and the appropriation process or to any legally authorized “nonappropriated budget” review and approval process, but still are relevant for sound financial management and oversight.

[NCGAI 10, ¶10]

.114 The following definitions are applicable for the purposes of budgetary comparisons presented in basic financial statements or required supplementary information:

Executive Budget: The aggregate of information, proposals, and estimates prepared and submitted to the legislative body by the chief executive and the budget office.

Appropriated Budget: The expenditure authority created by the appropriation bills or ordinances that are signed into law and related estimated revenues. Appropriated budgets include both original and final budgets:

a. The *original budget* is the first complete appropriated budget. The original budget may be adjusted by reserves, transfers, allocations, supplemental appropriations, and other legally authorized legislative and executive changes *before* the beginning of the fiscal year. The original budget should also include actual appropriation amounts automatically carried over from prior years by law. For example, a legal provision may require the automatic rolling forward of appropriations to cover prior-year encumbrances.
b. The *final budget* is the original budget adjusted by all reserves, transfers, allocations, supplemental appropriations, and other legally authorized legislative and executive changes applicable to the fiscal year,

whenever signed into law or otherwise legally authorized.

Nonappropriated Budget: A financial plan for an organization, program, activity, or function approved in a manner authorized by constitution, charter, statute, or ordinance but not subject to appropriation and therefore outside the boundaries of the definition of "appropriated budget."

Budgetary Execution and Management: All other suballocations, contingency reserves, recisions, deferrals, transfers, conversions of language appropriations, encumbrance controls, and allotments established by the executive branch, without formal legislative enactment. These transactions may be relevant for various accounting control and internal reporting purposes, but are not part of the appropriated budget. [NCGAI 10, ¶11; GASBS 34, ¶6 and ¶130]

Governmental Fund Budgets—Basis of Accounting

.115 State constitutions, statutes, political subdivisions, charters, and local ordinances assign the responsibility of the budgeting process and establish budgetary authority. The scope and method of state and local government budgetary practices are outside the scope of financial reporting standards. [NCGAI 10, ¶6]

.116 Budgetary compliance is a paramount consideration in government. Ideally, the basis on which the budget is prepared should be consistent with the basis of accounting used. The basis on which the budget is prepared establishes the basis on which the accounts usually are maintained and the budgetary reports must be prepared. It is recommended that governmental fund annual budgets be prepared on the modified accrual basis. Many of the modifications or adaptations of the accrual concept in its application to governmental accounting and reporting are similar to typical governmental fund budgetary practices. Thus, often there will be few differences, if any, between the budgetary basis and the modified accrual basis. [NCGAS 1, ¶78 and ¶87]

.117 Preparation of the budget on the cash basis or another basis not consistent with generally accepted accounting principles (GAAP) complicates financial management and reporting. Where legal requirements dictate another basis, governmental units typically (a) maintain the accounts and prepare budgetary reports on the legally prescribed budgetary basis to determine and to demonstrate legal compliance, and (b) maintain sufficient supplemental records to permit presentation of financial statements in conformity with GAAP. [NCGAS 1, ¶88]

Budgetary Account Integration

.118 Formal budgetary accounting is a management control technique used to assist in controlling expenditures and enforcing revenue provisions. Although governmental fund accounting is often referred to as "budgetary accounting," budgetary accounting procedures *per se* do not affect revenue and expenditure measurement. Budgetary accounting techniques are an extremely important control aspect of accounting for general, special revenue, and similar governmental funds, because the annual budget is a legal compliance standard against which the operations of such funds are evaluated. Integration of budgetary accounts in fund ledgers is a useful procedural adaptation of the usual governmental fund accounting equation and system to serve important interim managerial control purposes. (Similar adaptations may readily be made, and sometimes are made, to provide budgetary control in private business accounting systems.) When their interim managerial control purposes have been served, the budgetary account balances are reversed in the process of closing the books at year-end. Budgetary accounting procedures thus have no effect on the financial position of a governmental fund or on the changes in its fund balance (financial position). [NCGAS 1, ¶89]

.119 The extent to which budgetary accounts should be integrated in the formal accounting system varies among governmental fund types and according to the nature of fund transactions. Integration is essential in general, special revenue, and other annually budgeted governmental funds that have numerous types of revenues, expenditures, and transfers. Judgment should be used in other circumstances. For example, full or partial budgetary account integration would be essential where numerous construction projects are being financed through a capital projects fund or where such projects are being constructed by the government's labor force. On the other hand, where such funds are used to finance one or a few "turnkey" projects adequately controlled by contracts with independent contractors, formal budgetary account integration might not serve a useful purpose. Likewise, it would not be necessary in controlling most debt service funds, where the amounts required to be received and expended are set forth in bond indentures or sinking fund provisions and few transactions occur each year. [NCGAS 1, ¶90, as amended by GASBS 6, ¶13]

Proprietary Fund Budgeting and Budgetary Control

.120 The nature of most operations financed and accounted for through proprietary funds is such that the demand for the goods and services provided largely determines the appropriate level of revenues and expenses. Increased demand for the goods or services causes a higher level of expenses to be incurred, but also results in a higher level of revenues. Thus, as in commercial accounting, flexible budgets—prepared for several levels of possible activity—typically are better for proprietary fund planning, control, and evaluation purposes than are fixed budgets. Ideally, the basis on which the budget is prepared should be consistent with the basis of accounting used. [NCGAS 1, ¶78 and ¶94]

.121 When formally adopted, the expense estimates of flexible budgets typically are not viewed as appropriations but as approved plans. Budgetary control and evaluation are affected by comparing actual interim or annual revenues and expenses with planned revenues and expenses at the actual level of activity for the period. [NCGAS 1, ¶95]

.122 Fixed dollar budgets typically are not adopted for proprietary funds. Thus, integration of fixed dollar budgetary accounts usually is neither necessary nor appropriate in proprietary fund accounting systems. [NCGAS 1, ¶96]

.123 In some instances, fixed dollar budgets are adopted for proprietary funds either because of local legal requirements or in order to control certain expenditures (for example, capital outlay). In such cases, it may be appropriate to integrate budgetary accounts into the proprietary fund accounting system in a manner similar to that discussed for governmental funds in paragraphs .118 and .119. [NCGAS 1, ¶97]

Common Terminology and Classification

.124 The budget, the accounts, and the financial reports are inseparable elements in the financial administration process. Terminology and classification consistency among them is essential to achieving viable accounting systems and comparable, unambiguous financial reporting. [NCGAS 1, ¶124]

Governmental Funds

.125 The budget determines the nature and scope of most governmental fund financial operations by setting the amounts and sources of estimated revenues and transfers in, on the one hand, and the amounts and purposes of authorized expenditures and transfers out, on the other. The accounts of several types of governmental funds record, in summary and detail, both the planned revenues, expenditures, and transfers and the actual transactions. In the absence of significant conflicts between legal provisions and generally accepted accounting principles, the financial statements summarize the results of financial operations and financial position as reflected in the accounts. Where legal provisions conflict with GAAP, legal-basis data typically are reflected in the accounts and are used as the starting point for deriving statements prepared in conformity with GAAP. [NCGAS 1, ¶125]

.126 Effective management control and accountability for governmental funds can best be achieved by using a common language and uniform classification system in financial planning, management, and reporting. To the maximum extent practicable, the suggested terminology and classifications presented in Section 1800 should be used consistently in all phases of budgeting, accounting, and reporting. [NCGAS 1, ¶126]

Encumbrances

.127 Encumbrances—commitments related to unperformed (executory) contracts for goods or services—often should be recorded for budgetary control purposes, especially in general and special revenue funds. Encumbrance *accounting and reporting* may be summarized as follows:

a. Encumbrance accounting should be used to the extent necessary to assure effective budgetary control and accountability and to facilitate effective cash planning and control.
b. Encumbrances outstanding at year-end represent the estimated amount of the expenditures ultimately to result if unperformed contracts in process at year-end are completed. Encumbrances outstanding at year-end do not constitute expenditures or liabilities.
c. Significant encumbrances should be disclosed in the notes to the financial statements by major funds and nonmajor funds in the aggregate in conjunction with required disclosures about other significant commitments. Encumbering amounts for specific purposes for which resources already have been restricted, committed, or assigned should not result in separate display of the encumbered amounts within those classifications. Encumbered amounts for specific purposes for which resources have not been previously restricted, committed, or assigned should not be classified as unassigned but, rather, should be included within committed or assigned fund balance, as appropriate, based on the definitions and criteria in paragraphs .171–.177 of Section 1800.
d. If performance on an executory contract is complete, or virtually complete, an expenditure and liability should be recognized rather than an encumbrance.

[NCGAS 1, ¶91, as amended by GASBS 54, ¶24]

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.701 Introduction

No questions assigned.

.702 Types of Budgets

No questions assigned.

.703 Time Span of Budgets

No questions assigned.

.704 Fixed and Flexible Budgets

No questions assigned.

.705 Governmental Fund Budgeting and Budgetary Control

No questions assigned.

.706 Levels of Budgetary Control and Authority

No questions assigned.

.707 Governmental Fund Budgets—Basis of Accounting

.707-1 Q—Some funds that are maintained as special revenue funds for accounting purposes do not meet the criteria for separate reporting in external financial statements and therefore should be presented as part of the general fund or a qualifying special revenue fund. Should the budgetary information relative to those funds be included in the general fund or qualifying special revenue fund budgetary comparison?

A—No. The information in the budgetary comparison should be the legally adopted budget for the general fund or major special revenue fund. The additional revenues and expenditures pertaining to the other funds result from perspective differences and should be explained in the reconciliation of budgetary information to generally accepted accounting principles information.

[GASBIG 2015-1, QZ.54.41]

.708 Budgetary Account Integration

No questions assigned.

.709 Proprietary Fund Budgeting and Budgetary Control

No questions assigned.

.710 Common Terminology and Classification

No questions assigned.

.711 Governmental Funds

No questions assigned.

.712 Encumbrances

No questions assigned.

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General Fund or Major Special Revenue Fund Budgets Not Legally Required

.801 If the government chooses to present its required budgetary comparison information in the basic financial statements, [disclosure that a budget is not adopted for the general fund or a major special revenue fund because it is not legally required and, therefore, presentation of budgetary comparison information is not required] should be made in the notes to the financial statements [to explain why what might appear to be required information is not part of the presentation]. [AICPA SLG 2002, ¶11.16 and ¶14.56, fn19]