

# Budgeting and Control

*Lcdo. Edwin Renán Maldonado, CPA, LL.M.©*

*Prim. Sem. 2016-17*

# Textbook: Government and Not-for-Profit Accounting, Granof

- This presentation contains information, in addition to the material prepared and provided by the professor, from the book Government and Not-for-Profit Accounting, 7<sup>th</sup>. Ed., Granof which is the textbook assigned for the course CONT 4059 – “Contabilidad para Entidades que no son Negocios” at the University of Puerto Rico, Río Piedras Campus.

# Purposes of Budget

# Purposes of Budget

- Budgets are to governments and not-for-profits what the sun is to the solar system.
- Trying to understand government and not-for-profit accounting without recognizing the centrality of the budget would be like trying to comprehend the earth's seasons while ignoring the sun.

# Purposes of Budget

1. Planning
2. Controlling and administering
3. Reporting and evaluation

# Purposes of Budget

1. **Planning: Comprises**
  - a. programming (determining the activities that the entity will undertake),
  - b. resource acquisition, and
  - c. resource allocation.

# Purposes of Budget

- 2. Controlling and Administering:** Budgets help ensure that resources are obtained and expended as planned.

# Purposes of Budget

- 3. Reporting and Evaluating:**
  - a. Budgets lay the foundation for end-of-period reports and evaluations.
  - b. Budget-to-actual comparison reveal whether revenue and spending mandates were carried out.
  - c. Budgets can facilitate assessments of efficiency and effectiveness.



# Types of Budget

# Types of Budget

1. Appropriation budgets
2. Capital budgets
3. Flexible budgets

# Types of Budget

## 1. Appropriation budgets

- a. A government's current or operating budget covers its general fund.
- b. Determines the amount of taxes and other revenues that must be generated to cover expenditures. By law, must be balanced.
- c. Optional in special revenue, debt service and project funds.

# Types of Budget

## 2. Capital budgets

- a. Focus on the acquisition and construction of long-term assets.
- b. In contrast to an appropriation budget, typically covers multiple years, often as many as five (5).

# Types of Budget

## 3. Flexible budgets

- a. Focus on expected revenues, expenses, and net income under different assumptions of volume.
- b. Use in Enterprise Funds (Business-type activity)
- c. A flexible budget is a form of “What if?”.

# Classification of Revenues and Expenditures

# Classification of Revenues and Expenditures

## Expenditures (Budgets)

# Classification of Revenues and Expenditures

## Expenditures (Budgets)

1. **By fund.**
  - *Ex. General fund, special revenue fund, etc.*
2. **By Organizational Unit**
  - *Ex. Police Department, Fire Department*
3. **By Function or Program (same objective)**
  - *Ex. Public safety, recreation*



# Classification of Revenues and Expenditures

## Expenditures (Budgets)

4. By **Activity** (line of work of a program).
  - *Ex. Public safety = Burglary investigation, vice patrol.*
5. By **Character** (fiscal period they are presumed to benefit)
  - *Ex. Operating expenses (current); Capital project (future); debt service (prior, current and future).*
6. By **Object** classification (type of item)
  - *Ex. Salaries; travel; repair*

# Classification of Revenues and Expenditures

## Revenues

# Classification of Revenues and Expenditures

## Revenues (Budgets)

- Revenues present less significant issues of classification. Most revenues are not designated for specific purposes. Therefore, their classification is relatively straightforward.

# Classification of Revenues and Expenditures

## Revenues (Budgets)

- Suggested major revenue sources classifications include:
  - *Taxes*
  - *Licenses and permits*
  - *Intergovernmental revenues*
  - *Charges for services*
  - *Fines and forfeits*



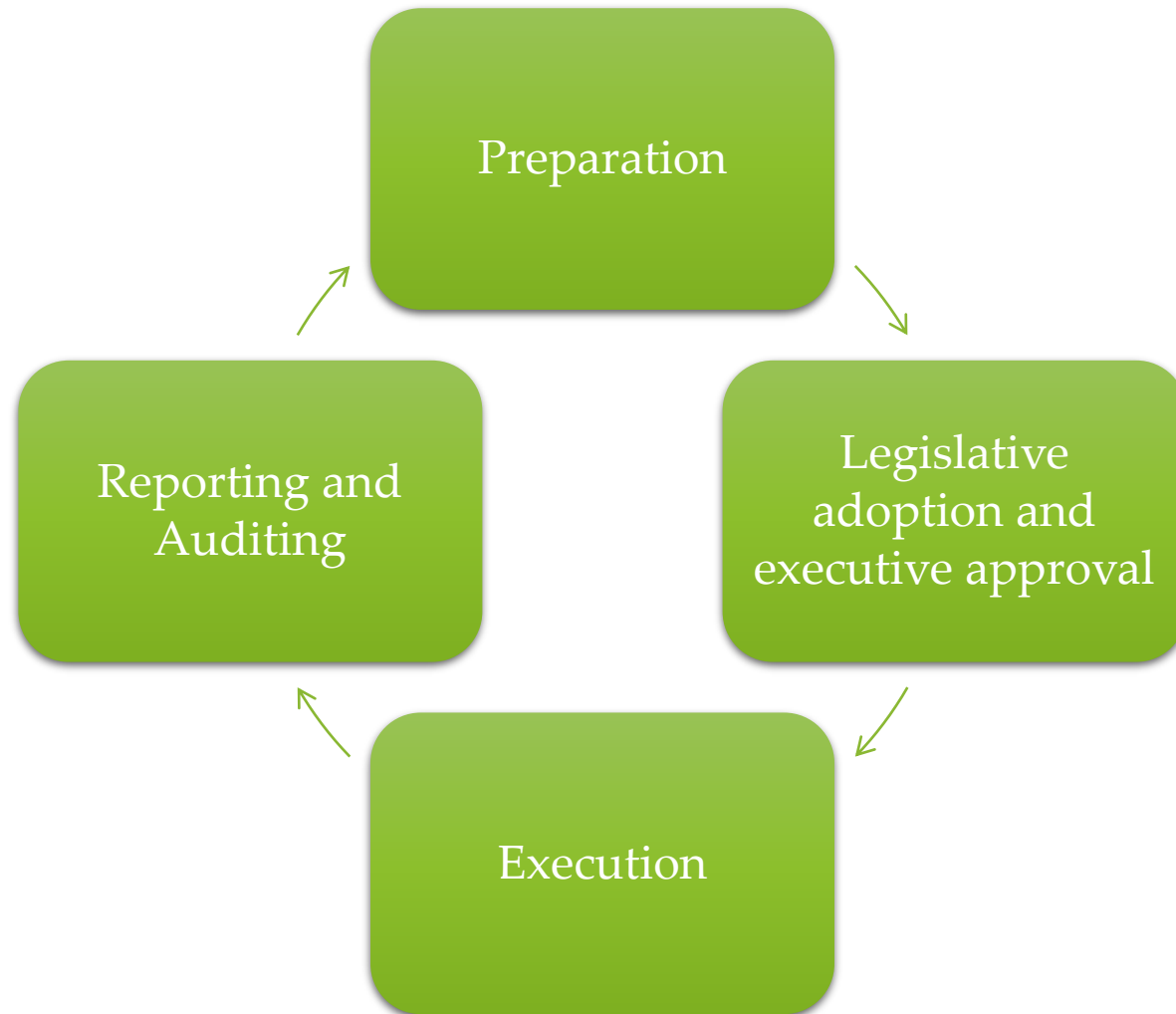
# Performance Budget

# Performance Budget

- Comprehensive performance budgeting systems require managers to specify objectives, consider alternative means of achieving them, establish workload indicators, and perform cost-benefit analysis.
- Most common type of performance budgets are **program budget**, whereby resources and results are identified with programs rather than traditional organizational units.

# Budget Cycle

# Budget Cycle





# Budget Cycle

- **Execution:**
  - The budget is executed (carried out) by an organization's executive branch.
  - In some jurisdictions, expenditures are assigned in particular months or quarters by **allotments** or **apportionments**.
  - Both **allotments** and **apportionments** are periodic allocations of funds to departments or agencies, usually made by the chief executive's office, to ensure that an entire year's appropriation is not dissipated early in the period covered by the budget.



# **Basis of Accounting are Budget Prepared**

## Basis of Accounting are Budget Prepared

- Budgetary principles are established either by individual governments or organizations or by the government or organizations that supervise them.
- *GASB and FASB do not established principles for budgeting.*

## Basis of Accounting are Budget Prepared

- GASB recommends that governments prepare their annual budgets for governmental funds on the modified accrual basis.
- However, many governments reject the GASB's advice, they opt to prepare budgets on a **cash basis** or a slightly modified cash basis.

## **Basis of Accounting are Budget Prepared**

- **Rationale for budgeting on cash basis:** bill must be paid with cash.
- **Adverse consequences of the cash basis:** May be decidedly unbalanced as to economic costs and revenues.



# Reporting Budgets

## Reporting Budgets

- The current GASB model requires governments to report their actual results and both their original and final appropriated budgets.
- The GASB encourages, but does not require, governments to present in a separate column the variances.



# Budgetary Control Features



## Budgetary Control Features

- By recording its budget, a government builds into its accounting system a gauge that warns of excesses in spending and deficiencies in collections.

## Budgetary Control Features

- The budgetary entries are reversed at year end and have no impact on year-end financial statements.
- To external report users, budgetary entries are irrelevant.



# Budgetary Entries

# Budgetary Entries

## Revenues and Expenses

- The government records its budget using an:
  - **Estimated revenue account**
  - **Appropriation account**
- The estimated revenue and appropriations accounts can be thought of as contra accounts to the actual revenue and expenditure accounts.

# Budgetary Entries

## Revenues and Expenses

### Revenues

- Estimated revenues (DR) – Actual Revenues (CR) =  
Revenues still to be recognized

### Expenses

- Appropriations (CR) - Actual expenditures (DR) =  
Balance available for expenditure

# Budgetary Entries

## Revenues and Expenses

Example (pg. 117)

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

1. A school district adopts a budget calling for travel revenues of \$400 million and total expenditures of \$390 million.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

1. A school district adopts a budget calling for travel revenues of \$400 million and total expenditures of \$390 million.

<b>Estimated revenues</b>	<b>400</b>	
<b>Fund balance</b>		<b>400</b>
<i>To record estimated revenues</i>		



# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

1. A school district adopts a budget calling for travel revenues of \$400 million and total expenditures of \$390 million.

**Fund balance**

**390**

**Appropriations**

**390**

*To record appropriations (estimated amount to be spent)*

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

#### 1. Budget

<i>Fund Balance</i>			
<i>Budget</i>	<i>390</i>		<u><i>400</i></u>
		<i>Bal.</i>	<i>10</i>

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

2. Suppose that during the year both revenues and expenditures were as estimated and that all transactions were for cash.

<b>Cash</b>	<b>400</b>	
<b>Revenues</b>		<b>400</b>
<i>To record revenues</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

2. Suppose that during the year both revenues and expenditures were as estimated and that all transactions were for cash.

<b>Expenditures</b>	<b>390</b>	
<b>Cash</b>		<b>390</b>
<i>To record expenditures</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

3. *Closing entries - budget.*

<b>Appropriations</b>	<b>390</b>	
<b>Fund balance</b>	<b>10</b>	
<b>Estimated revenues</b>		<b>400</b>
<i>To close budgetary accounts</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

#### 3. *Closing entries - budget*

<i>Fund Balance</i>			
<i>Budget</i>	<i>390</i>		<u><i>400</i></u>
		<i>Bal.</i>	<u><i>10</i></u>
<i>Closing</i>	<i>10</i>	<i>Bal.</i>	<u><i>0</i></u>

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

3. *Closing entries – Actual revenue and expenditures.*

<b>Revenues</b>	<b>400</b>	
<b>    Expenditures</b>		<b>390</b>
<b>    Fund balance</b>		<b>10</b>
<i>To close revenue and expenses</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

#### 3. Closing entries - budget

<i>Fund Balance</i>	
<i>Budget</i>	<u><i>400</i></u>
	<i>Bal.</i> <u><i>10</i></u>
<i>Closing (b)</i>	<i>Bal.</i> <u><i>0</i></u>
<i>Closing (a)</i>	<u><i>10</i></u>
	<i>Bal.</i> <i>10</i>



# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

4. Suppose alternatively that actual revenues were \$420 and actual expenditures were \$415.

Cash	420	
Revenues		420
<i>To record revenues</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

4. Suppose alternatively that actual revenues were \$420 and actual expenditures were \$415.

<b>Expenditures</b>	<b>415</b>	
<b>Cash</b>		<b>415</b>
<i>To record expenditures</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

5. *Closing entries - budget.*

<b>Appropriations</b>	<b>390</b>	
<b>Fund balance</b>	<b>10</b>	
<b>Estimated revenues</b>		<b>400</b>
<i>To close budgetary accounts</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

5. *Closing entries - budget*

<i>Fund Balance</i>			
<i>Budget</i>	<i>390</i>		<u><i>400</i></u>
		<i>Bal.</i>	<u><i>10</i></u>
<i>Closing</i>	<i>10</i>	<i>Bal.</i>	<u><i>0</i></u>

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

5. *Closing entries – Actual revenue and expenditures.*

<b>Revenues</b>	<b>420</b>	
<b>    Expenditures</b>		<b>415</b>
<b>    Fund balance</b>		<b>5</b>
<i>To close revenue and expenses</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 117)

5. *Closing entries - budget*

<i>Fund Balance</i>	
<i>Budget</i>	<u><i>400</i></u>
	<i>Bal.</i> <u><i>10</i></u>
<i>Closing (b)</i>	<i>Bal.</i> <u><i>0</i></u>
	<i>Closing (a)</i> <u><i>5</i></u>
	<i>Bal.</i> <i>5</i>

# Budgetary Entries

## Revenues and Expenses

### Alternative Methods

- Some governments maintain an account called budgetary control.
- Budgetary control is a temporary account to be used to record the budget instead of fund balance.
- This avoid contaminating the actual fund balance with appropriations and estimated revenues.
- See page 119.



# **Budgetary Entries Encumbrances**



# Budgetary Entries

## Encumbrances

- Governments and some not-for-profit record encumbrances to help prevent overspending the budget.
- The entry to record an encumbrance is usually prepared when:
  - A purchase order is issued.
  - A contract is signed.
  - A commitment is made.

# Budgetary Entries

## Encumbrances

- Most organizations do not encumber all anticipated expenditures.
- Many does not encumber salaries and wages because it is a routine recurring expenditure, or expenditure below a specific amount.

# Budgetary Entries

## Encumbrances

- The entry to record an encumbrance reduces the budgeted amount available for expenditures (as if the amount had already been spent).
- Concurringly designates a portion of what would otherwise be unassigned fund balance as committed or assigned for encumbrances.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

As of January 1, a state university general fund balance sheet shows the following:

Cash	<u>\$5,000</u>
------	----------------

Fund balance – unassigned	<u>\$5,000</u>
---------------------------	----------------

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

As of January 1, a state university general fund balance sheet shows the following:

Fund Balance	
1/1/X1	5,000

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

1. A state university contracts for repair services that it estimates will cost \$5,000.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

1. A state university contracts for repair services that it estimates will cost \$5,000.

Encumbrances	5,000	
Reserve for encumbrances		5,000
<i>To encumbered \$5,000 for repair services</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

Encumbrances	5,000	
Reserve for encumbrances		5,000
<i>To encumbered \$5,000 for repair services</i>		

\* **Encumbrances account** is not an expenditures, but, it is similar to an expenditure in that at year-end any remaining balance is closed to unassigned fund balance.



# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

Encumbrances	5,000	
Reserve for encumbrances		5,000
<i>To encumbered \$5,000 for repair services</i>		

\* The **Reserve for Encumbrances account** is a balance sheet account (a commitment of fund balance).

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

**Encumbrances**

---

**5,000**

**Reserve for Encumbrances**

---

**5,000**

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

2. The repairs are completed and, as anticipated, the university is billed for \$5,000.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

2. The repairs are completed and, as anticipated, the university is billed for \$5,000.

Expenditure	5,000	
Accounts payable		5,000
<i>To record repair expenditure</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

2. The repairs are completed and, as anticipated, the university is billed for \$5,000.

Reserve for encumbrances	5,000	
Encumbrances		5,000
<i>To reverse the encumbrance entry upon receipt of services</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 120)

#### Encumbrances

	<u>5,000</u>	5,000
Bal.	0	

#### Reserve for Encumbrances

5,000	<u>5,000</u>
Bal.	0

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

3. The contractor completes only 40% of the repairs and accordingly bills the university for only \$2,000.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

3. The contractor completes only 40% of the repairs and accordingly bills the university for only \$2,000.

<b>Expenditure</b>	<b>2,000</b>	
<b>Accounts payable</b>		<b>2,000</b>
<i>To record repair expenditure</i>		





# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

#### Encumbrances

<u>5,000</u>	2,000
Bal. 3,000	

#### Reserve for Encumbrances

2,000	<u>5,000</u>
Bal. 3,000	

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

3. Closing entry – year end: All temporary accounts are closed.

<b>Fund balance - unassigned</b>	<b>5,000</b>	
<b>Expenditures</b>		<b>2,000</b>
<b>Encumbrances</b>		<b>3,000</b>
<i>To close expenditures and encumbrances</i>		

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

Encumbrances	
<u>5,000</u>	2,000
Bal. 3,000	
Closing	→ 3,000
Bal. 0	

Reserve for Encumbrances	
2,000	<u>5,000</u>
Bal. 3,000	

Presented at balance sheet: Assigned or Committed Fund Balance.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

As of January 1, a state university general fund balance sheet shows the following:

Fund Balance			
12/31/X1	5,000	1/1/X1	<u>5,000</u>
			0

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 122)

4. At the end of the first year (the start of the second), the University had \$3,000 of outstanding commitments for repairs.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 122)

4. At the end of the second year (the start of the second), the University had \$3,000 of outstanding commitments for repairs. The university must restore the encumbrances and the appropriations.

**Encumbrances**

**3,000**

**Fund balance - unassigned**

**3,000**

*To restore encumbrances at the start of the new year.*

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

As of January 1, a state university general fund balance sheet shows the following:

Fund Balance			
12/31/X1	5,000	1/1/X1	<u>5,000</u>
			0
		1/1/X2	3,000



# Budgetary Entries

## Revenues and Expenses

### Example (pg. 122)

5. Contractor completes the repair.

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 122)

5. Contractor completes the repair.

Expenditures	3,000	
Account payable		3,000

*To record repair expenditures.*

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 122)

5. Contractor completes the repair.

Reserve for encumbrances	3,000	
Encumbrances		3,000

*To reverse the encumbrances entry upon the contractor's completion of the remaining \$3,000 of repairs.*

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 122)

5. Closing entry at year end.

Fund balance - unassigned	3,000	
Expenditures		3,000

*To close expenditures.*

# Budgetary Entries

## Revenues and Expenses

### Example (pg. 121)

As of January 1, a state university general fund balance sheet shows the following:

#### Fund Balance

12/31/X1	5,000	1/1/X1	<u>5,000</u>
			0
12/31/X2	3,000	1/1/X2	<u>3,000</u>
			0