

APIPA 2020 – How to Read Government Financial Statements

Exercise 1: Audit Problems

Each item below represents a problem encountered in an audit.

For each item: Identify

- The type of problem: GAAP departure or Scope limitation.
- The type of audit opinion that might result: Unmodified, modified, adverse, disclaimer
- The financial statement opinion affected: Governmental activities, aggregated discretely presented component units, major fund, aggregate remaining fund information.

<i>Audit problem</i>	<i>Type of problem</i>	<i>Type of audit opinion</i>	<i>FS opinion affected</i>
1. The component unit's column does not include the financial statements of the Healthcare Corporation.			
2. Management has not adopted GASB Statement No. 68, Accounting and Financial Reporting for Pensions. The government has not recorded pension expense, related net pension asset or liability, deferred outflows of resources, and deferred inflows of resources.			
3. The Government has not recorded a liability for land leases and related claims payable in the governmental activities and the General Fund and has not recorded the current period expense.			
4. The financial statements do not include financial data for the Fishing Authority, a component unit.			
5. The financial statements for the Technology Park have not been audited. The Park's financial activities have been included in the basic financial statements as discretely presented component units.			
6. The Government's aggregate remaining financial information does not include the financial statements of the Settlement Fund, a fiduciary fund component unit.			

Exercise 2: Internal Control and Compliance Findings

Each item below represents an internal control or compliance problem encountered in a Single Audit.

For each item: Identify

- The type of problem: Internal Control over Financial Reporting (ICFR) or Compliance (C).
- How to fix the problem
- How long it will take to fix the problem
- Whose responsibility it is to fix the problem

Problem #1: Management Estimates

Criteria & Condition: The Government's operations are complex and many accounts require management estimation and judgment. GAAP requires that management analyze and assess the reasonableness of such accounts on a recurring basis. Multiple audit adjustments were required to correct errors in these accounts. One example is the compensated absences liability account which is not being properly tracked and adjusted.

Cause: There are no formal policies or procedures in place to analytically review each management estimate account, or to assess large, unusual transactions.

Effect: The Government's financial statements are not fairly presented on a monthly or interim basis.

Recommendation: We recommend that policies and procedures governing management estimate accounts be formally documented. There should be a robust analysis and detailed support for each calculation and transaction. This function should be performed by a senior accountant or appropriate departmental staff person with review and oversight by a qualified individual. Certain accounts may lend themselves to quarterly or even monthly review.

Type of problem:

How to fix it:

How long it will take:

Whose responsibility is it?

Problem #2: Procurement

Criteria & Condition: Procurement transactions are required to be conducted in a manner providing full and open competition. Price quotations sent to vendors included requirements for a particular brand name, product, or feature of a product, peculiar to one manufacturer, thereby precluding consideration of an equivalent product manufactured by another company.

Cause: The Government is not consistent in applying applicable procurement requirements.

Effect: The Government is in potential noncompliance with procurement regulations and questioned costs of \$75,000 have resulted.

Recommendation: The Government should follow and document full and open competition procedures in accordance with applicable procurement regulations.

Type of problem:

How to fix it:

How long it will take:

Whose responsibility is it?

Problem #3: Compensated Absences

Criteria & Condition: Accrued leave is limited to 45 days or 360 hours. Accrued annual leave for separated employees should be identified and reviewed for validity. As of year-end, compensated balances payable included \$100,000 of accrued leave for inactive, terminated, resigned, or retired employees. The balance also included \$755,000 accrued leave in excess of the 45-day/360-hour limit. Individual debit balances of \$100,000 were also present.

Cause: The Government lacks adequate procedures and controls to determine that accrued annual leave is reviewed for validity and lacks timely updates of payroll records.

Effect: Compensated absences payable and related expenditures could be misstated.

Recommendation: Responsible personnel should record valid charges as compensated absences payable.

Type of problem:

How to fix it:

How long it will take:

Whose responsibility is it?

Exercise 3: Loan Approval

Assume that you are the loan officer for the Pacific Region Development Bank. The Island Government is seeking a \$5 million, 20-year loan to construct a new administrative center.

The audited financial statements for Island Government provide the following information:

From the **Statement of Activities**:

Revenues from taxes and fees	\$3,800,000
Revenues from other sources	<u>200,000</u>
Total revenues	\$4,000,000
Total expenditures	<u>4,000,000</u>
Net (expenses) revenues	<u>\$ -0-</u>

From the **Statement of Net Position**:

Cash and investments (at market value)	\$ 800,000
Capital assets, net	<u>4,200,000</u>
Total assets	<u>\$5,000,000</u>
Total liabilities	500,000
Total net position	<u>\$4,500,000</u>
Total liabilities and net position	<u>\$5,000,000</u>

Provide answers to the following questions:

Question	Response
1. What information in the financial statements is relevant to your decision?	
2. Is there other information that you would like to review before making the decision?	
3. Will you approve the loan? Why or why not?	

Exercise 4: Financial Statements

An adjusted trial balance has been prepared for the Island Government General Fund as of 9/30/19. Use the balances provided to prepare the financial statements for the General Fund. Prepare the Statement of Revenues, Expenditures, and Changes in Fund Balance first. Then prepare the Balance Sheet.

Island Government - General Fund Trial Balance - 9/30/19			
#	Account Name	DR	CR
100	Cash	460,000	
110	Accounts Receivable	194,400	
111	Allowance for Doubtful Accounts		18,000
115	Travel Advances Receivable	18,000	
117	Advances to Vendors	3,400	
130	Due From Other Funds	1,000	
200	Accounts Payable		76,000
205	Salaries Payable		4,500
210	Withholding Taxes Payable		450
220	Social Security Taxes Payable		270
230	Allotments Payable		1,200
240	Due to Other Funds		500
300	Fund Balance - Unassigned		82,420
310	Fund Balance - Assigned		5,000
400	Compact Revenues		1,320,000
410	Import Tax Revenues		120,500
420	Withholding Tax Revenues		98,600
430	Fuel Excise Tax Revenues		54,000
440	Interest Income		1,100
490	Operating Transfers (In)		15,300
510	Salaries Expenditures	652,300	
515	Employer Tax Contributions Exp.	39,140	
520	Materials & Supplies Expenditures	56,700	
530	Travel Expenditures	32,100	
535	Equipment Expenditures	129,500	
540	Utilities Expenditures	157,800	
550	Telephone Expenditures	34,200	
570	Bad Debt Expenditures	3,000	
580	Misc. Expenditures	2,000	
590	Operating Transfers (Out)	14,300	
	TOTAL	1,797,840	1,797,840

GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
For year ending September 30, 2019

REVENUES

Compact Revenues	_____	
Import Tax Revenues	_____	
Withholding Tax Revenues	_____	
Fuel Excise Tax Revenues	_____	
Interest Income	_____	
Total Revenues		_____

EXPENDITURES

Salaries	_____	
Employer Tax Contributions	_____	
Materials and Supplies	_____	
Travel	_____	
Equipment	_____	
Utilities	_____	
Telephone	_____	
Bad Debts	_____	
Miscellaneous	_____	
Total Expenditures		_____

EXCESS (DEFICIT) OF REVENUE OVER EXPENDITURES _____

OTHER SOURCES (USES)

Operating Transfers (In)	_____
Operating Transfers (Out)	_____

NET CHANGE IN FUND BALANCE _____

FUND BALANCE, BEG. OF YEAR _____

FUND BALANCE, END OF YEAR _____

**GENERAL FUND
BALANCE SHEET
September 30, 2019**

ASSETS

Cash	_____	
Accounts Receivable, net of allowance	_____	
Travel Advances Receivable	_____	
Advances to Vendors	_____	
Due from Other Funds	_____	
Total Assets		_____

LIABILITIES

Accounts Payable	_____	
Salaries Payable	_____	
Social Security & Withholding Taxes Payable	_____	
Allotments Payable	_____	
Due to Other Funds	_____	
Total Liabilities		_____

FUND BALANCE

Fund Balance - Assigned	_____	
Fund Balance - Unassigned	_____	
Total Fund Balance		_____
Total Liabilities and Fund Balance		_____