

WILEY

Federal Accounting Handbook

SECOND EDITION

Policies, Standards, Procedures, Practices

Cornelius E. Tierney
Roldan Fernandez

Edward F. Kearney
Jeffrey W. Green

KEARNEY & COMPANY



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PREFACE

Knowledge of federal budgeting, accounting, costing, and reporting is essential for all doing business with the federal government. This includes the 50 U.S. states; tens of thousands of counties, cities, municipalities, special authorities, and districts; over 100,000 prime and subcontractors, and nonprofits, colleges, and university grantees to the federal government; and beneficiaries of federal loans and loan guarantee programs. All have a need to know what is accounted for, how, when, and why by the federal government.

Hundreds of thousands of persons are involved daily with planning, budgeting, accounting, processing, and reporting on activities of the federal government—including those within and external to the federal government. Little, however, has been published on this field of financial management, and even less is taught about this financial specialty in universities, colleges, and business schools. Further complicating federal financial management is the fact that accepted and practiced federal accounting principles and procedures are not necessarily the generally accepted accounting principles of the private sector, nonprofit sector, or other levels of government.

The accounting and reporting required by federal laws, federal program regulations and rules, and federal department and agency guides significantly affects decisions relating to federal subsidies, federal contract and grant funding and refunding, the availability of advanced federal funding, recoveries of overhead costs, loan guarantees, and the determinations of allowable and unallowable costs, among others. Knowledge of what federal financial executives must do to “keep the books straight” is information vital to all those doing business with the federal government and all recipients of federal assistance. Having a general awareness of federal finances and accounting provides federal stakeholders with an indication of ultimate financial decisions and positions concerning federal contract awards, grant funding, entitlements, claim payments, reimbursements, compensation for overruns, recovery of overhead costs, and payment of claimed overtime, to cite a few.

The federal government, like other organizations and industries, has generated its own phrases, terms, words, and terminology—a jargon, or financial management language all its own. These descriptors are associated with or related to fiscal actions and economic events of federal organizations such as the Executive Office of the President, Congress, the Office of Management and Budget, the Department of the Treasury, and individual executive branch departments and agencies. Many of these terms permeate federal financial management, accounting, and reporting, and are defined and illustrated in this book. Most specialized are the terms relating to the budgeting, monitoring, and accounting for congressional appropriations and related revenues and expenditures. Additionally, requirements for concurrently performing budgetary accounting, accrual accounting, cash basis accounting, and cost accounting have resulted in the emergence of accounting procedures and processes that may be applicable only to the federal sector.

The *Federal Accounting Handbook, Second Edition*, is written for the reader at all levels of management, professionals within and external to the federal government, academics and students, or really anyone who has or should have a continuing interest in or has repeated dealings with the federal government. This book addresses interests of a diverse constituency—legislators, their staffs, program managers and analysts, financial managers, budget examiners and analysts, accountants, academics, researchers, and those doing business with the government—depending on the level of detail desired by each constituent.

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KEARNEY & COMPANY is a CPA firm that provides audit, accounting, and consulting services to the federal government. Additional details on Kearney & Company can be found on the Web at www.kearneyco.com.

INTRODUCTION

Every day, tens of thousands of people work at the financial management of the federal government—planning, budgeting, accounting, processing, and reporting. Hundreds of thousands more, working for local and state governments; public-sector and nonprofit organizations; and federal contractors, subcontractors, and grantees, are also responsible for accurately accounting for and reporting on their use of federal funds.

The accepted financial management practices and accounting principles of the federal government are not, however, those generally accepted practices of the private sector; neither are they the practices of state or local governments, nor those of the nonprofit sector. Nonetheless, these entities and any other entities or individuals receiving some form of federal funding or other federal financial assistance (e.g., grants, subsidies, loans, loan guarantees, contracts, appropriations, direct cash) should be conversant with federal financial management procedures.

The nexus of federal financial management is no less than the Constitution itself, which states

The Congress shall have the power to lay and collect taxes, duties, imposts, and excises, and to pay the debts and provide for the common defense and general welfare of the United States....(Section 8, Clause 1)

[and]

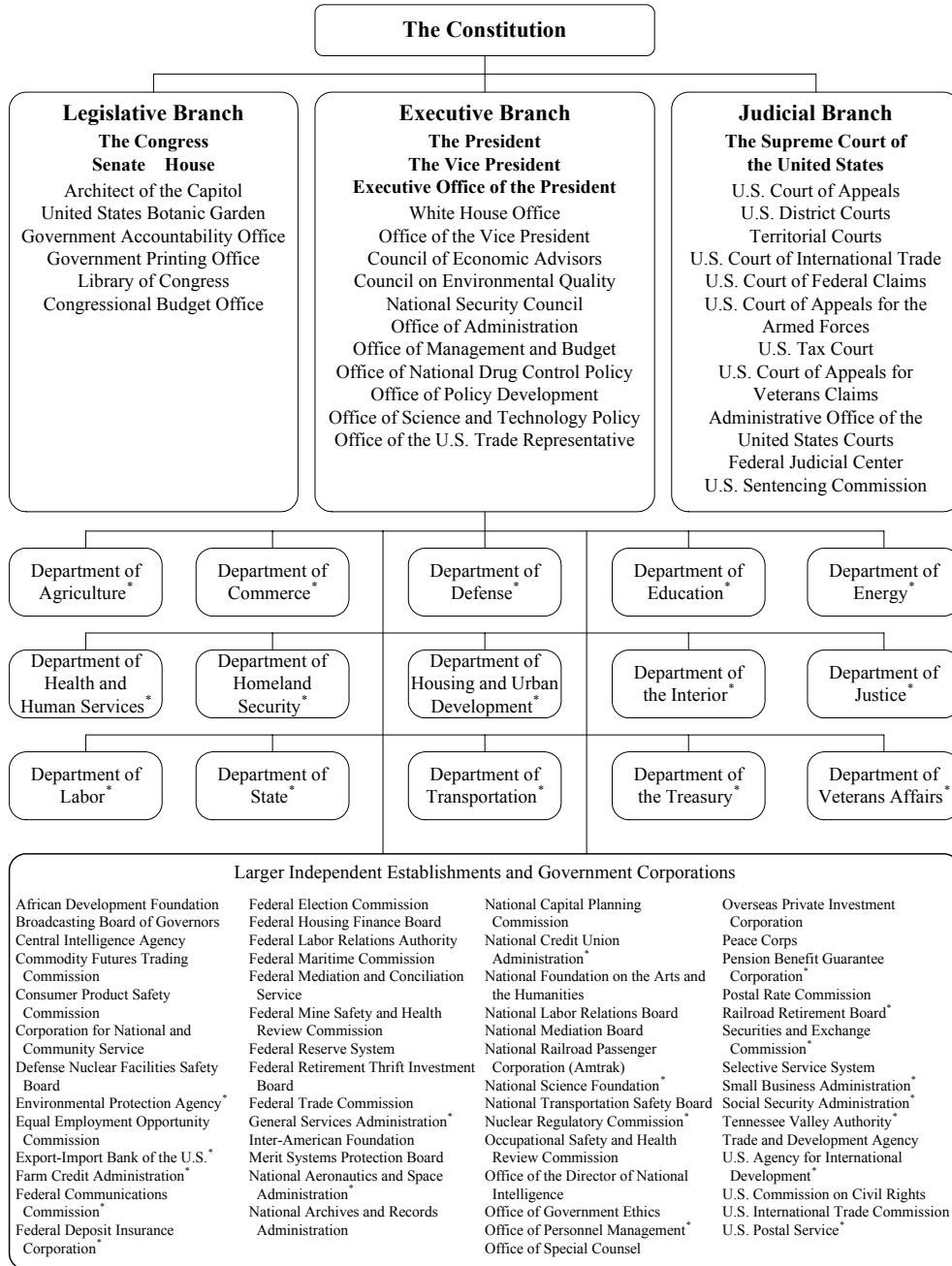
to borrow money on the credit of the United States....(Clause 2)

Furthermore, the Constitution requires that

No money shall be drawn from the Treasury, but in consequence of appropriations made by law; and a regular statement and account of receipts and expenditures of all public money shall be published from time to time. (Section 9, Clause 7)

To say that the federal government is big would be an understatement. It employs millions, owns billions, and collects and spends trillions every year. The executive branch manages this activity, and is permitted only to implement the will of Congress, as expressed by law. Exhibit I.1 illustrates the composition of the executive branch—its several cabinet-level departments, agencies, administrations, offices, commissions, corporations, boards, systems, and so forth; the legislative branch—Congress, its responsible offices, the Library of Congress, the Government Printing Office, United States Tax Court, and others; and the judicial branch with its component units—the Supreme Court of the United States, courts of appeal, district and other courts, and the Administrative Office of the United States Courts.

Exhibit I.1: The Government of the United States



*Indicates a significant entity included in the **Financial Report**. Original source: *U.S. Government Manual 2005/2006*.

IMPACT OF THE FEDERAL GOVERNMENT

In the State of the Union message, the President comments on the austerity of his budget requests; promises to hold expenditures to an absolute minimum; and then outlines programs and initiatives that seem, more often than not, to cost more than they did in the prior years. Regardless, or perhaps because of, explanations and good intentions, however, the federal government's spending and the national debt are both in the trillions of dollars. By any measure, the economic impact of the federal government is "big."

Annual federal outlays account for approximately 25% of the country's gross national product. These direct outlays do not include the expenditures and contingent liabilities of the Federal Reserve Board, several government-sponsored enterprises, and government corporations. These independent boards and hybrid corporations are responsible for various other direct expenditures and risks related to insurance programs, loans, and loan guarantees, and for federal-related guarantees and financings that are considered "off-budget" (which in federal parlance means "off the books"), but which, nonetheless, are in the trillions of dollars.

FEDERAL FINANCIAL MANAGEMENT BACKGROUND

Prior to the 1990s, government-wide efforts to improve federal financial management were sporadic and sometimes uncoordinated; at times these efforts received less than enthusiastic support from the Department of the Treasury (Treasury), the Office of Management and Budget (OMB), and Congress. Today, however, several laws set overall guidelines and establish detailed uniform federal financial management policy. The executive branch now places additional emphasis on changing and improving financial management practices in the federal government. OMB has issued several government-wide regulations to implement and enforce financial management improvement driven by congressional mandates.

Since the Constitution, the federal budget process—from the budget preparation phase through the budget execution phase—has been the continuum on which federal financial management rests. The federal budget is simply the money and expenditure authority, given by Congress, that forms the financial corpus that must be planned, budgeted, controlled, managed, accounted for, and ultimately reported upon by federal departments and agencies. As noted, until 1990, laws of Congress gave the Government Accountability Office (or GAO, formerly General Accounting Office), Treasury, OMB, and the heads of just about every individual agency some role in defining selected aspects of federal accounting, reporting, and controls for the budget.

Over the years the federal government has tested certain concepts to provide more precision in the estimation of budgets, monitoring of expenditures, cost accounting for programs, and so on. Concepts such as zero-based budgeting (ZBB); planning, programming, and budgeting systems (PPBS); and to a lesser degree, management by objectives (MBO) have been required by presidents, although not always with the full agreement or support of Congress. More recently, concepts such as activity-based costing (ABC) and Six Sigma (borrowed from the private sector),

and service efforts and accomplishments (SEAs) adopted from state and local governments, are being tried at the federal level as well.

In the 1950s, the Comptroller General of the United States had, pursuant to law, issued federal accounting and reporting standards. Decades later, half of the federal departments and agencies had not yet complied with these guidelines, and no pressure was exerted by Congress to force compliance. Uniformity and consistency of accounting and financial reporting among other federal entities—and even within an individual federal entity—was nonexistent.

In the 1980s and 1990s, several factors influencing Congress and federal executives led to the adoption of uniform federal accounting and reporting. The adopted standards, however, were not the accounting practices of corporations, state and local governments, or governmental nonprofits. At the federal level, departmental and agency financial managers found that they would have to require accounting: to ensure compliance with legal conditions and limitations; to do internal costing to manage their program and functional operations; to meet externally imposed reporting requirements; to compile the information necessary to monitor programs with state and local governments, nonprofits, and even individual citizens; and more. All of this complex activity must conform to the specifics of the Constitution, the bedrock accounting guide for expending all federal monies.

Generally accepted accounting principles are the accounting rules, practices, and conventions used for decades to account for and report on financial operations of the private sector, state and local governments, and nonprofit entities. These accounting rules, with regard to the private sector, have been promulgated since 1973 by the Financial Accounting Standards Board (FASB), with close oversight by the federal Securities and Exchange Commission (SEC) for corporations with registered securities. For state and local governments, certain public-sector nonprofit organizations, and many colleges, generally accepted accounting principles have been promulgated since 1984 by the Governmental Accounting Standards Board (GASB). State and local government securities are specifically exempted from SEC oversight unless fraudulent practices are involved with government securities. None of these widely accepted accounting and reporting guidelines was adopted to describe or report on the breadth of the federal government's financial management activities.

Further, until 1990, the responsibility for federal accounting and financial reporting was split between one legislative branch agency—the U.S. GAO—and two executive branch agencies—OMB and Treasury—and other federal executive branch departments and agencies. By laws dating back to 1921, GAO prescribed forms, systems, procedures, and accounting standards for the federal government. By these same laws, heads of each federal department or agency were required to develop and maintain the systems of accounting, reporting, and internal controls that best met that department's or agency's needs.

The accounting and reporting that did exist was an amalgam of congressional laws and the practices of several departments and agencies, supplemented and refined by miscellaneous regulations, rules, and directives. Over many years, GAO, Treasury, OMB, and scores of separate departments and agencies contributed to the body of practices that comprised federal financial management.

A CHANGING ENVIRONMENT

The more important forces of change in federal financial management were less financial in nature, but nonetheless contributed to an environment that required or permitted changes and improvements not possible in earlier decades.

In Congress

The 1980s witnessed an almost total generational change in Congress. Newer members may have been more business oriented, and unquestionably, they were younger. Older, more experienced members, who served in the 1960s, 1970s, and into the 1990s, had grown up with a federal government that was growing ever larger. To these latter members, the 1960s were simpler; growth had happened by steady evolution. Years of experience had provided many of the senior members with an intuitive feel for the numbers. Federal finances were not yet out of control; large deficits and an ever increasing federal debt were problems for future generations.

The newer congresses of the 1980s and 1990s found that there was no overall financial statement for the federal government, no enforcement of consistent accounting standards in departments and agencies, antiquated and unreliable department and agency reporting systems, and no history of annual department and agency financial statements. The newer, younger members of Congress, lacking the knowledge and history of what had gone before their elections, were aghast at the state of federal financial management.

In Individual Federal Entities

Almost at the same time, within departments and agencies, senior financial personnel changed. To reduce the federal budget and expenditures, early retirement options and buyouts were offered by Congress. These initiatives precipitated an unanticipated wholesale retirement or resignation of federal financial managers. Within a very few years, the expertise of an entire generation of experienced financial managers left the federal government; it was a government-wide brain drain. The succeeding financial managers lost their mentors, those who knew what had gone before and who could make the systems work.

Like members of Congress, the senior federal appointed executives of the 1980s and 1990s were new to the higher levels of government and were both younger and less experienced. These financial executives needed data that did not exist or that could not be produced without great effort. At best, some systems generated data that was “close” or may have been “good enough” for governments of past years. These executives were now charged with the financial management of a government that, in the 1990s, was spending over \$1.6 trillion annually, and with overseeing a federal debt that may never be paid in full.

The failure to require or implement essential accounting standards, consistent financial reporting, program and activity cost accounting, and departmental and government-wide financial statements all contributed to a crisis not publicly known, but one that was exacerbated by past inadequacies. Heretofore, while there had been

a system of federal financial management, most of the data elements and details of that system were known to only a few executives and managers. No single manual, repository, or source existed where one could find a comprehensive description of the accounting and reporting processes of the federal government. Further, up-to-date, continual financial management training had not been a high priority of past congresses and presidencies.

With minimal formal training and few books available, even those who wanted to learn the federal system ran into considerable difficulty. Budget requests for new or improved systems, and training for more financial managers and larger staffs, were the perennial targets of congressional and executive branch budget cuts. Governmental financial managers learned by doing, living, and being inside of a federal entity. Over many years, the diligent financial executive became well versed, but in only one system—his or her own.

Even with the support of later congresses and presidents, and despite the best efforts of all federal financial managers, better accounting, timely reporting, and adequate controls may not have been possible in those years. The federal government was enormous and the financial management task daunting. Managers were faced with the challenge of budgeting, accounting, and reporting on trillions in federal spending. To meet this challenge, they needed detailed budgeting and reporting of funds by every U.S. congressional district, and at all levels of government—50 states, more than 3,000 counties, and tens of thousands of cities, towns, and special government districts. This mass of information also needed to come from tens of thousands of federal contractors and grantees and from more citizens receiving direct federal assistance than one would care to count.

But this growth in size and complexity was happening at a time when computers and software technology were in their infancies. The data processing technology was not advanced, and almost no federal financial manager had tools to meet the data and information challenge. Slowly, the availability of friendlier, more advanced computer technology increased, and more sophisticated databases and application software were developed. In the late 1980s, a series of systems improvement efforts were identified, codified, and published by teams of federal financial executives under the auspices of the government's Joint Financial Management Improvement Program (JFMIP). Although the success of new financial systems implementation has been at times erratic, today, with available funding, departments and agencies are steadily acquiring the acumen—tools, software, people, training, improvement in internal controls, and so on—that they have long needed.

Major Federal Initiatives

In the 1980s, three products of the JFMIP had a significant impact on improving federal financial management: (1) a comprehensive compilation of federal financial information requirements and standard financial reporting requirements; (2) a document outlining core financial system requirements for the federal government; and (3) the Standard General Ledger (SGL) for the government. Each of these initiatives was a first-time effort, and all were needed to provide the systems of accounting and controls desired by Congress and federal managers.

In 1990, the Chief Financial Officers Act (CFO Act) gave the OMB the main responsibility for federal financial reporting, and financial managers in the Treasury began to support departments and agencies wanting to improve federal accountability. The Treasury also became a more active partner with the OMB in conducting research and experimenting with alternatives to enhance accounting and reporting within departments and agencies government-wide.

Following the passage of the CFO Act, the U.S. Comptroller General (who heads the GAO), the Secretary of the Treasury, and the Director of the OMB established the Federal Accounting Standards Advisory Board (FASAB). The FASAB was instructed to develop and recommend accounting and reporting standards for use by each federal department and agency, as well as for government-wide applications.

With the mandate of the CFO Act, initiatives to improve financial management moved forward in the 1990s. The OMB became the authoritative source for agency financial statement auditing, financial management, accounting, and reporting policies. By 1993, the newer policy direction, uniform accounting and reporting standards, and government-wide systems requirements with which federal departments and agencies must comply were well established.

In 1992, the FASAB began recommending accounting policy. By 1993, the OMB had directed departments and agencies to establish and maintain an integrated financial management system that complied with FASAB, OMB, and Treasury promulgations.¹

FEDERAL ACCOUNTING AND REPORTING TODAY

The Federal Reporting Entity

Until the 1990s, there had been no uniform resolution of what constituted a federal accounting and reporting entity. There is only one overall economic entity: the federal government as a whole. But the federal government operates by a network of somewhat autonomous, subordinate departments, agencies, commissions, and other federally funded organizations. Each entity manages activities, legally obligates the government, and spends federal monies.

The FASAB recommended that the federal accounting and reporting entity would be the organization that issued general-purpose financial statements. That is, departments and agencies would be the reporting entities of the federal government. This was a long-needed clarification. Historically, many had supported the view that the congressional appropriation (i.e., the funds made available by Congress) was the accounting and reporting entity. Others, with different responsibilities, believed that budget accounts or Treasury accounts (and they are not the same) would provide more accurate and revealing financial disclosures of the operations of the federal government. Still others thought the primary reporting entity ought to be the special funds or trust funds established pursuant to law.

¹ OMB Circular A-127, *Financial Management Systems*, 1993, which updated and, in part, revised an earlier OMB Circular A-127 of December 1984.

Some federal entities have a single appropriation as their primary financing resource for operations. Other federal departments and agencies may be responsible for two or more congressional appropriations. When a single department or agency is responsible for multiple appropriations, these funds may, by law, support a variety of operations or a combination of programs. There may be instances when an agency, by law, must operate programs without having received any direct appropriation, but is provided spending authority through an allocation from another agency's appropriation.

Congressionally enacted appropriation laws have a unique status in federal accounting. The passage of revenue and expenditure appropriation legislation by Congress provides the basis for federal departments and agencies to collect taxes, revenues, and other fees from the public and to incur obligations and make expenditures from the Treasury. These laws form the legal, economic, accounting, and reporting criteria for federal entities.

To illustrate, prior to the 1990s, congressional appropriations were viewed as accounting entities; the federal departments and agencies, as reporting entities. The ideal condition, of course, from an accounting, financial, and reporting point of view, would exist if all operations of a federal entity were supported by a single congressional appropriation. This considerably simplifies the budgeting, managing, accounting, and reporting issues.

Since an appropriation is an accountable happening, the recipient federal entity must record, account for, and report assets, liabilities, and investments of the government, as well as its expenditures and any revenues, by each individual appropriation. Stated another way, an integrated set of records is required to account fully for the stewardship of all funding to an entity; the details, with respect to each appropriation, must be separable in the records of the entity. However, accounting and reporting by appropriations only is not satisfactory for managing and measuring program performance. Accounting only by appropriation portrays departments and agencies in a somewhat fractured perspective.

Nonetheless, accounting by appropriations was the prevalent form of accounting and financial disclosure in the federal government through the 1960s, until computer technology permitted reporting on other bases and dimensions. In 1994, the FASAB recommended that federal organizations report on all of their stewardship responsibilities provided by congressional authority. The FASAB, in its federal accounting concepts, stated that a basic postulate of accounting is that federal accounting information pertains to the federal reporting organization.

Included within the federal government are other entities, such as government-sponsored enterprises. These entities, while they are federally chartered and overseen by Congress and have private stockholders, are no longer directly financed by congressional appropriations. The accounting for assets and liabilities of these entities is off the books of the federal government; such assets and liabilities include their guaranteed debt, the liability for which has never been clarified by Congress. In addition, other federal organizations, such as the Federal Deposit Insurance Corporation and the Federal Reserve Board, are subject to congressional oversight, but

their operations are financed by levies on the constituencies they regulate rather than by direct appropriations of Congress.

The Federal Financial Statements

Historically, department- or agency-wide financial statements were of minimal concern to legislators and the central agencies of the federal government. These parties gave primacy to appropriation accounting. While not ideal, and not full disclosure, the primary historical system of reporting is this: matters related to budgetary status must be reported to the OMB; cash must be reported to Treasury; and accounting for specific appropriations must be reported to Congress. With continuing GAO emphasis over the years and the more widespread introduction of computer technology, the organizational entity gained prominence as the reporting entity in the 1980s and 1990s.

Since the passage of the CFO Act and later laws, annual financial statements are now compiled department- and agency-wide and are independently audited. Subsequent to the CFO Act, agencies have striven to ensure that these federal financial statements conform to the accounting and reporting standards recommended by the FASAB and promulgated by the OMB.

Financial reporting for corporations, state and local governments, academic institutions, and nonprofit organizations is typically provided through a package of four financial statements—a Statement of Financial Position (i.e., the balance sheet), a Statement of Operations (i.e., the income and expense statement), a Statement of Retained Earnings, and a Statement of Cash Flows. The FASAB concluded that this level of reporting would not suffice for the federal government and cited a need for other types of financial statements. The OMB, in its circular on the form and content of federal financial statements, requires federal agencies to prepare and have audited five principal annual financial statements:

1. The *Balance Sheet* is needed to present resources, liabilities, and the financial status of the entity at a specific point in time, however measured (i.e., budgetary, cash, accrual, etc.), and to show total balances of appropriate assets, liabilities, and equities of a federal organization.
2. A Statement of *Net Cost* is needed to present the various components of the net cost of a reporting entity's operations (i.e., total, gross, or full costs less any exchange revenues).
3. A Statement of *Changes in Net Position* reports the beginning net financial position, the items that caused changes in the net position, and the ending net position of a federal entity.
4. A Statement of *Budgetary Resources* provides information on the status of congressional spending authority by those entities whose financing derives, wholly or in part, from congressional budget and spending authority.
5. A Statement of *Financing* is an accrual-based reporting, in contrast to the budget-based reporting of the Statement of Budgetary Resources. The Statement of Financing reconciles the financial (or proprietary) net cost of operations with the obligational basis of budget authority.

6. A Statement of *Custodial Activity* is used to record custodial revenue collected by a federal agency which is not considered revenue to the entity. Typically, these are collections on behalf of other funds (e.g., Treasury's General Fund, trust funds, etc.). These are normally nonexchange revenues with (arguably) the best known example being collection of taxes by the Internal Revenue Service. This statement applies only to entities engaged in custodial activities and only if the custodial activity is a significant part of the agency's mission. Incidental custodial collections do not require the separate statement.

These are statements of a different character, in greater number, and with different content than those appearing in an annual financial report of private-sector organizations or other public-sector and nonprofit entities. Other reporting is dictated by legislation and compliance criteria imposed on a department by Treasury or the OMB. Further, there is no prohibition in the federal standards against a department or agency having statements unique to itself, designed to provide data on performance indicators or its operations.

Parallel Accounting Bases

Laws, regulations, terminology, financial practices, and the simple enormity of federal government operations have fostered specialties that hint at a somewhat fractured system (or sets of systems). Federal laws, regulations, rules, and promulgations often refer to various types of accounting—budgetary, financial (proprietary), cost, and even cash accounting. The next section is an overview of these terms, which are described, discussed, and illustrated in the chapters that follow.

Budgetary accounting. This accounting applies to the processes, controls, monitoring, and reporting required to track the execution of the budget laws of Congress. Budgetary accounting in the federal government has given rise to a body of terminology, descriptive of both legal and economic events and accounting procedures, required of federal entities to monitor and manage the financial impact of these events. Some examples of these events and their relevant terminology include

- Only Congress can *authorize* and *appropriate* funds or budget authority to permit the collection of revenues or expenditure of federal money. Authorization and appropriation legislation are separate legislative actions of Congress.
- Permission to *allocate* a portion of an appropriation between agencies is an exclusive prerogative of Congress. Allocations must be specifically identified by Congress in its laws.
- By law, the OMB has the responsibility to *apportion* the various funds appropriated or allocated by Congress to regulate the rate of fund use by agencies. Thus, the OMB must approve all apportionment requests before a federal department and agency can obligate the government or spend federal money.
- The individual federal departments and agencies are responsible for *allotting*, *obligation*, *expending* or *disbursing*, and *costing* the funds of an appropriation or other budgetary authority as they execute and manage federal programs. The accounting and reporting of these activities must be by each congressional

appropriation, and by the individual programs and activities of the federal entity, in total for the entire entity and ultimately government-wide.

By a variety of laws, department and agency accounting and financial reporting procedures must be established and used to ensure compliance with government-wide criteria and with a department's or agency's own policies and controls for proper management of funds, assets, and other federal resources. Understanding the budgetary accounting process is a prerequisite to understanding the uniqueness of federal accounting. It is the reporting for the legal, economic, and accounting events and actions alluded to earlier that distinguishes federal accounting from the accounting of private-sector and other public-sector organizations.

Financial (proprietary) accounting. There is also an accounting for the assets, liabilities, investments, revenues, and expenditures related to an appropriation by federal entities that is somewhat similar to the accounting process used in the private sector. This basis of accounting is referred to as *proprietary accounting*.

Overall, Congress and the OMB require that systems of accounting and internal controls exist to acquire, safeguard, account for, report on, and dispose of funds and properties and settle debts of the government. This financial accounting, however, varies for two types of governmental entities. The accounting for all cabinet departments and most federal agencies is premised on an appropriation-based as well as an accrual-based accountability for governmental activities.

Funds are also established by Congress to finance certain business-type organizations, the accounting for which is generally conducted pursuant to the legal requirements for working capital funds, revolving funds, and more recently termed "franchised" operations. These operations, often supply and industrial funds, perform a variety of business services from wholesaling to manufacturing, and (in a sense) sell services or products to other units within their department or externally to other federal departments and agencies. For these business-type operations, business or private-sector accounting is generally applied; often cost accounting is an integral aspect of the financial management of such entities.

As with the corporate sector, the accounts of a federal entity must provide a ready reporting of activities on both a cash basis and an accrual basis. Neither basis is best; both are required to manage, but for reasons that might differ somewhat from those of the corporate sector. Ideally, a federal entity should manage and monitor its operations on the accrual basis of accounting; but the Treasury requires daily information to support its cash-basis accounting. The OMB is in legal trouble if it does not require agencies to report on the basis of obligations, and Congress wants reporting by appropriations, a language it understands.

Cash accounting. To meet the constitutional mandate to provide "a regular statement and account of receipts and expenditures of all public money," the Treasury needs specific information. This necessitates that the Treasury maintain and operate a central cash accounting and financial reporting system for the federal government.

As the "keeper of the government's purse," the Treasury must, pursuant to the Constitution and other laws, render regular statements of receipts and expenditures of the government. While this is an important accounting and significantly impacts

individual departmental and agency accounting and reporting, the accounting needed by the Treasury is essentially a cash-in, cash-out system, fulfilling a single purpose, the federal cash-balance reporting, with minimal utility for overseeing and managing the programs and activities of federal entities.

The central requirement of the Treasury automatically becomes a detailed accounting and reporting requirement of all federal entities. Information on entity programs and activities must be compiled and monitored on a cash or checks-issued basis, as well as on the other bases.

Cost accounting. Knowledge of the costs of programs, activities, and outputs is necessary if Congress and federal executives are to make sound decisions about resource allocations, authorizing and managing programs, and evaluating performance. Industrial funds, working capital, and federal revolving funds have long been concerned with capturing and reporting costs—of activities, products, operations, and so on. Historically, though, cost accounting was not regarded as a high priority in federal accounting by managers of programs financed by annual appropriations. Considerable legal impetus was provided by several congresses with the passage of many laws impacting financial management (e.g., the Government Performance and Results Act, the Government Management Reform Act, and the Federal Financial Management Improvement Act). These initiatives caused departments and agencies increasingly to examine the financing, spending, and financial monitoring of programs and operations from a cost perspective. The full-cost view is in contrast to financial reporting made on the more historically popular cash, appropriation, obligation, and fund views, all of which provide less than a total financial accounting.

Cost accounting is viewed as a more precise recording, accumulating, accounting, and reporting of the costs of a product, service, activity, or even a program, than is the case with typical appropriation-based accounting. While later discussed separately from budgetary and financial accounting, cost information must be from the same financial and nonfinancial and statistical databases as are used by the entity for its budgetary, accounting, and financial reporting purposes.

DIFFERENT VIEWS ON FEDERAL FINANCIAL MANAGEMENT

The public's views about federal financial management and data needs seem limited only by the number of views solicited. In its 1997 statement of federal accounting concepts, the FASAB provided an illustrative comment on viewpoints, such as those of an economist, a financial analyst, a federal budget analyst and program manager, and a federal accountant and auditor:

- The economist is seeking data on the national society as a whole most importantly, possibly for the National Income and Product Accounts, a system that emerged in the 1940s in the Department of Commerce and earlier in private organizations.
- The Wall Street analyst is more likely to view federal financial reporting in terms of the “Daily Treasury Statement” or the “Monthly Treasury Statement of Receipts and Outlays” of the United States Government.

- Budget formulators and analysts want data from the federal budgetary accounting system, which tracks spending authority, controls expenditures, assesses economic implications, and is used in planning for government.
- Accountants, program managers, and auditors in the federal environment want accountings of assets, liabilities, levels of revenues and expenditures, and periodic status reports of budget execution (i.e., budget versus actual).

Users of federal financial information—citizens (defined in the broadest term), Congress, federal executives, and operating managers—all require data that asserts the integrity of the federal budget and its execution; discloses the cost of federal program operations and federal securities; and provides an accounting on stewardship of federal assets, pensions, insurances, and programs. Only with such information can citizens be assured, as noted in the Constitution, that no money is being drawn from the Treasury except in compliance with a law by Congress, and that for such receipts and expenditures there is a regular statement and accounting.

PART 1

THE NATURE OF FINANCIAL MANAGEMENT IN THE FEDERAL GOVERNMENT

1 FINANCIAL MANAGEMENT LEGISLATION AND POLICY

Under the United States Constitution, the responsibility for federal financial policy rests exclusively with the U.S. Congress. Over the years, the level of congressional involvement in department and agency operations has varied from macro-management to micromanagement.

By various laws, Congress has directed that certain central agencies establish specific financial management policies and that these agencies issue specific accounting and reporting principles, standards, and administrative guidelines for compliance by other federal departments and agencies of the government. These central agencies include the Office of Management and Budget, the Government Accountability Office, the Department of the Treasury, the General Services Administration, and the Office of Personnel Management. These agencies have published regulations and rules giving operating departments and agencies further guidance in implementing legislation. A considerable body of policy has been legislated relating to overall federal financial management. Furthermore, Congress also gives broad discretion to individual departments and agencies in determining managerial, accounting, and control procedures and practices needed to manage their own operations, programs, and activities.

OBJECTIVES OF FEDERAL ACCOUNTING

The overall objectives of appropriation budgetary fund accounting are directed toward fiscal accountability and compliance with the expressed intent of Congress. These objectives include

- Ensuring that federal monies are spent only for purposes, with only those constituents, in only those locations, for only the amounts, and only within the time period set forth by Congress in its authorization and appropriation laws
- Preventing obligations, expenditures, or disbursements of federal monies in excess of the appropriations or budget authority legislated by Congress
- Fixing personal responsibility with designated federal executives for any violations or instances of noncompliance with congressional limitations or restrictions
- Assisting with or promoting increased effectiveness and economy in the application and rate of expending federal money

Implicit features of a federal entity's systems of accounting and controls are checks and balances to ensure that several criteria of a federal appropriation are considered by a federal executive prior to the obligation or expenditure of federal monies and that program performance is consistent with law. At a minimum, all appropriations and budget authorities have three specific compliance considerations:

1. *Timing*—The commitment and, on occasion, the rate of expenditure of appropriated funds must be made only during the time period permitted by Congress in legislation.
2. *Purpose*—Appropriated funds may be obligated and expended only for those purposes intended or expressed by Congress in an agency's authorization or appropriation legislation.
3. *Amount*—The total amount of obligations and expenditures may not exceed the appropriation or amount of budgetary authority legislated by Congress.

IMPLEMENTING ACCOUNTING IN THE FEDERAL GOVERNMENT

The implementation of overall federal financial policy through more detailed regulations, rules, and other publications is dispersed among the aforementioned central agencies as well as among other executive branch entities. The three agencies having the majority of specific government-wide financial management responsibility include the GAO, the Office of Management and Budget (OMB), and the Department of the Treasury (Treasury). The General Services Administration (GSA), the Office of Personnel and Management (OPM), and the Congressional Budget Office (CBO) have also been given either government-wide or more specific roles by Congress.

Several individual operating departments and agencies are given further responsibility by law for designing, implementing, and maintaining their own systems of accounting and internal and administrative controls.

Office of Management and Budget

Broad changes were made in federal financial management with the passage of the Budget and Accounting Act of 1921. The most significant provisions of that Act included

- Title II, which established for the first time a national budget system requiring the President to formally transmit the national budget proposal to Congress at the beginning of each session. This Act also created the Bureau of the Budget (BOB) within the Department of the Treasury.
- Title III, which established the GAO, to be headed by a Comptroller General of the United States. The GAO is a legislative branch agency, independent of the executive branch, and responsible only to Congress.

In 1939, the BOB was made a part of the Executive Office of the President, where it exercised the role of budget officer for the President. Later the BOB was reorganized and subsequently renamed the OMB, by Reorganization Plan No. 2 of 1970. By that plan, all functions of the former BOB were transferred to the director of the OMB. Since the 1980s, the OMB has operated in an increasingly broader and stronger role as the federal government's office of financial management.

Over the years, many laws have given the OMB extensive responsibilities for prescribing regulations and rules governing the federal government's financial management systems of budgeting, accounting, reporting, and auditing. These tasks have been broadly mandated to include planning, programming, monitoring, performance