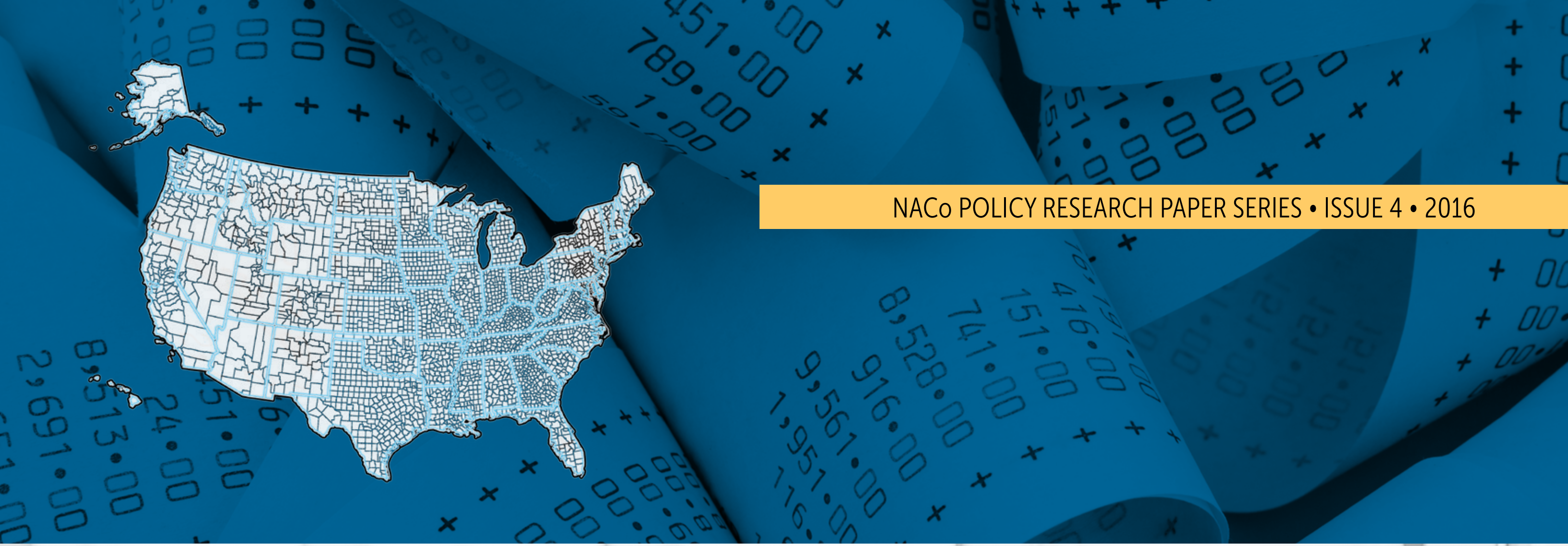

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COUNTING MONEY

STATE & GASB STANDARDS *for* COUNTY FINANCIAL REPORTING

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NATIONAL ASSOCIATION *of* COUNTIES NACo

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INTRODUCTION

Counties provide essential services to more than 308 million residents across the country to keep communities prosperous, safe and secure. Creatures of the states, county governments operate in a constrained financial environment, conforming to state and federal mandates and limited by state caps on their ability to raise revenue. Understanding the diversity of county financial reporting and data is a first step towards examining national trends in county financial health. It also lays the foundation for future research about the impact of changes in state financial reporting standards for county governments. This study provides a comprehensive, national view of the variations among county governments in terms of financial reporting, as well as state and other standards with which counties have to comply for financial reports. This analysis intends to educate a policy audience evaluating the parameters of fiscal transparency placed on counties.

UNDERSTANDING THE DIVERSITY OF COUNTY FINANCIAL REPORTING AND DATA IS A FIRST STEP TOWARDS EXAMINING NATIONAL TRENDS IN COUNTY FINANCIAL HEALTH.

Most state and local governments follow generally accepted accounting principles (GAAP), standards of accounting and financial reporting developed by the Governmental Accounting Standards Board (GASB), an independent, private organization. The accounting and capital markets recognize GASB as the official source of GAAP for state and local governments.[1] State auditors or independent public accountants audit county financial statements through the lens of GASB standards. If a county's financial report is fairly and appropriately presented in accordance with GAAP, the county receives an unqualified opinion. An adverse opinion from auditors can negatively affect a county's borrowing costs.

THE ACCOUNTING AND CAPITAL MARKETS RECOGNIZE GASB AS THE OFFICIAL SOURCE OF GAAP FOR STATE AND LOCAL GOVERNMENTS.

GASB periodically issues new accounting standards that state and local governments observing GAAP have to implement. For example, GASB Statement No. 68 reporting standard issued in June 2012 set new requirements for government employers with defined benefit pension plans to include a net pension liability in their financial report balance sheet for fiscal years after June 15, 2014.

County financial reporting, however, extends beyond GAAP. Depending on state requirements, county governments may use alternative methods of financial reporting and accounting to GASB standards, ultimately affecting how and what financial activities counties report to stakeholders and the public. As a result, financial reporting may differ substantially among counties across the country. This study examines state requirements for county financial reporting, as well as the types of financial statements and accounting methods county governments employ. The immediate goal is to provide an understanding of the diversity of financial reporting among counties, how financial data differs among county governments and the extent of observance of GASB standards. This report intends to create a foundation for future policy research on county finance and transparency.

FINDINGS

1 **THE MAJORITY OF STATES REQUIRE COUNTY GOVERNMENTS TO OBSERVE GASB STANDARDS FOR THEIR ANNUAL FINANCIAL REPORTS.** County governments apply GASB standards either because the state requires them to do so or to receive a favorable audit. Thirty-two (32) states require counties to follow GAAP through statute and 295 counties in another 13 states and the District of Columbia choose to file their financial reports according to GASB standards (See Map 1). Western states are the most likely to require counties to follow GASB standards. All but two Western states – Washington and Nebraska – require counties to report according to GAAP issued by GASB. In contrast, about half of Midwest states require their counties to use GAAP when filing annual financial reports. In these 32 states, county governments follow the GAAP approved format of the report (basic financial statements) and the accounting method (accrual basis) (See Appendix for more explanation of basic financial statement and accrual basis of accounting).

KEY TERMS USED IN THIS STUDY

COUNTY GOVERNMENT An organized entity with governmental character, sufficient discretion in the management of its own affairs to be an independent governmental unit and covering the geographical area of a county or county equivalent. Depending on the state, it can be known also as parish government or borough government. This study includes among county governments the following types of local governments defined by the U.S. Census Bureau as consolidated county-city entities; areas designated as metropolitan governments; cities administering functions performed by county governments and areas with certain types of county offices, but included as part of another government, because these government entities have county government status by county charter, state legislation or constitution. There are 3,069 county governments in the United States. For ease of use, this study employs interchangeably "county" and "county government."

GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB) The independent organization that sets the accounting standards for U.S. state and local governments, known as generally accepted accounting principles (GAAP).

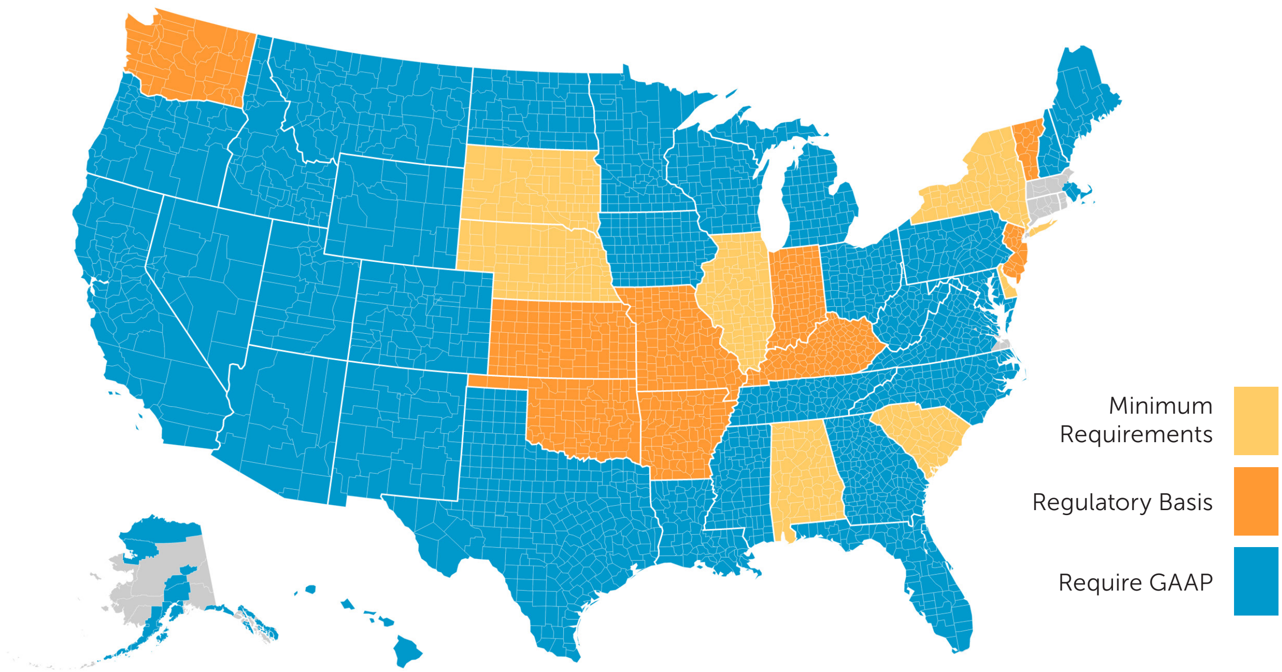
GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP) The commonly accepted set of accounting principles, standards and procedures to compile financial statements. GAAP is a combination of authoritative standards (set by GASB policy boards) and commonly accepted ways of recording and reporting accounting information. This study also calls them "GASB standards."

BASIC FINANCIAL STATEMENTS Accounting reports compiled in conformity with the provisions of GAAP issued by GASB. For governments, this consists of government-wide financial statements, fund financial statements and notes to the financial statements.

ACCRUAL BASIS OF ACCOUNTING A comprehensive method of accounting that reports revenues when earned. Expenses are matched with the related revenues and/or reported when the expense occurs. GASB approves this method of accounting for state and local government financial reporting.

MAP 1. THE MAJORITY OF STATES REQUIRE COUNTIES TO OBSERVE GASB STANDARDS

AS OF NOVEMBER 2015



Notes: Conn., R.I., and parts of Mass. have counties or county-equivalents with no county governments (marked in grey on the map).
Many states specify whether counties must report annual financial statements in accordance with Generally Accepted Accounting Principles (GAAP) set by the Governmental Accounting Standards Board (GASB) or, alternatively, meet state regulatory requirements that do not comply with GAAP (Regulatory Basis). Other states have minimal reporting requirements placed on counties (Minimum Requirements).

STATES REQUIRE COUNTIES TO PRODUCE AN ANNUAL FINANCIAL REPORT AUDITED BY A THIRD PARTY. Most states specify the accounting methods and financial reporting standards for counties either by statute or by giving authority to state comptrollers (or similar positions) to choose the financial reporting standards. In some instances, the state acts as the independent third party auditor for the county governments. For example, the Alabama Examiner of Public Accounts audits the accounts, books and records of all county offices.[2] In North Dakota, the Office of the State Auditor performs the audits for all 53 counties in the state.[3] Other states, like Texas, are more nuanced. The Texas Local Government Code determines the audit procedure based on the county population size. Counties with more than 350,000 residents must have an independent audit conducted by a third party every year. County governments in counties with populations between 40,000 to 100,000 residents must appoint a county auditor. The smaller county governments, in counties with less than 25,000 residents, can pool their resources with other county governments to hire a public accountant to conduct these audits.[4]

THIRTY-TWO (32) STATES REQUIRE COUNTIES TO FOLLOW GAAP THROUGH STATUTE.

NINE STATES ASK COUNTIES TO FOLLOW AN ALTERNATIVE METHOD OF FINANCIAL REPORTING AND ACCOUNTING TO GAAP. These nine states (Ark., Ind., Kan., Ky., Mo., N.J., Okla., Vt. and Wash.) use a regulatory basis of accounting, in which the state determines the framework, including measurement, recognition, presentation and disclosure requirements of the county financial reports. They also use other comprehensive basis of accounting (OCBOA), such as cash basis of accounting and different from the GASB accrual bases of accounting (See Key Terms for definitions).

MOST REGULATORY STATES ALLOW COUNTIES TO CHOOSE BETWEEN THE STATE REQUIREMENTS AND GASB STANDARDS. About 8 percent of counties in these states elect to follow GASB standards (both the format of the financial report and method of accounting), to increase their chances of receiving a favorable audit. While states may allow counties to choose GAAP over the state regulatory basis, in some cases counties need additional measures to adopt their preferred accounting standards. For example, counties in Oklahoma and Washington choose between GASB and the statutory alternative without any additional preliminary approval from the state.[5] Alternatively, Kansas counties adopt the state regulatory basis of accounting by county board resolution.[6] As of November 2015, 96 out of 105 Kansas counties have adopted state reporting standards by board resolution. Large counties in regulatory states are more likely to follow GASB standards. Ten of the 20 large counties in regulatory states — with more than 500,000 residents — report according to GAAP, while a quarter of mid-sized counties — with 50,000 to 500,000 residents — and 1 percent of small counties do so. Most of the large counties that do not follow GASB are in New Jersey, a state with strict requirements for counties to follow the state reporting standards.

MOST REGULATORY STATES ALLOW COUNTIES TO CHOOSE BETWEEN THE STATE REQUIREMENTS AND GASB STANDARDS.

KEY TERMS USED IN THIS STUDY

REGULATORY BASIS OF ACCOUNTING Also known as statutory basis of accounting. A basis of accounting in which the state regulator (the state or a state agency) establishes the financial reporting provisions and standards separate from GAAP.

OTHER COMPREHENSIVE BASIS OF ACCOUNTING (OCBOA) System of methods of accounting other than GAAP, including cash basis, modified cash basis and regulatory basis of accounting.

CASH BASIS OF ACCOUNTING Accounting method that records transactions at the time cash is received or paid out for revenues and expenses. This method is different from GASB standards for financial reporting.

LARGE COUNTIES County governments of counties with more than 500,000 residents, living in both incorporated and unincorporated areas, as of 2014.

MID-SIZED COUNTIES County governments of counties with populations between 50,000 and 500,000 residents, living in both incorporated and unincorporated areas, as of 2014.

SMALL COUNTIES County governments of counties with less than 50,000 residents, living in both incorporated and unincorporated areas, as of 2014.

THE REMAINING SEVEN STATES WITH COUNTY GOVERNMENTS (ALA., DEL., ILL., NEB., N.Y., S.C. AND S.D.) HAVE MINIMUM REQUIREMENTS ON COUNTY FINANCIAL REPORTING. Adherence to GAAP in these counties is more of a tradition than a state requirement. The majority of the counties in these seven states elect to organize their financial statements according to GASB standards, including all large counties. For example, Delaware and Nebraska do not have a state statute or policy instructing counties how to report their annual financials.[7] Instead, counties choose to report according to GAAP to increase their chances for favorable reviews by bond rating agencies.

ANNUAL AND BIENNIAL AUDITS OF COUNTY FINANCIAL REPORTS. The time of the release of a county financial statement varies depending on the period of the fiscal year in the county and other factors. In some states, such as Arizona, the county fiscal year runs from July 1 of the preceding calendar year to June 30 of the current calendar year. For example, Maricopa County, Arizona's 2007 Comprehensive Annual Financial Report (CAFR) reflects the county financial activity occurring between July 1, 2006 and June 30, 2007.[8] In other states, like Minnesota, the fiscal year for financial reporting matches the calendar year, meaning that a county financial report reflects fiscal activity from January 1 to December 31 of the given calendar year. Further, the audits of some of the county financial reports are not released annually. In 17 states, a state auditing agency conducts all or some of the audits of county financial statements. In the rest of the counties in these states and around the country, a county auditor or an independent auditor perform the audit of the county financials. In some states, such as Missouri and North Dakota, the state auditor conducts the majority of county financial statement audits and release biennial audits. In South Dakota, the State Auditor releases biennial audits mostly for smaller counties.[9]

IN TOTAL, 16 STATES EITHER ASK TO REPORT USING ALTERNATIVE METHODS TO GAAP OR ALLOW COUNTY FINANCIAL REPORTING TO DEVELOP BY TRADITION.

Under the jurisdiction of their respective states, county governments file annual financial reports in accordance with state regulations. While the vast majority of states require adherence to GAAP for county financial reporting, GASB standards are not the only paradigm for conveying county financials. In total, 16 states either ask counties to report using alternative methods to GAAP or allow county financial reporting to develop by tradition. The variation of state requirements lends to the diversity of county financial reporting.

KEY TERMS USED IN THIS STUDY

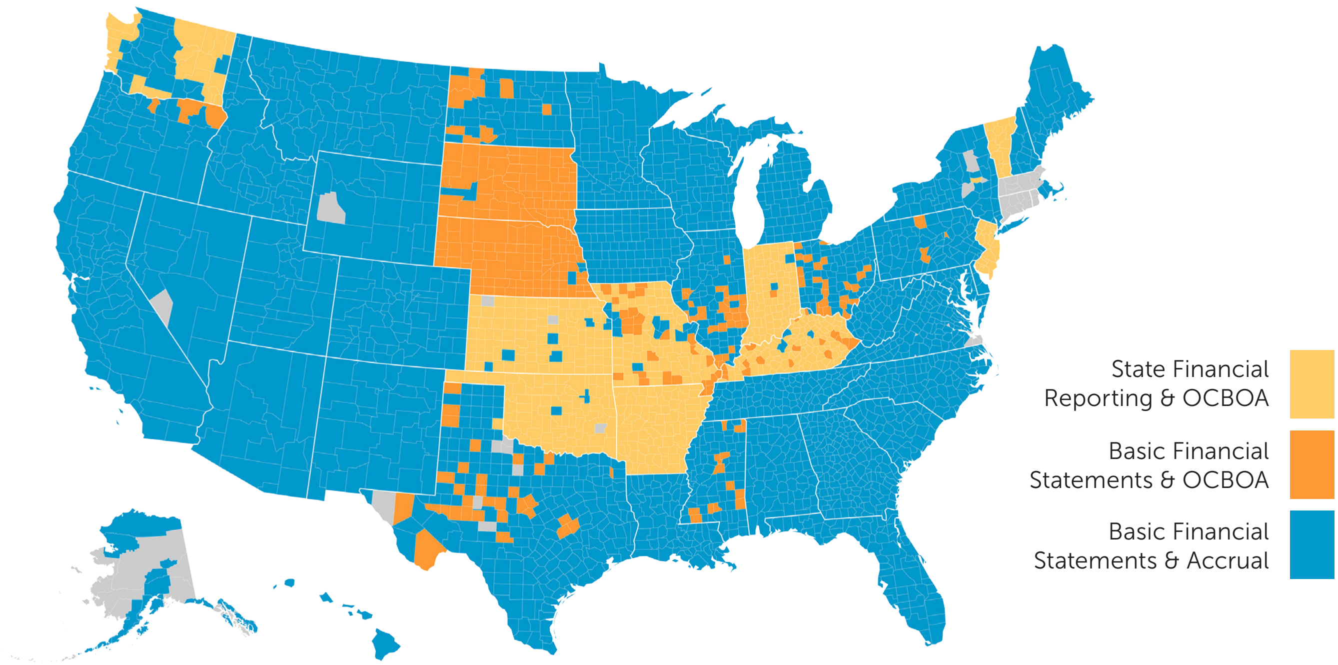
COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR) A state or local government financial report that meets the reporting standards and provides additional statistical and demographic information useful to the government entity board members, management and outside groups for financial analysis.

REGULATORY BASIS FINANCIAL STATEMENTS Financial statements prepared and presented using criteria established by the regulator (state or government agency).

MAP 2.

ALMOST A FIFTH OF COUNTIES FOLLOW STATE SPECIFIC FINANCIAL REPORTING STANDARDS

AS OF NOVEMBER 2015



Notes: This study identified the type of financial report and method of accounting for 3,053 of the 3,069 county governments. Conn., R.I. and parts of Alaska, Mass. and Va. have counties or county-equivalents with no county governments (marked in grey). County governments from which NACo could not retrieve financial statements by November 2015 are also marked in grey. County financial statements classified as "State Financial Reporting & OCBOA" represent county financial reports that use state regulated statement format and alternative methods of accounting to GAAP. "Basic Financial Statements & OCBOA" indicate counties that use GASB approved financial statement format, but use alternative methods of accounting to GAAP. Reports classified as "Basic Financial Statement & Accrual" use GASB approved financial statement format and method of accounting.

2 **STATE SPECIFIC RULES FOR FINANCIAL REPORTING ARE THE STANDARD FOR ABOUT A FIFTH OF COUNTY GOVERNMENTS.** GASB standards are predominant among county governments, with almost three-quarters (71 percent) of counties reporting their annual financial information in the format of basic financial statements and on an accrual basis of accounting, as of November 2015 (See Appendix for more information of GASB standards on the format of the financial report and method of accounting). Large counties — with more than 500,000 residents — are the most likely to follow GAAP for annual financial reporting (92 percent of large counties). The majority of counties of smaller sizes — 87 percent of mid-sized counties, with populations between 50,000 and 500,000 and 64 percent of small counties, with less than 50,000 residents — also apply GASB standards.

ALMOST A FIFTH OF COUNTIES FOLLOW STATE SPECIFIC FINANCIAL REPORTING STANDARDS.

Not all counties, however, follow GAAP. Almost a fifth (19 percent) of counties use a financial reporting format decided by their state (henceforth, "regulatory basis statements") and other comprehensive basis of accounting (OCBOA) and ten percent of county governments use basic financial statements, but not accrual accounting (they use OCBOA) (See Map 2).

STATE-SPECIFIC REGULATORY FINANCIAL REPORTING REQUIREMENTS AND OCBOA ARE THE STANDARD FOR 19 PERCENT OF COUNTY GOVERNMENTS. The overwhelming majority of these counties are in all nine of the regulatory states (Ark., Ind., Kan., Ky., Mo., N.J., Okla., Vt. and Wash.), mostly in the Midwest and South. All the counties in Ark., N.J. and Vt. file reports in accordance with state regulatory requirements. They do not employ either the GAAP format of financial statements (basic financial statements) or the method of accounting (accrual). Instead, they use the format decided by their state and accounting bases other than accrual. The state determines the funds and methodology to be used primarily for compliance with legal provisions and budgetary restrictions.[10] Most of these county governments are on the smaller side; 83 percent of them have less than 50,000 residents. However, nine large counties (all large counties in N.J.) also implement this type of financial reporting. Bergen County, N.J. is the largest county filing a regulatory basis statement, with more than 933,000 residents in 2014.

83% OF COUNTIES THAT REPORT ACCORDING TO STATE REGULATORY REQUIREMENTS HAVE LESS THAN 50,000 RESIDENTS.

While state requirements for accounting methods and formats for county financial reports vary widely, the one commonality is the requirement that counties report by fund type. Unlike government-wide statements that disaggregate financial information by fund and present primary government financial activities as a whole, the state regulatory requirements examine county government funds as separate, distinct accounts that cannot be added together. The funds that counties report differ according to state regulations. For example, Oklahoma counties must produce financial statements that present only the funds representing 10 percent or more of the county's total revenue.[11] Indiana and Missouri counties must report all county funds as separate line items.[12] Meanwhile, Kentucky counties must report their funds in statements as budgeted and demonstrate that fund expenditures did not exceed the appropriated amounts in accordance with state budgeting and financial reporting laws.[13]

KEY TERMS USED IN THIS STUDY

GOVERNMENT-WIDE FINANCIAL STATEMENTS Presentation of a government's financial information; includes all governmental and business-type activities without displaying individual funds or fund types. The information is presented in two statements, the statement of net position and the statement of activities.

STATEMENT OF ACTIVITIES Financial statement within the government-wide financial statements that demonstrates the gross and net costs by function of the primary government and component units, which are supported by general and program revenues.

ENTERPRISE FUNDS A type of proprietary fund that accounts for goods and services provided by the government to the public on a charge, user fee basis. Fund financial statements report enterprise funds.

COMPONENT UNITS Legally separate entities for which the primary government is fiscally accountable. Examples include school districts, sanitary commissions and housing authorities.[15]

MODIFIED CASH BASIS OF ACCOUNTING Accounting method that combines elements of cash and accrual methods of accounting. The modified cash basis of accounting generally uses the accrual method of accounting for fixed liabilities and assets and the cash basis method for short-term items when transactions occur. Generally, different from GASB standards.

KEY TERMS USED IN THIS STUDY

PRIMARY GOVERNMENT A local government with independent authority to determine its own budget, levy taxes, and issue bonds.[14]

COMPONENT UNITS Legally separate entities for which the primary government is fiscally accountable. Examples include school districts, sanitary commissions and housing authorities.[15]

A SMALL PERCENTAGE OF COUNTIES REPORT THEIR FINANCIALS IN THE FORM OF BASIC FINANCIAL STATEMENTS, BUT USE OCBOA FOR ACCOUNTING.

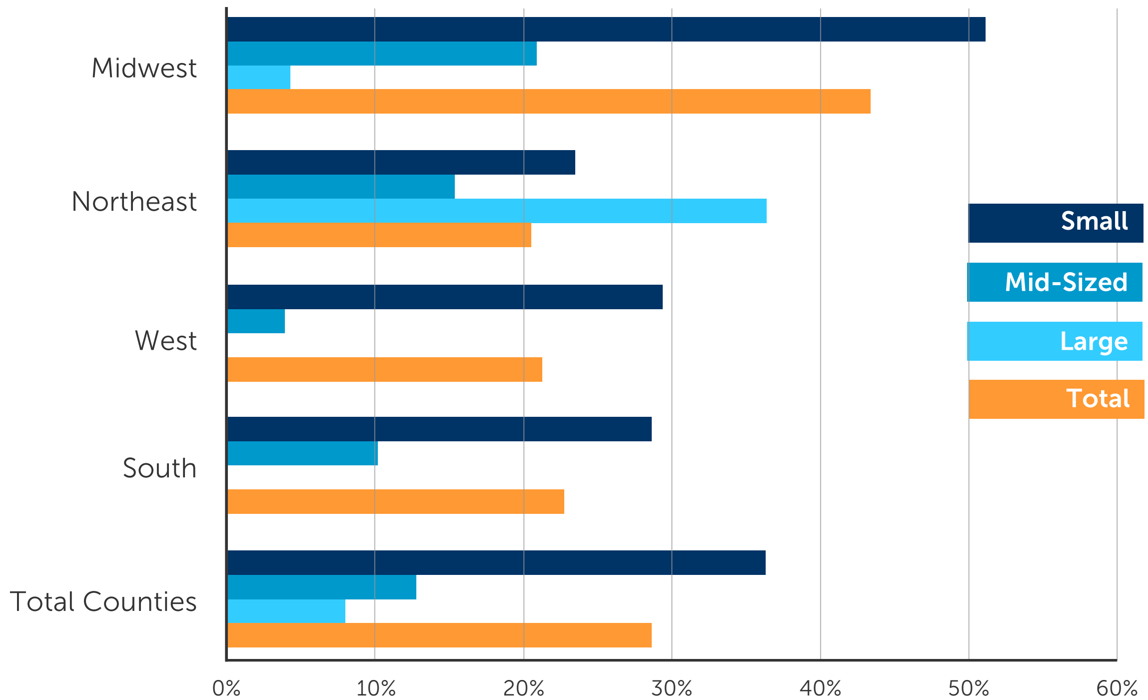
DIFFERENCES WITH GASB BASIC FINANCIAL STATEMENTS. The state regulatory basis statements differ from basic financial statements done on an accrual basis of accounting in a number of ways. While the state regulatory statements present the primary government financials by fund type, the GASB-approved statement of activities aggregates the financial activity of the county by major function/program. The regulatory basis statements blend the enterprise revenues within funds and do not delineate business-type activities as in government-wide financial statements. Another distinct difference is the absence of the financials of county component units from the regulatory basis county financial statements. The component units of New Jersey counties, such as vocational school districts, economic development authorities and utilities authorities, produce separate financial reports from the county financial statement. The regulatory basis statements do not include management's discussion and analysis, as the basic financial statements do.

These county governments also use other comprehensive bases of accounting (OCBOA) that are different from GAAP standards. These include a cash basis of accounting, which recognizes revenues when transaction occurs and expenses when paid for, and a modified cash basis accounting, which combines cash basis and accrual basis of accounting. Modified cash basis of accounting uses accrual accounting for expenditures and cash basis for revenues (See Key Terms for definitions). These methods are different from the accrual basis of accounting. In the case of the accrual method of accounting, when a county receives an invoice from an outside party, for example, the county records the full expense of the invoice before any payment is made by the county to the outside party. With the cash basis of accounting, however, the county would record the invoice as an expense only when the county paid the invoice in cash. The accounting literature is still debating the benefits and costs of using different methods of accounting. Counties may use OCBOA for several reasons. Small county governments may view GAAP reporting as less useful for budgetary and administrative decision-making.[16] Preparing financial statements on an accrual basis of accounting may be labor intensive for counties that track their annual financial activities on a cash basis. Some voices in the accounting literature consider cash and modified cash basis of accounting easier to understand, verify and execute.[17]

FIGURE 1.

ABOUT A THIRD OF COUNTY GOVERNMENTS USE OTHER COMPREHENSIVE BASIS OF ACCOUNTING (OCBOA)

AS OF NOVEMBER 2015, PERCENTAGE OF COUNTY GOVERNMENTS BY REGION THAT USE OCBOA



Notes: "Small" counties are county governments of counties with less than 50,000 residents, living in both incorporated and unincorporated areas, as of 2014; "mid-sized" counties are county governments of counties with populations between 50,000 and 500,000 residents, living in both incorporated and unincorporated areas, as of 2014; and "large" counties are county governments of counties with more than 500,000 residents, living in both incorporated and unincorporated areas, as of 2014. Regions follow U.S. Census Bureau delineations. This study identified the type of financial report and method of accounting for 3,053 of the 3,069 county governments.

KEY TERMS USED IN THIS STUDY

STATEMENT OF NET POSITION Financial statement within the government-wide financial statements that demonstrates the financial position of the government at the end of the fiscal year. This statement presents all capital assets and the depreciation expense of those assets.

COUNTY EXPENDITURE Spending by the county government in order to perform key functions financed by county revenues.

COUNTY REVENUES County government income from taxes, fees, borrowing and grants.

RECEIVABLES A county's claim to future collections of cash or assets.

GOVERNMENT FINANCE OFFICERS ASSOCIATION An international organization that represents public finance officials in Canada and the United States and works to promote the professional management of governmental financial resources.

A SMALL PERCENTAGE OF COUNTIES (10 PERCENT) REPORT THEIR FINANCIALS IN THE FORM OF BASIC FINANCIAL STATEMENTS, BUT USE OCBOA FOR ACCOUNTING. The overwhelming majority of these counties (94%) have less than 50,000 residents. The vast majority of them are in the seven states with minimum financial reporting standards (Ala., Del., Ill., Neb., N.Y., S.C. and S.D.). Further, 44 counties in regulatory states elect to report according to GASB standards in the form of basic financial statements, but do not use the accrual method of accounting that is required by GAAP. Forty-three of these counties are in Kentucky and Missouri. Marion County, Ind. — with a population of 934,243 — is the other county in a regulatory state that uses OCBOA for its financial reports. Compliance with GAAP is optional for counties in all these states. Even though these counties use basic financial statements — and have a statement of net position and statement of activities — their financials are not comparable with those counties that use basic financial statements and accrual basis of accounting. Because they use OCBOA (mainly cash basis accounting), the amounts shown for primary government functions in the statement of activities and net position do not include the costs and revenues incurred during the fiscal year that have outstanding payments or receivables. For example, their statement of net position would not include any depreciation of county-owned properties or investments earned for post-employment benefits but not yet paid.

ABOUT A THIRD OF COUNTY GOVERNMENTS DO NOT USE ACCRUAL BASIS OF ACCOUNTING, RELYING ON OCBOA INSTEAD. Midwestern counties are most likely to use other methods of accounting than any other region (See Figure 1). Forty-three (43) percent of Midwestern counties report using other methods of accounting than accrual; these are mostly counties on the smaller side (less than 50,000 residents). While 21 percent of Northeastern counties report with alternative methods of accounting to GAAP, more than a third of large counties in this region use OCBOA because of New Jersey State's strict requirements for counties. In contrast, all the Western and Southern large county governments use accrual basis of accounting, as approved by GASB.

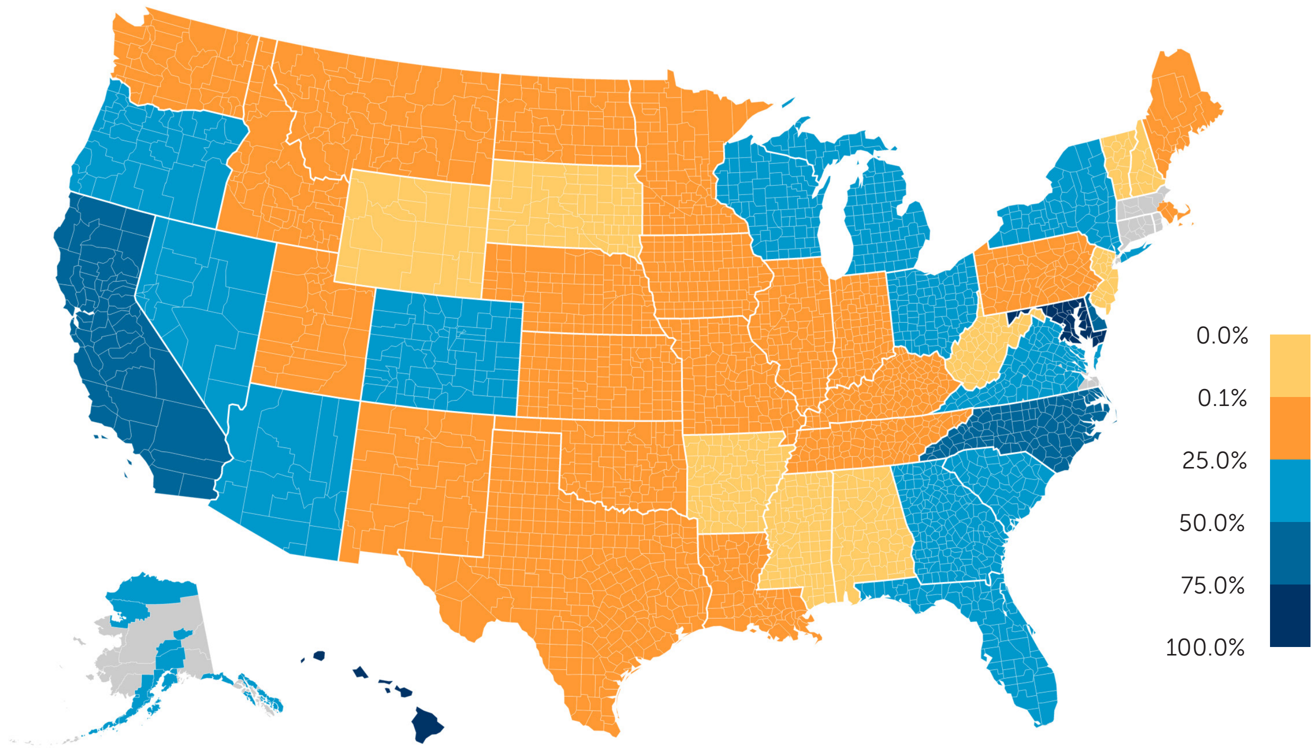
GAAP is the standard for 71 percent of counties, but not all. About 19 percent of counties financially report according to state regulatory standards in order to meet the financial and budgetary requirements of their state governments. Another fraction of counties use the basic financial statements format required by GASB but use OCBOA to suit county needs. The variation in financial reporting among counties nationwide shows the diversity of state regulatory requirements, county needs and the staffing and administrative capacity of county governments.

3 A QUARTER OF COUNTY GOVERNMENTS FOLLOWING GASB STANDARDS PRODUCE COMPREHENSIVE ANNUAL FINANCIAL REPORTS (CAFRs). The Government Finance Officers Association (GFOA) and GASB consider Comprehensive Annual Financial Reports (CAFRs) to be the most thorough version of financial reporting. These financial reports have to fulfill GASB standards and GFOA requirements, as established by GFOA's Certificate of Achievement for Excellence in Financial Reporting Program. They are expanded basic financial statements on an accrual accounting basis, intended to provide a more robust financial and historical context of the county government. Besides the basic financial statements, a CAFR has a defined introductory section — table of contents, letter of transmittal and organizational chart for the county government — intended to familiarize the reader with the report. Further, it includes a statistical section with additional financial and statistical data, such as financial trends, debt capacity and demographics and economy, relevant to understanding the county financial standing. CAFRs are not required, but encouraged by GASB and GFOA as a best practice.

A QUARTER OF COUNTY GOVERNMENTS FOLLOWING GAAP COMPILE CAFRs.

MAP 3. COUNTIES IN 39 STATES AND THE DISTRICT OF COLUMBIA ISSUE CAFRs FOR THEIR FINANCIAL STATEMENTS

AS OF NOVEMBER 2015



Notes: Comprehensive Annual Financial Reports (CAFRs) are the most thorough version of financial reporting that must fulfill GASB standards and GFOA requirements, as established by GFOA's Certificate of Achievement for Excellence in Financial Reporting Program.

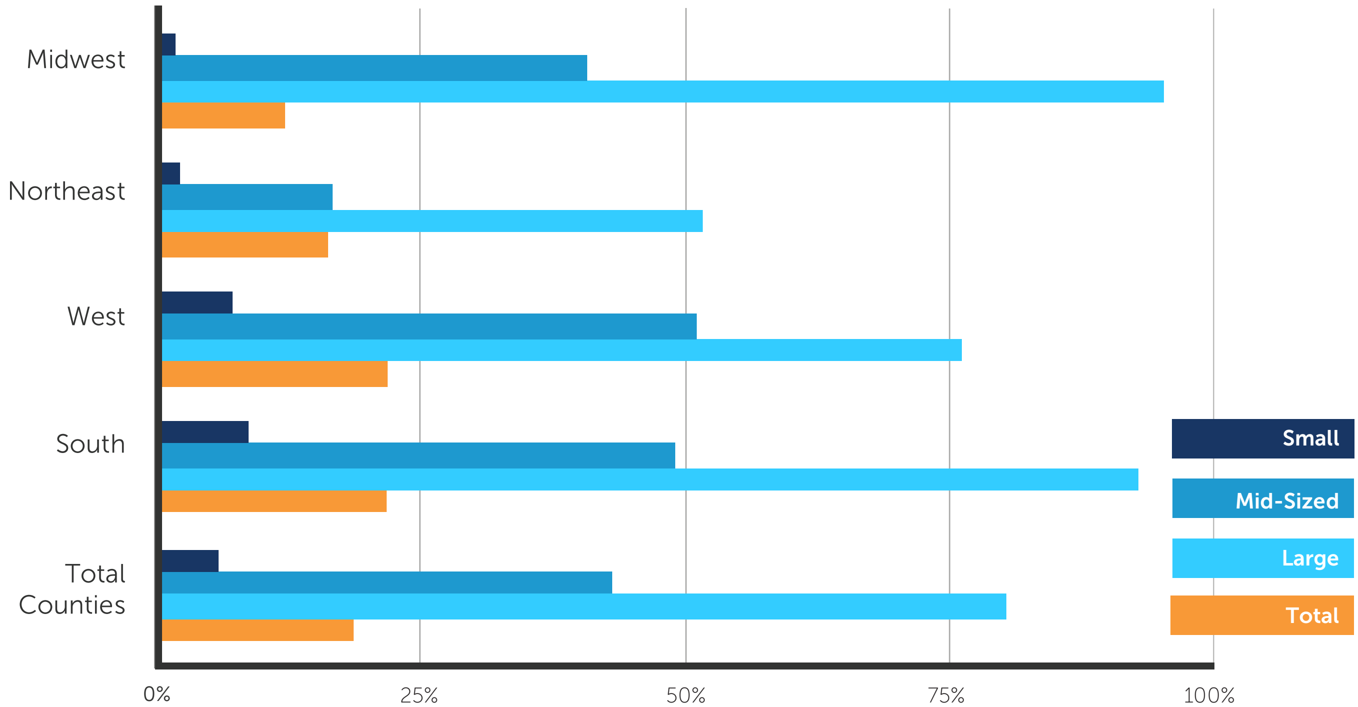
This study identified the type of financial report and method of accounting for 3,053 of the 3,069 county governments. Conn., R.I., and parts of Mass. have counties or county-equivalents with no county governments (marked in grey on the map).

A quarter of county governments following GAAP compile CAFRs. County governments opt to report their financial statements as a CAFR for a couple of reasons. A CAFR's additional discussions and analyses of county trends and statistical data add to the picture of a county's financial standing. Bond rating agencies and bondholders use the additional information from a CAFR to assess the investment risk of the county government.[18] By completing a CAFR, a county can submit their audited financial statement for consideration for the Government Financial Officers Association (GFOA)'s Certificate of Excellence in Financial Reporting. Receiving GFOA's certificate increases the chances that credit agencies or other stakeholders may consider the county's financials positively.

The 567 counties that issue CAFRs are found across 39 different states and the District of Columbia (See Map 3). Western and Southern counties are most likely to use a CAFR for financial reporting. The majority of counties in five states (Calif., Del., Hawaii, Md. and N.C.) use CAFRs. Hawaii is the only state in which all the counties release a CAFR for their annual financial report. The counties that report CAFRs are also in regulatory states, but in much smaller numbers. Three percent of counties in states with regulatory reporting requirements (Kan., Ky., Mo. and Okla.) use CAFRs, half of which are mid-sized counties (populations between 50,000 and 500,000). None of the counties in the remaining six non-regulatory states (Ala., Miss., N.H., S.D., W.Va. and Wyo.) report with CAFRs.

FIGURE 2. LARGER COUNTIES ARE MOST LIKELY TO COMPILE CAFRs

AS OF NOVEMBER 2015, PERCENTAGE OF COUNTY GOVERNMENTS BY REGION THAT REPORT WITH CAFRS



Notes: "Small" counties are county governments of counties with less than 50,000 residents, living in both incorporated and unincorporated areas, as of 2014; "mid-sized" counties are county governments of counties with populations between 50,000 and 500,000 residents, living in both incorporated and unincorporated areas, as of 2014; and "large" counties are county governments of counties with more than 500,000 residents, living in both incorporated and unincorporated areas, as of 2014. Regions follow U.S. Census Bureau delineations. This study identified the type of financial report and method of accounting for 3,053 of the 3,069 county governments. CAFR is an acronym for Comprehensive Annual Financial Reports, the most thorough version of financial reporting that must fulfill GASB standards and GFOA requirements, as established by GFOA's Certificate of Achievement for Excellence in Financial Reporting Program.

Larger county governments are more likely to compile CAFRs (See Figure 2). Releasing a CAFR helps counties that issue municipal bonds more regularly. The larger county governments are more likely to issue municipal bonds to fund capital investment and they also have larger tax bases to back general obligation bonds. Often, large counties have in-house staff that structures the county's municipal bonds.[19] Eighty-one percent of large counties — with more than 500,000 people — report using a CAFR. In comparison, 43 percent of mid-sized counties (with populations between 50,000 and 500,000) compile this extended financial report. Only 5 percent of small counties (with less than 50,000 people) issue CAFRs. Cheyenne County, Colo. is the least populous county in the country compiling a CAFR (1,871 residents in 2014). Regardless of size, counties in the West and South are most likely to report with a CAFR. About a fifth of counties in each of these regions report CAFRs (See Figure 2). Further, the majority (51 percent) of western mid-sized counties use CAFRs. Few of the Midwestern counties report with CAFRs, with the exception of their large counties; 96 percent of large counties in the Midwest use this extended financial report.

Counties that seek to receive awards and favorable ratings from credit and bond rating agencies elect to report a CAFR. These expanded basic financial statements provide a robust financial and historical context of the county government. CAFRs are not exclusive to large county governments, but counties who issue municipal bonds more regularly are more likely to release CAFRs.

CONCLUSION

Understanding county financial reporting helps comprehend how counties function and deliver services to their constituents. As local governments under the jurisdiction of the states, counties observe accounting procedures designated by their state legislatures and statutes. Often, states defer to GASB standards for rules for county financial reporting. While the majority of counties follow GASB, some states have different reporting requirements for their counties. County adherence to state and GASB standards and the amount of information disclosed in their financial reports may influence county government creditworthiness.

This study shows the diversity of financial reporting, state rules for county financial reporting and county financials among county governments. A majority of counties follow GASB standards when compiling their annual financial reports, primarily because their state requires adherence to GAAP. In addition, about 10 percent of counties use cash or modified cash basis of accounting (OCBOA), methods of accounting different from GASB standards, while reporting with GASB approved formats (basic financial statements). Finally, close to 20 percent of county governments follow state specific methods of accounting and reporting that are different from GASB standards.

Counties constantly balance serving residents while meeting the demands of state and federal mandates. Ongoing changes to GASB standards affect the majority of counties in how they report their annual financials. An understanding of the nature of the county financial data provides the basis for future policy research in county finance.

APPENDIX: GASB STANDARDS FOR COUNTY FINANCIAL REPORTING

County governments that follow GASB standards for their financial reports for audit review compile basic financial statements and mainly use an accrual basis of accounting.[20] As standardized by GASB Statement No. 34 in 2002, the basic financial statements include fund financial statements that report on the county's major funds; government-wide financial statements that report on the county government as a whole; and notes to financial statements.

THE COMPOSITION OF BASIC FINANCIAL STATEMENTS

FUND FINANCIAL STATEMENTS report county revenues and expenditures by major fund type and non-major fund type. Major funds include governmental and enterprise funds. While the governmental funds are the chief operating funds of the county government, enterprise funds report the financials on county activities that charge user fees. Non-major funds represent governmental and enterprise funds that make up less than 10 percent of the funds in that category (governmental or enterprise) and less than 5 percent of the combined total of governmental and enterprise funds. Separate fund statements report internal service funds (a type of proprietary fund for cost reimbursements for goods or services within county government) and fiduciary fund information (the pension, investment and private-purpose trusts of the county government and agency funds).

KEY TERMS USED IN THIS STUDY

FUND FINANCIAL STATEMENTS The statements of primary government funds established by legal requirements or legislative action. They are part of the basic financial statements and include separate balance sheets per fund type. Fund types include fiduciary, governmental and proprietary funds.

MAJOR FUNDS Types of governmental or enterprise funds that are the largest within their category (governmental or enterprise).[21] A governmental or enterprise fund qualifies as a major fund if its total assets, liabilities, revenues or expenditures are at least 10 percent of the total for the funds in that category (governmental or enterprise) and at least 5 percent of the combined total of governmental and enterprise funds. All other governmental or enterprise funds may qualify as a major fund if the reporting entity determines that those funds are important to the understanding of the financial position of the public entity. The fund financial statements report the financials of major funds.

GOVERNMENTAL FUNDS Funds that account for tax-supported activities and include the general fund, special revenue funds, debt service funds, capital project funds and permanent funds. The fund financial statements report on governmental funds.

AGENCY FUNDS A type of fund that accounts for assets held by the government for purely custodial purposes, such as payroll deduction collections and payments. In a county financial statement, it is part of the fiduciary funds and reported in the fund financial statements.

USER FEES Government entity charges for services provided or use of government assets, such as road tolls, park entry fees and parking charges.

INTERNAL SERVICE FUNDS A type of proprietary fund that accounts for cost-reimbursements for goods or services to other government funds, departments, agencies or component units within the county government.

GOVERNMENT-WIDE STATEMENTS report the totality of the financial activities of the governmental and enterprise activities of the primary government and component units — the legally separate entities for which the primary government is fiscally accountable. Governmental activities are services primarily funded through a dedicated tax revenue stream, while enterprise (or business-type) activities are funded by user fees (such as road tolls, park entry fees and parking charges). These statements show the financial sustainability of the county government as an entity and the change in the county's net position over the previous fiscal year.[22]

The government-wide statements include a statement of net position and a statement of activities. The financial reports reflect an economic resources measurement focus, meaning that the organization of the statements and method of accounting allow for the examination of all of the revenues, expenditures, assets and outstanding balances of the county government. The statement of activities includes revenues, expenses, gains and losses, while the statement of net position reports the county assets and liabilities. Each statement distinguishes between the governmental and business-type activities of the primary government.

STATEMENT OF ACTIVITIES

COUNTY EXPENDITURES. The statement of activities shows county expenditures as expenses for primary government functions (such as judicial and public safety programs) and business-type activities (such as waste disposal and collection and permitting services) (See Table 1). The expenditure categories differ from county to county, depending on the primary government's functions and programs, as well as the county's business-type activities. For example, the fiscal year 2013 statement of activities of Prince George's County, Md., presents seven primary governmental activities, such as "health and human services," "public safety" and "infrastructure and development." Alternatively, Calvert County, Md., financial statement for fiscal year 2013 listed 11 different primary governmental activities and reported separately "social services" and "health and hospital," instead of "health and human services."

The statement of activities also shows separately the expenses of the county's component units – legally separate entities for which the primary government is fiscally accountable, such as school districts, sanitary commissions and housing authorities (See Table A1). As legally separate entities, their expenses are not included in the county government's expenses. Component units are distinctly apart from the primary government as they have their own appointed or elected members that decide their policy. For example, one of Broward County, Fla.'s component units is the Housing Finance Authority. The board of Broward County, Fla., Housing Finance Authority retains the authority to set the agency's policies. However, the Broward County Board of Commissioners appoints the members of this board.[23]

COUNTY REVENUES. Total county revenues include both revenue restricted to a specific activity (program revenues) and unrestricted county general revenues. The statement of activities links the expenditures of each governmental and business-type activity to their program revenue sources (See Table A1). The program revenue for an activity is the income generated by charges for services provided under that activity ("charges for services") or intergovernmental grants and contributions restricted to meet operational or capital requirements ("operating grants and contributions" and "capital grants and contributions"). GASB standardizes these three types of program revenue and they appear regularly in the statement of activities of county governments

KEY TERMS USED IN THIS STUDY

INVESTMENT TRUST FUND A type of fiduciary fund that represents the combined resources in investment portfolios for the benefit of bondholders. Resources include the investment of the government's own money and from other governments. Investment trust funds resemble the arrangement of mutual trust funds in the private sector. Fund financial statements report investment trust funds.

FIDUCIARY FUNDS Funds held by a government, but belonging to individuals or other entities. The government acts as the disbursing or collecting agent for these funds. These include pension trusts, investment trusts, private-purpose trusts and agency funds. Fund financial statements report fiduciary funds.

PRIVATE-PURPOSE TRUST FUND A type of fiduciary fund that accounts for funds other than investment and pension trust funds. Private-purpose funds account for trust arrangements where the purpose of the fund benefits individuals, organizations or other governments. Examples include scholarship trust funds or funds allotted for county court appointed guardians. The fund financial statements report on private-purpose trust funds.

PROPRIETARY FUNDS Government funds financed by user fees activities. It includes enterprise and internal service funds. The fund financial statements report the financials of the proprietary funds.

ASSETS Cash or items of ownership that can be converted into cash.

LIABILITIES Debts and financial obligations.

TABLE A1. STYLIZED TABLE OF GOVERNMENT-WIDE STATEMENT OF ACTIVITIES

			PROGRAM REVENUE			NET (EXPENSE) REVENUE AND CHANGES IN NET POSITION	
	FUNCTIONS/PROGRAMS	EXPENSES	CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS	PRIMARY GOVERNMENT	COMPONENT UNITS
Governmental Activities (examples):	General government	1	8	15	22	(8+15+22)-1	
	Public safety	2	9	16	23	(9+16+23)-2	
	Transportation	3	10	17	24	(10+17+24)-3	
	Environmental protection	4	11	18	25	(11+18+25)-4	
	Economic and physical development	5	12	19	26	(12+19+26)-5	
	Human services	6	13	20	27	(13+20+27)-6	
	Workforce development	7	14	21	28	(14+21+28)-7	
Total Governmental Activities		**Total Expenses for Governmental Activities (1+...+7)**	**Total Charges for Services for Governmental Activities (8+..+14)**	**Total Operating Grants and Contributions for Governmental Activities (15+...+21)**	**Total Capital Grants and Contributions for Governmental Activities (22+...+28)**	**Total Program Revenues- Total Expenses for Governmental Activities**	
Business-Type Activities (examples):	Airport	29	33	37	41	(33+37+41)-29	
	Permitting services	30	34	38	42	(34+38+42)-30	
	Waste disposal and collection	31	35	39	43	(35+39+43)-31	
	Water management	32	36	40	44	(36+40+44)-32	
Total Business-Type Activities		**Total Expenses for Business-Type Activities (29+...+32)**	**Total Charges for Services for Business-Type Activities (33+...36)**	**Total Operating Grants and Contributions for Business-Type Activities (37+...+40)**	**Total Capital Grants and Contributions for Business-Type Activities (41+...+44)**	**Total Program Revenues - Total Expenses for Business-Type Activities**	
TOTAL PRIMARY GOVERNMENT		**Total Expenses for Governmental Activities and for Business-Type Activities**	**Total Charges for Services for Governmental Activities and for Business-Type Activities**	**Total Operating Grants and Contributions for Governmental Activities and for Business-Type Activities**	**Total Capital Grants and Contributions for Governmental Activities and for Business-Type Activities**	**Total Program Revenues- Total Expenses for Governmental Activities and for Business-Type Activities**	
Component Units (examples):	Affordable housing (Housing Finance Authority)	45	48	51	54		(48+51+54)-45
	Landfill (Solid Waste Authority)	46	49	52	55		(49+52+55)-46
	Elementary and Secondary Education(School Board)	47	50	53	56		(50+53+56)-47
TOTAL COMPONENT UNITS		Total Expenses for Component Units (45+...+47)	Total Charges for Services for Component Units (48+...+50)	Total Operating Grants and Contributions for Component Units (51+...+53)	Total Capital Grants and Contributions for Component Units (54+...+56)		Total Program Revenues - Total Expenses for Component Units
General Revenues (examples):	Property taxes					57	62
	County income taxes					58	63
	Hotel-motel taxes					59	64
	Investment income					60	65
	Transfers					61	66
	Total General Revenues & Transfers					(57+58+59+60+61)	(62+63+64+65+66)
	Change in Net Position					(Total Program Revenues- Total Expenses) + Total General Revenues and Transfers for Primary Government	(Total Program Revenues- Total Expenses) + Total General Revenues and Transfers for Component Units
	Net position – beginning of the fiscal year					Net Position at the beginning of the current Fiscal Year for Primary Government	Net Position at the beginning of the current Fiscal Year for Component Units
	Net position – ending of the fiscal year					Net Position at the beginning of the current Fiscal Year + Change in Net Position for Primary Government	Net Position at the beginning of the current Fiscal Year + Change in Net Position for Component Units

that follow GAAP. However, the county government might not generate all the types of program revenue for each of its governmental and business-type activities. For example, in the fiscal year 2013 financial statement of Tuscaloosa County, Ala., none of the eight government functions reported program revenues generated from capital grants and contributions, whereas nearly half of the government functions in Shelby County, Ala., financial statement had associated revenues from capital grants and contributions in the county's fiscal year 2013.

The statement of activities keeps track of the difference between expenses and program revenues separately for each of the governmental activities, business-type activities and component units. The total revenue of the primary government does not include the revenues from component units. County general revenues and transfers among county programs cover the difference, in case program revenues come short of expenses. The result is the change in net position of the county, which shows how the financial position of the government has changed over the fiscal year. Added to the net position from the beginning of the fiscal year, it yields the net position of the county government at the end of the fiscal year (See Table A1).

STATEMENT OF NET POSITION. Accompanying the statement of activities, the statement of net position presents the county's assets and liabilities of the primary government's governmental and business-type activities, as well as the associated component units. County assets range from highly liquid cash and receivables to illiquid capital assets, like county owned buildings or trucks. The county's outstanding liabilities delineate items such as accounts payable, deposits, dues within county government, to component units or other governments as well as non-current liabilities Amounts disclosed for liabilities show the remaining balances to be paid off. The difference between total assets and total liabilities is the county's net position, which matches the end result within the statement of activities.

KEY TERMS USED IN THIS STUDY

CAPITAL GRANTS AND CONTRIBUTIONS A type of program revenue encompassing grants and contributions from other governments or organizations restricted for capital purposes (construction, purchasing or renovations for capital assets) associated with a specific program. The statement of activities reports capital grants and contributions.

OPERATING GRANTS AND CONTRIBUTIONS A type of program revenue encompassing multi-purpose grants and contributions from transactions with other governments or organizations restricted for specific program use for operating expenses or capital assets. The statement of activities reports operating grants and contributions.

PROGRAM REVENUES Fees or charges to the customers who use a specific government service. It also includes grants and contributions restricted for specific program use, for operational or capital purposes.[24]

TRANSFERS The movement of financial resources between governmental and business-type activities, as well as the primary government's component units. The statement of activities reports transfers within the general revenues section.

NON-CURRENT LIABILITIES Long-term financial obligations not due within the present fiscal year.

NET ASSETS: Cash and resources left after the county has paid its debts. Net assets are calculated by subtracting total assets from total liabilities.

TABLE A2. STYLIZED TABLE OF GOVERNMENT-WIDE STATEMENT OF NET POSITION WITH GASB 68 CHANGES, FISCAL YEARS AFTER JUNE 2014

		GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL PRIMARY GOVERNMENT	COMPONENT UNITS
ASSETS	CASH AND CASH EQUIVALENTS	$ 15,000,000			
	NET RECEIVABLES	$ 5,000,000			
	CAPITAL ASSETS	$ 65,000,000			
	TOTAL ASSETS	$ 85,000,000			
LIABILITIES	PAYABLES	$ 300,000			
	LONG-TERM LIABILITIES	$ 70,000,000			
	NET PENSION LIABILITIES	$ 50,000,000			
	TOTAL LIABILITIES	$ 120,300,000			
	TOTAL NET POSITION	($ 35,300,000)			

Source: California Committee on Municipal Accounting, "Implementing GASB Statement No. 68 Accounting and Financial Reporting for Pensions: A CCMA White Paper for Cal. Local Governments"(2015).

The items within the statement of net position may change depending on new GASB standards. For example, for fiscal years after June 15, 2014, GASB Statement No. 68 requires that all state and local governments must include within the statement of net position a "net pension liability," as a new, separate liability (See Table A2). Previously, outstanding county employee pension obligations were sections within notes to financial statements and required supplementary information tracked by reporting the schedules when promised benefits are to be paid. Starting with fiscal year 2015 financial statements, the statement of net position will feature a "net pension liability" on an accrual basis with pending pension contributions expensed immediately. This change in GASB standards presents potential problems for county governments. Component units of county government and internal service funds may be adversely affected if there are significant employee cost allocations. Further, the added liabilities may be sufficiently large enough to negatively skew the value of the county's ending net position.[25]

KEY TERMS USED IN THIS STUDY

NOTES TO THE FINANCIAL STATEMENTS Additional information provided for financial statements, such as method of accounting used, description of major county funds and notes about any depreciating assets.

REQUIRED SUPPLEMENTARY INFORMATION Budgetary comparisons and schedules, pension fund data and statements about infrastructure maintenance and condition. This is information deemed by GASB to be relevant to the county fiscal condition.[26]

PENSION TRUST FUND A type of fiduciary fund established by an employer to facilitate and organize the investments of employees' retirement funds contributed by employers and employees. Fund financial statements report pension trust funds.

MODIFIED ACCRUAL BASIS OF ACCOUNTING A combination of cash basis and accrual basis accounting. It accounts revenues on a cash basis, when the revenue is available for use within the next 60 days. Expenditures use accrual basis, accounted for when incurred. GASB approves this method of accounting for reporting the fund financial statements.

NOTES TO FINANCIAL STATEMENTS AS REQUIRED BY GASB STANDARDS provide additional information about the government's basic financial statements not conveyed by the government-wide or fund statements. Items include background of the county government, like the history or government structure, an explanation of the financial reporting standards applied to the statements, as well as the accounting methods used for government-wide and fund statements. Additional information may refer to the used methods of valuation and depreciation for county assets. Notes to financial statements also describe the primary government's relationship to their associated component units.

ACCRUAL ACCOUNTING METHOD. The GAAP observing counties employ an accrual accounting method, which requires the county to report expenses and revenues when expenses and revenues occur, not necessarily when cash is paid. For example, when a county receives an invoice from an outside contractor, the county records the full expense of the invoice before the county pays the invoice in full. The accounting literature is still debating the benefits and costs of using the accrual basis of accounting. Some financial organizations consider accrual basis of accounting as most reflective of county economic health.[27] Yet, some sources consider the accrual method of accounting to be overly complex, potentially leading to more errors by smaller governments and encouraging the overstatement of total revenues by inflating income and receivables.[28] County governments that follow GASB standards report the government-wide statements on an accrual accounting method. GASB approves the use of the modified accrual basis of accounting only for the governmental fund financial statements. Modified accrual accounting is a combination of the accrual and cash bases of accounting, which records revenues when they become available (cash basis accounting) and recognizes expenditures when incurred (accrual basis accounting). Governmental funds are expected to be used within a fiscal year since those funds provide direct services – such as public safety and capital improvements to roads.

As standardized by GASB, the elements of basic financial statements come together and tell the financial story of county governments. Presented as a whole, the fund financial statements, government-wide financial statements and notes to financial statements depict the economic resources of a county when earned, allowing users to understand the short and long-term financial narrative of county government.

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ABOUT NACo

The National Association of Counties (NACo) is the only national organization that represents county governments in the United States. Founded in 1935, NACo provides essential services to the nation's 3,069 counties. NACo advances issues with a unified voice before the federal government, improves the public's understanding of county government, assists counties in finding and sharing innovative solutions through education and research and provides value-added services to save counties and taxpayers money. For more information about NACo, visit **www.NACo.org**.

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