

# CHAPTER 1

## INTRODUCTION TO THE UNIFORM MUNICIPAL ACCOUNTING SYSTEM

### Background

Since the late nineteenth century, the various cities and towns in the Commonwealth of Massachusetts have kept their accounting records in a manner prescribed by the "Uniform Municipal Accounting System" (UMAS). This system was developed and has been maintained and administered by the State Department of Revenue through the Bureau of Accounts. UMAS is one of, if not the oldest, statewide uniform municipal accounting systems in the country.

UMAS has served the Commonwealth of Massachusetts and its communities well since its implementation. In several other states where a less structured approach to municipal accounting was taken, municipalities developed their own systems of accounting and reporting. The result was a hodgepodge of reporting formats that were not easily comparable among communities within the state, and were much less comparable with reports issued by municipalities in other states. The Massachusetts system is reasonably comprehensive and includes a chart of accounts, limited fund structure and recommended forms to complement most aspects of the various systems. The use of the system by each Massachusetts community, supported by technical assistance from Bureau of Accounts personnel, has resulted in a reasonably high level of consistency in accounting and reporting within the State. Nevertheless, it has been recognized that the system has limitations and that changes are necessary to make it more responsive to today's requirements.

### Stimulus for Change

In recent years there has been increasing pressure on all levels of government to increase services while simultaneously cutting costs. The accuracy and adequacy of financial disclosure has become a particular focus of two major groups attempting to evaluate the "health" of their investment: the taxpayers and the financial community. Although every level of government is undergoing closer scrutiny, none is under more intensive pressure than local government. To understand these pressures, one needs only consider a few developments which have occurred during the past few years:

**New York City** - In 1974 the nation was alarmed to learn that its largest city was in grave danger of defaulting on certain bond issues. Subsequent investigation disclosed that its financial statements had been substantially misleading, both because of the accounting basis on which they had been prepared, and because of grossly inadequate financial disclosures.

**The Securities Acts Amendments of 1975.**- Congress reacted to the New York City revelations by passing legislation designed to regulate the minimum level of financial disclosure made by Municipalities in connection with bond offerings.

**1976 Amendment to Revenue Sharing Act** - In order to ensure proper accountability for revenue sharing funds, the 1976 amendments included a provision requiring an audit of the financial statements of municipalities receiving \$25,000 or more in entitlements.

**"Proposition 2-1/2"** - The intensity of taxpayer frustrations with increasing property tax rates was first given vent in the State of California with the passage of Proposition 13. Since that time many states have followed that lead by enacting similarly restrictive legislation. In Massachusetts, the first significant step was the implementation of a 4% tax cap in 1979. In November of 1980, however, the electorate took a second step which promises to have considerably greater impact. As this manual goes to press, the constitutional questions raised by Proposition 2-1/2 and the problems of implementation are being debated in the courts, in the State Legislature and in every community across the State. Viewed in the context of the series of events described above, however, Proposition 2-1/2 simply reflects the next step in the process; the escalation of the taxpayer's frustration with rising property taxes.

Each of these events has contributed to increase the pressure for change in virtually every area of municipal operations. Certainly, the area of financial reporting, both as to the amount of disclosure and to format, has been among those most affected. In 1979, the Municipal Finance Officers' Association (MFOA) issued a revised version of its publication "Disclosure Guidelines for State and Local Governments," which described in detail the increased degree of disclosures required in published financial statements. It also stated:

Uniformity in the presentation of financial information and the consistent application of accounting principles are essential for adequate financial reporting. To that end, financial statements should be prepared and presented in conformity with generally accepted government accounting principles ... (GAAP)."

Standard & Poors, one of the major municipal credit rating agencies, asserted in May of 1980 that it would downgrade the investment ratings on the securities of any municipality which did not prepare its published financial statements in accordance with GAAP. This position was not particularly surprising and would appear to have brought all of the increasing concerns to a logical conclusion. Governmental financial statements in accordance with GAAP, then, have become the standard of the financial marketplace for the "801s."

It was recognized that UMAS did not facilitate financial reporting in compliance with GAAP in Massachusetts. Accordingly, the investigation of the amount and nature of changes that would be necessary was undertaken.

## Development of a Revised System

Work on developing a revised system was begun in April of 1980 by the Bureau of Accounts with the assistance of the accounting and consulting firm of Touche Ross & Co. The joint project team began with an analysis of the existing system's strengths and weaknesses. This was done to ensure that the strengths of UMAS would be preserved and possibly enhanced, while its weaknesses were being minimized or eliminated.

The next step was to clearly identify differences between UMAS and GAAP. Each difference was treated as a potential change, and evaluated based upon the following criteria:

- How important is it to make the change?
- What other system will be affected by the change at the state, county and local levels?
- What types of problems will be encountered in implementing the change?
- Should the change be incorporated in every municipality?

Through this process the initial draft of a revised system was designed and developed. The system was then implemented in three pilot communities (City of Haverhill, Town of Marblehead, Town of North Reading) on July 1, 1980. At approximately the same time, the revised system was presented for comment to the Board of oversight, a project review board appointed by the Director of the Bureau of Accounts. Members of the Board included representatives from many organizations in the Commonwealth with a direct interest in municipal finance. Based on the experience in the pilot communities and the comments from the Board of Oversight, changes were incorporated into the revised system, and are presented in this manual.

## Future Directions

The Uniform Municipal Accounting System defined in this manual may be thought of as the most recent update to a uniform system initially implemented almost a century ago. In essence, it picks up where the "Greenbook"\* leaves off. As such, it is likely that the system will continue to grow and change so that it can continue to support the needs of the municipalities in the Commonwealth.

\*The "Greenbook" refers to the publication entitled "Functions of General Ledger Accounts for Uniform Municipal Accounting System" published by the Commonwealth of Massachusetts.

## Using This Manual

This manual has been developed primarily as a reference document for use by municipal accountants and auditors throughout the Commonwealth. To the extent possible, it is also intended to serve as a training tool for those unfamiliar with UMAS. In order to avoid the unnecessary proliferation of terms in the text whenever the term accountant is used, it should be understood to encompass the terms auditor, comptroller, and other such positions. When the term municipality is used, it encompasses town, city, county, school district, and other special districts. The manual has been organized into four major sections as follows:

**Overview:** Includes, in addition to this introductory chapter, a discussion of the basic accounting principles which have been incorporated into the revised system of accounting. This discussion is spread over two chapters. Chapter 2 sets forth a summary of the basic accounting principles which have been defined by the National Council on Governmental Accounting and highlights the degree to which these principles have been adopted in the revised system. Chapter 3 is a review of basic accounting and bookkeeping procedures and standards which provide a practical complement to the more theoretical discussions of Chapter 2.

**Uniform Chart of Accounts:** Deals with both the theoretical and practical aspects of the Chart of Accounts. Chapter 4, "Developing Your Own Chart," describes how to use the structure and the accounts to develop a chart which simultaneously meets local needs and supports uniform reporting at the state level. Chapter 4 should be read and understood before attempting to digest the reporting and accounting sections. The practical aspects of the chart are covered through detailed descriptions of each individual account and the types of transactions which should be classified there.

**Reporting:** Covers the three major types of reports prepared by municipal accountants:

- **Statutory Report**, which describes the financial statements and other schedules which must be submitted to the Bureau of Accounts annually.
- **Comprehensive Annual Financial Report**, which describes the financial statements which should be prepared by municipalities at the close of each fiscal year. These statements are the major source of information for the users of municipal financial information (taxpayers, lenders, and others).
- **Interim Reports**, which describe the reports that are normally used for internal, day-to-day management purposes

**Accounting:** Provides detailed discussions of the application of Massachusetts GAAP to the wide variety of accounting transactions which must be recorded by municipal financial officers. This is done through a combination of narrative and over 400 illustrative journal entries.

Several appendices have been provided which cover topics of special interest:

**Conversion:** The effort required to convert from the existing UMAS to the revised accounting system can be minimized if the conversion is done systematically. This appendix presents a discussion of the changes that have been made in the structure of the accounting system, and suggests a step-by-step plan for conversion. The process of conversion has been illustrated by means of sample worksheets and journal entries.

**Detailed Principles:** This is a lengthy, more detailed discussion of the generally accepted accounting principles incorporated in the revised system than has been included in Chapter 2. A considerable amount of the material included in this chapter was taken directly from the publication *Governmental Accounting, Auditing and Financial Reporting*, published by the Municipal Finance officers' Association in November 1980.

**Requirements for School Districts:** This appendix has been provided to assist school districts in complying with reporting requirements of the State Department of Education.

## Other Resources

Anyone who is not familiar with the basic structure and operation of municipal government in Massachusetts may find it helpful to learn about it before attempting to use this manual. Resources for obtaining such knowledge include:

Executive Office of Communities and Development - which has a variety of publications covering many aspects of municipal governance and finance.

Local municipal officers' associations which include:

- Massachusetts Municipal Association
- Massachusetts Municipal Auditors' and Accountants' Association
- Massachusetts Collectors' and Treasurers' Association
- Massachusetts Association of School Business Officials

National organizations:

- Municipal Finance Officers' Association - International City Management Association

And a variety of other groups:

- Massachusetts Taxpayers' Foundation
- Massachusetts Society of CPAs
- -League of Women Voters

Source references:

- -"Your Massachusetts Government" by Levitan and Mariner

## **Special Acknowledgement**

The term "generally accepted accounting principles" in the municipal governmental field primarily encompasses the body of information contained in the publication *Governmental Accounting, Auditing, and Financial Reporting* (GAAFR), as revised in November 1980, published by the Municipal Finance Officers' Association. Given this fact, it would have been impossible to have prepared this manual for a revised accounting system without constant reference to that publication. Accordingly, the MFOA has consented to the inclusion in this manual of several significant excerpts from GAAFR. In particular, Chapter 9, Principles of Reporting, and Appendix B, Principles of Accounting, are largely based upon or taken directly from that publication. It is suggested that every municipality in Massachusetts obtain a copy of GAAFR for ready reference by its officials.