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Exercise 3: What are the objectives of governmental financial reporting?

Financial reporting is the summarized events put into a reporting form to show managers and outsiders the present financial status of the organization and the financial results of its activities (Finkler, 2005). It contains the financial information for managers to optimize the outcomes of the organization, and for outsiders to understand how well the organization performs (p 314). Even though public and private sectors have different purposes in doing their own business, they both still require financial reporting to declare the financial standpoints. To answer the question posed above, I will describe the meaning of financial reporting, clarify its types and then explain what are the objectives of governmental financial reporting.

Financial reports are formal recording events of an organization's financial activities. These statements are the summarized financial position and financial results of the organization (p 344). There are three basic financial statements:

1. The Balance Sheet – it is the first of financial statements and also referred to as the statement of financial position. It reports on a company's information about assets, liabilities and net equity as of a specific point in time.

Assets are things that an organization or a company has as a result of its operation. This should include assets, which can “either be sold or used by the company to make products or provide services that can be sold”. Assets include tangible assets, such as buildings, vehicles and equipment. It also includes intangible assets, such as trademarks and patents.

Liabilities are amounts of debts that a company owes to others. They can be loans from banks to build a building or create a new program, rent for use of a plant, money owed to pay for its employees and so forth. They also mean goods or services that an organization or a company promises to provide customers in the future.

Owners’ equity is sometimes called capital or net worth. “It’s the money that would be left if a company sold all of its assets and paid off all of its liabilities”. This leftover money belongs to the shareholders, or the owners, of the company.

2. The Income Statement – it is also referred to as the activity statement, the operating statement and the profit or loss statement. It is a summary of revenues and expenses on a company's results of operations over a period of time.

An income statement is a report that demonstrates how well an organization or a company performs its operation. It will show revenue an organization or a company received as well as expenses it paid over a time period (usually for a year). Therefore, we will know how much it gained or lost over that specific time.

An income statement also reports earnings per share (or “EPS”). It can tell us “how much money shareholders would receive if the company decided to distribute all of the net earnings for the period”.

3. The Cash Flow Statement - it focuses on financial rather than operating aspects of the organization. While an income statement can tell whether a company made a profit, a cash flow statement can tell whether the company generated cash. Generally, cash flow statements report on three main parts. Each part reviews the cash flow from one of three types of activities: (1) operating activities; (2) investing activities; and (3) financing activities.

Cash flow statements report a company's inflows and outflows of cash. Normally, a company needs to have enough cash to go on its business. The net increase or decrease in the cash flow statement will tell us how viable a company is (www.wikipedia.org).

Financial reports are prepared by organizations each year. These financial statements clarify the financial situation and the financial results not only for managers of the organization, but for outsiders as well. (Finkler, 2005, p 344).

Internal Users are managers, employees and other persons who are directly involved with a company. The financial statements help managers to make significant business decisions to continue operations and maximize profits. "Financial analysis is then performed on these statements to provide management with a more detailed understanding of the figures". These statements are also used as part of management's report to people involved with a company. For employee, they also need these reports in making collective bargaining agreements (CBA) with the management, in the case of labor unions or for individuals in discussing their benefits such as compensation, promotion and rankings.

External Users are outside user such as banks, donors, landlords, government agencies and other persons who are outside the business but require financial information about the business (www. answer.com).

Governmental financial reporting is the tool to maintain accountability for the government's operation. Its first purpose is to clarify whether the organization performs job activities responsive to the public. The details in the reports will tell what goes right and what goes wrong in the organization.

The objectives of financial reporting are also to tell how the public organization works. By looking at the reports, we can compare the actual outcome with the authorized budget. We will understand the financial condition of the organization and the financial results of its operation. We also can assess that the organization follows the rule and regulation in doing its process. Finally, from the result of its operation, we can tell how effective and efficient the organization performs. In addition, the information in the governmental financial reporting will tell the user to realize whether the government reaches interperiod equity (Finkler, 2005, p 452).

As Finkler mentioned in his book, interperiod , or intergenerational, equity is about the government "has used revenues from the current period to pay for services provided in the current period". Therefore, with the reports, people will know that the government spends the money effectively and doesn't create an unfair debt for the future generation (p 453).

Governmental financial reporting uses the modified accrual basis of accounting. Under this method, the main issue is the financial resource such as cash and other assets that can be changed to be cash in the process of operations. However, government-wide statements

are also prepared on accrual basis because they can provide more details for better understanding how well a government has reached interperiod equity. As a result, government-wide statements based on accrual basis should provide information for users to do the following (p 453).

1. Understand the overall finances and operating results of the government.
2. Assess whether financial results are improving or getting worse.
3. Understand the cost of services provided to the public.
4. Understand the sources of money that government uses to pay for its programs.
5. Understand the government's investment in capital assets.
6. Be able to compare the government with other governments (p 453).

In sum, governmental financial reporting is to ensure that the public organization responds to the needs of the public. People can understand what and how the government performs its services. In addition, public managers still can use its information to improve the operations. The financial report will be a guideline for them to optimize the organization's results.

References

Steven, A. Finkler. (2005). *Financial management for public, health, and not-for-profit organizations*. New Jersey: Pearson.

<http://www.answer.com>

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