Arkansas Municipal League

Municipal Accounting Handbook

Revised August 2013

(Arkansas legislative updates revised June 2017)

INTRODUCTION

This booklet was compiled by the working group listed below that was organized by the Arkansas Municipal League. Our goal was to provide an accounting guide to assist local government employees in performing their financial and other related duties. It was specifically written for non-accountants in non-technical language

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Concerning the June 2017 Legislative Update:

The Arkansas Municipal League staff has updated this publication to reflect changes in Arkansas law resulting from the 2017 legislative session of the Arkansas General Assembly. No other material has been updated at this time, so users of this publication should verify the current status of any such information. A future update will be forthcoming. The names and positions of the working group members listed above are as they appeared in the August 2013 edition of this handbook.

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ACCOUNTING SYSTEM AND BASICS

Accounting System

Before you can set up or understand your accounting records, dive into your day to day transactions, and get your books ready for end-of-month or end-of-year reporting you must gain an understanding of basic accounting concepts.

Accounting is the method in which financial information is gathered, processed, and summarized into financial statements and reports. An accounting system is represented by the following graphic, which is explained below.

1	2	3	4	5
Business Transactions (source)	Journal Entry	General Ledger	Trial Balance	Fund Statements (Financial Statements)

Every accounting entry is based on a business transaction, which is always evidenced by a business document, such as a check or invoice or travel form.

1. A journal is a place to record the transactions of a municipality. The typical journals used to record the chronological, day-to-day transactions such as revenue and expenditures are cash receipts journals and cash disbursements journals.
2. While a journal records transactions as they happen, a ledger groups transactions according to their type, based on the accounts they affect. A general ledger is a collection of all balance sheet, revenue and expense accounts used to keep municipal accounting records. At the end of an accounting period (a calendar month), all journal entries are summarized and transferred to the general ledger accounts. This procedure is called "posting."
3. A trial balance is prepared at the end of an accounting period by adding up all the account balances in your general ledger. The sum of the debit balances should equal the sum of your credit balances. If total debits do not equal total credits you must track down the errors.
4. Finally, financial statements (fund statements consisting of balance sheets and income statements) are prepared from the information in your trial balance.

Basic accounting records are required by Arkansas law and are important because the resulting financial statements and reports assist you, your mayor, and city council in planning and making sound financial decisions.

Accounting Basics

Assets = Liabilities + Fund Balance

If you understand the definition and goals of an accounting system, you are ready to learn the following accounting concepts and definitions.

Assets: Items of value held by the municipality. Assets are balance sheet accounts. Examples of assets are cash, investments, fixed assets, etc.

Liabilities: What your municipality owes to creditors. Liabilities are balance sheet accounts. Examples are payroll taxes payable, loans and bonds payable, money due to other governmental agencies etc.

Fund Balances: The net worth of each of your funds. An accumulation of revenues received less expenses incurred. Assets, liabilities and fund balances are permanent accounts. (Do not close at the end of accounting period.) Fund Balances are reported in the following classifications:

- **Nonspendable**: Fund balances that are either not in spendable form or legally or contractually required to be maintained intact.
- **Restricted**: Fund balances which have constraints on the use of resources that are either: a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments; or b) imposed by law.
- **Committed**: Fund balances that can only be used for specific purposes pursuant to constraints imposed by ordinances.
- **Assigned**: Fund balances that are constrained by the City's intent to be used for specific purposes, but are neither restricted nor committed. Assigned fund balances include all remaining amounts (except negative fund balances) that are reported in governmental funds, other than the general fund, that are not classified as nonspendable, restricted, nor committed, and amounts in the general fund that are intended to be used for a specific purpose. Cities should not report an assigned fund balance if the assignment would result in a negative unassigned fund balance.
- **Unassigned**: Unassigned fund balance is the residual classification of the general fund. The general fund should be the only fund that reports a positive unassigned fund balance amount. In other governmental funds, if expenditures incurred for specific purposes exceeded the amounts restricted, committed, or assigned to those purposes, it may be necessary to report a negative unassigned fund balance.

The accounting equation: Assets = Liabilities + Fund Balance. Note that assets are on the left-hand side of the equation, and liabilities and fund balances are on the right-hand side of the equation.

Once you master the above accounting terms and concepts, you are ready to learn about the following day-to-day accounting terms.

Debits: At least one component of every accounting transaction (journal entry) is a debit amount. Debits increase assets and decrease liabilities and fund balance.

Credits: At least one component of every accounting transaction (journal entry) is a credit amount. Credits increase liabilities and fund balances and decrease assets.

(In bookkeeping texts, examples, and ledgers, you may see the words "Debit" and "Credit" abbreviated. **Dr.** stands for Debit; **Cr.** Stands for Credit.)

Assets = Liabilities + Equity (Fund Balance) Revenues - Expenditures

Assets	(Increase =Debit) (Decrease = Credit)
Liabilities	(Increase = Credit) (Decrease = Debit)
Fund	(Increase = Credit) (Decrease = Debit)
Revenue	(Increase = Credit) (Decrease = Debit)
Expenditures	(Increase = Debit) (Decrease = Credit)

Arkansas Municipal Accounting Law and Arkansas Municipal Water & Sewer Accounting Law

Municipal Accounting is governed by state statutes known as Arkansas Municipal Accounting Law (A.C.A. §§ 14-59-101 through 118) and Arkansas Municipal Water & Sewer Accounting Law (A.C.A. §§ 14-237-101 through 113). These statutory provisions are found in the *Handbook for Arkansas Municipal Officials* which is published bi-annually after each regular session of the Arkansas General Assembly. The statutory provisions may also be found at www.lexisnexis.com/hottopics/arcode, or at the Arkansas General Assembly website, www.arkleg.state.ar.us. The Municipal Accounting Law should be referred to for specific guidance as to the type and information that the above records are required to contain in accordance with Arkansas law. A.C.A. §§ 14-237-101 through 14-237-113, referred to as the Municipal Water and Sewer Department Accounting Law, gives specific guidance relating to accounting records for water and sewer departments.

Here you will learn the requirements for:

- Bank Accounts and Bank Reconciliations
- Prenumbered Checks and Electronic Funds Transfers
- Disbursements of municipal funds
- Petty Cash
- Fixed Assets
- Prenumbered Receipts
- Cash Receipts and Disbursements Journals
- Maintenance and destruction of records
- Annual publication of financial statement
- Turnback withholding for noncompliance

Arkansas Self-Insured Fidelity Bond Program

All Arkansas municipalities participate in the Self-Insured Fidelity Bond Program administered by the Governmental Bonding Board. This program covers actual losses sustained by the participating entity through any fraudulent or dishonest act or acts committed by any of the officials or employees, acting alone or in collusion with others, during the bond period to an amount not exceeding the lesser of $300,000 or the amount of the bond. Premiums for coverage are determined by the State Risk Manager and approved by the Board. These premiums are paid by the State Treasurer from funds withheld from the Municipal Aid Fund. There is a $2,500 deductible per occurrence. A certificate of coverage may be obtained by contacting the Risk Management Division at 501-371-2690 or via email: insurance.risk.management@arkansas.gov. Copies of the bond policy may be obtained at www.insurance.arkansas.gov/risk.htm or by contacting the Risk Management Division by phone at the number above. All Proof of Loss notices must be submitted to the Arkansas Governmental Bonding Board by the Division of Legislative Audit. Coverage is provided for funds audited in compliance with Section 4 of the Bond policy. Private audits (those not performed by Legislative Audit) must be completed within 18 months of each participating governmental entity's fiscal year end.

ACCOUNTING AND BUDGETING

Fund Accounting

A fund is an accounting entity with a set of self-balancing accounts. It is used to record financial information associated with the specific activities of that entity. Sounds simple enough. A bunch of account numbers or names that tell the financial story of an activity. Self-balancing means debits equal credits. Every time a financial transaction takes place at least one account is debited and one account is credited.

HOW MANY FUNDS SHOULD A GOVERNMENT HAVE?

There is no set number of funds that a government should have. The number depends on the complexity and size of a government. A practical accounting rule states that a government should use the smallest number of funds possible that will allow the government to meet legal and sound financial administration requirements. Arkansas statutes require a minimum of two funds and bank accounts: General Fund and Street Fund (see A.C.A. § 14-59-101 *et al*).

WHAT ARE FUND TYPES AND CLASSIFICATIONS?

Every general purpose (city, county, state, etc.) government should have a general fund. a general fund means one, and only one general fund. There are three types of funds that a government may use: governmental fund types, proprietary fund types, and fiduciary fund types. The chart below shows all of the fund types and fund classifications. Don't panic! The list is here just to let you know that these things exist. You will probably not have to use all of them.

Fund Type:	Governmental	Proprietary	Fiduciary
Fund Classifications:	General Fund	Enterprise Funds(2)	Pension Funds (3)
	Special Revenue (1) Debt Service Capital Projects Permanent Funds	Internal Service	Investment Trust Private Purpose Trust Agency Funds(4)
Examples:	General Fund Street Fund (1)	Water Fund (2) Sewer Fund (2)	Fire Pension (3) Admin. of Justice (4)

WHICH FUNDS WILL I HAVE TO USE?

Most cities and towns in Arkansas will use two fund types and three fund classifications. The governmental funds are used to account for activities primarily supported by taxes, grants, and similar revenue resources. Under the governmental fund type, there is the general fund, capital projects fund, debt service fund, permanent fund e.g. municipal cemetery fund, and special revenue fund (e.g. street fund). The fiduciary funds are used to account for activities that cannot be used to support the government's own programs. Under the fiduciary fund type, there is the agency fund (e.g. the Administration of Justice Fund) and the pension fund (e.g. the Police Pension and Relief Fund). The proprietary funds are used to account for activities supported from fees and charges (e.g. water fund or sewer fund).

DESCRIBE THE GENERAL FUND

The general fund is used to record all financial activities primarily supported by taxes, grants and similar revenue sources that are not required to be recorded elsewhere. It's the potpourri of funds, the animal shelter for wayward financial transactions. Basically, the general fund is the main operating fund of the government.

WHEN WILL I USE SPECIAL REVENUE FUNDS?

Special revenue funds are used to account for and report the proceeds of specific revenue sources that are restricted (legally or by an outside constraint) or committed (by ordinance) to expenditure for specified purposes other than debt service or capital projects. For instance, a portion of the state turnback revenues are legally restricted for street maintenance. You have to show that the monies you received for that purpose are spent for that purpose. A special revenue fund called street fund will enable you to show legal compliance with this legislation. The city receives a direct deposit from the State Treasurer's Office for turnback. The one labeled "Municipal Highway Aid Funds" will be deposited into the street fund and the other will be deposited into the general fund.

A point to remember is that a restriction for special revenue funds must be from outside agencies like creditors, grantors, contributors, or laws from the State of Arkansas or the federal government, and a commitment must be made by ordinance by the city council.

WHEN WILL I USE AGENCY FUNDS?

Agency Funds are used to account for situations where the government's role is strictly custodial in nature. A good example of an agency fund is the Administration of Justice Fund. State legislation requires that the city clerk deposit the court costs received from the District Court into a fund entitled "Administration of Justice Fund." Basically, the city clerk deposits a check from the court and then writes checks to the state and county and other agencies that are entitled to the revenues. The Administration of Justice Fund is just a pass through fund that is required by state legislation to act as a custodian of the court costs. Usually, agency funds consist of assets and liabilities, with the asset being the checking account balance and the liabilities being payable to other agencies.

WHEN WILL I USE PROPRIETARY FUNDS?

Proprietary funds are used to account for activities where the government charges a fee for a service provided or is used to allocate shared costs. A good example is the water fund. If a government provides the water supply normally there is a fee charged for this service. You would record all revenue and expenses related to this water service in the water fund. Another good example is a motor pool, called an internal service fund, where all revenue and expenses related to the upkeep of all city vehicles is accounted for in this fund.

Cash And Bank Accounts

Cash management internal controls represent an application of common sense and prudent conduct to the use and proper safeguarding of government assets. Cash is the most liquid asset a municipality has, which means it more easily stolen. It is important that safeguards are in place to protect your cash on hand. This requires that cash be locked in a safe at all times. Cash receipts should always be issued when receiving cash from patrons to establish a record of where the funds originated. The cash on hand should not be utilized to cash personal checks of employees or patrons. It is important for deposits to remain intact, which means money received for deposit should not be utilized to make change or reimburse employees for city expenditures, etc. Cash duties, such as receipting, disbursing, cashiering, reconciling and, collecting should be segregated as much as possible coupled with accountability and oversight from management. Cash should be counted daily and balanced with receipts before deposit. *See* Appendix A for Cash Receipt and Disbursements Journal Template.

PETTY CASH

Municipalities are permitted to have petty cash funds as long as the establishment of fund is approved by the city council. When establishing this fund a check from the general fund should be made payable to "petty cash." This fund can be utilized for the handling of small expenditures, such as, postage, light bulbs, delivery fees, etc. A paid out slip should be prepared for each expenditure from this fund and signed by the person receiving the money. When replenishing this fund the check should be made payable to "petty cash". The amount to replenish this fund should be the total of all of the paid out slips. This fund should not be used to cash employee's personal checks, buy lunch for employees or make personal purchases.

BANK RECONCILIATIONS

All municipalities should reconcile all bank accounts on a monthly basis. This requires that all cash receipts and cash disbursements be balanced to the amount on deposit at the banks. See A.C.A. § 14-59-108 for the form that should be used when reconciling bank statements.

Chart Of Accounts

The chart of accounts is a listing of all of the accounts used in keeping your books. It should be a comprehensive listing of all the accounts you will need organized by type, e.g. asset, liability, fund balance, revenue, and expense. These accounts will be the basis for most of your financial records and reports including the general ledger and financial statements.

The sample chart of accounts assumes that your books are kept on the cash basis meaning that you record revenues when cash is received and expenditures when paid. If you use an accrual or modified accrual basis of accounting you will need to add certain asset and liability accounts such as accounts receivable, prepaid expenses, and accounts payable. The accrual basis means that you recognize revenues when earned instead of when received and expenditures when liabilities are incurred instead of when paid.

Most Arkansas municipalities will use the cash basis. A sample chart of accounts can be used for each fund although some of the funds will not need all of the accounts. *See* Appendix B for Sample Chart of Accounts Template.

City Budgets

Your city's annual operating budget should be the principal policy management tool for governing. It should be the mechanism to:

1. Evaluate city services.
2. Measure and compare needs.
3. Set priorities and balance community public service demands against the tax revenues required to furnish them. Therefore, it is important that governing officials participate in the policies and decisions that go into building your municipal budget.

ARKANSAS LAW AND BUDGETING

Every city and town must have an annual operating budget approved by its governing body (A.C.A. §§ 14-58-201 through 203). Before December 1 of each year, mayors of all cities and incorporated town with a mayor-council form of government must submit to the governing body of those cities a proposed budget. This will enable the council to study the document, make any proposed changes and get the budget adopted before February 1.

The fiscal year of each city and town shall begin January 1 and end at midnight, December 31 of each year (A.C.A. § 14-71-102). It is mandatory for the governing body of the municipality to adopt a budget for the operation of the city on or before February 1 of each year. *See* A.C.A. § 14-58-202.

Deficit spending is prohibited. Cities are not allowed to spend more money than they accrue during a year (Ark. Const. Art. 12 Sec. 4). Exceptions to this rule are made for capital improvement, revenue, and energy efficiency bonds (Ark. Const. Amend. 62, 65 and 89) and for short term (up to five years) financing (Ark. Const. Amend. 78 sec.2).

Under A.C.A. §14-58-203, the governing body of the city, from time to time, may alter or revise the budget to better suit city governmental needs. There are two exceptions: Taxes that are levied for specific purposes may not be diverted for other purposes and creditors may not be prejudiced by the diversion of funds.

The budget may be adopted by an ordinance or resolution of the city council. *See* A.C.A. § 14-58-201. The Arkansas Municipal League recommends using a resolution for ease of adoption and amendment.

All cities and town must have the financial affairs of the city or town audited annually by a certified public accountant or by the Division of the Legislative Audit of the State of Arkansas (A.C.A. § 14-58-101).

Purchasing

It is highly recommended that your city formally draft and adopt a purchasing policy by ordinance. It is recommended that this policy address monetary limits by spending levels. This document needs to address emergency spending of city funds, annual supply contracts, on-line sales, cooperative purchasing agreements, protest procedures, disadvantaged and minority owned business enterprises, change orders on construction contracts, and standards of conduct at a minimum.

The following wording regarding State and Federal Regulations is advised to be in the ordinance as well: "*State or Federal Regulations*. To the extent that state or federal regulations applicable to a particular purchase (e.g., grants projects) are more restrictive than the procedures set forth in this ordinance, the state or federal regulations shall apply."

The state statutes address standards of conduct and conflicts of interest in A.C.A. §§ 14-47-115, 14-47-137 and 14-42-107.

The state statutes address the procurement of several different types of commodities and services. One item specifically addressed is the use of subcontractors on items exceeding $50,000 regarding mechanical, indicative of heating, air conditioning, ventilation, and refrigeration, plumbing, electrical, and roofing. Before entering into contracts on these items please read section A.C.A. § 22-9-204. Note also that an exception is made for projects designed to meet the city's need for utilities (A.C.A. § 22-9-201).

A.C.A. § 19-11-801 et seq. Establishes the policy of the state of Arkansas and the political subdivisions that contracts for certain professional services (including legal, architectural, engineering, construction management, land surveying, auditing/accounting, and consulting) be negotiated on the basis of demonstrated competence and qualifications, at a fair and reasonable price, and prohibits the use of competitive bidding for the procurement of such professional services. The act specifies a procedure whereby the political subdivision (city) receives statements of qualifications once a year or as deemed necessary. At such time thereafter that a specific project may arise, the city shall evaluate the statements of qualifications on file and select a firm.

A.C.A. §§ 14-58-303 and 22-9-101, 203 establishes requirements regarding the timing for advertising.

W-9—Request for Taxpayer Identification Number and Certification - This form is used to get the correct TIN (taxpayer identification number) to report, for example, real estate transactions, transactions with vendors, etc.

1099—Form used to report income of vendors that are not incorporated, whom you have paid over $600 and must be sent out by January 31. Reports must be filed with the IRS with a recap form 1096. (These forms should be ordered in October or November.)

Accounting For Grants

Money may be obtained for your city via grants. It is important for the finance department, finance director/treasurer, and city accountant to be involved in the grant process from the beginning. Agreeing to certain grant stipulations may obligate your city in several financial ways that may not be apparent. It is important to consider the "cost" of adhering to these regulations before you agree to accept the grant. If the grant requires a separate bank account you need to consider the cost of this additional bank account and whether or not this "administrative" cost can be paid for by the grant. Many times this is not the case.

If your city expends more than $500,000 of grant funds in one fiscal year it will need to have an Office of Management and Budget (OMB) Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations (Circular A-133) audit conducted. The state does not conduct 133 audits and this too can be an additional cost to the city that won't be covered by the grant.

Additionally, many grants require monthly, quarterly and/or annual reporting in state or federal databases. These reports will need to be maintained for the auditors and can be difficult and time consuming to complete.

Many grants also allow for sub recipients. If you become a sub recipient make sure you understand your requirements to the primary grant beneficiary. If you are allowed to have sub recipients make sure you outline and have your sub recipients sign your requirements before the grant begins.

All Federal Grants have a CFDA (Catalog of Federal Domestic Assistance) number that you will have to list on your Schedule of Federal Awards if you are audited. Additionally if audited your city will need to do a SF-SAC Data Collection Form for Reporting on Audits of States, Local Governments, and Non-Profit Organizations.

The Clearinghouse maintains a site on the Internet at harvester.census.gov/fac/. For Data Collection Form (SF-SAC) and OMB Circular A-133 submission questions, contact the Federal Audit Clearinghouse by email at govs.fac@census.gov, phone 301-763-1551 or toll free at 800-253-0696, or fax 301-457-1592. For questions regarding previous submissions, contact the Federal Audit Clearinghouse Processing Unit at 888-222-9907. The Form SF-SAC and A-133 submission should be mailed to Federal Audit Clearinghouse, 1201 E. 10th Street, Jeffersonville, IN 47132.

If certain particular grants are obtained through FTA or HUD you will need to have a cost allocation plan formalized and approved by the Cognizant Agency (*see* Glossary of Terms).

Sometimes the Department of Labor's (DOL) Davis-Bacon Act requires all laborers and mechanics employed by contractors or subcontractors working on construction contracts in excess of $2,000 financed by federal assistance funds must be paid wages not less than those established for the locality of the project (prevailing wage rates) by the DOL (40 USC §§ 3141-3144, 3146, and 3147 (formerly 40 USC §§ 276a to 276a-7)). Please also look up the Buy America Act, which may apply to federal funds. If federal funds result in the earning of money (through interest or other avenues) it may trigger program income status and these funds have to either be returned to the federal government or be subject to certain spending guidelines themselves.

Additionally, title to equipment acquired by a non-federal entity with federal awards vests with the non-federal entity. Equipment means tangible nonexpendable property, including exempt property, charged directly to the award having a useful life of more than one year and an acquisition cost of $5000 or more per unit. However, consistent with a non-Federal entity's policy, lower limits may be established.

Matching or cost sharing includes requirements to provide contributions (usually non-Federal) of a specified amount or percentage to match Federal awards. Matching may be in the form of allowable costs incurred or in-kind contributions (including third-party in-kind contributions).

Lastly, most grants have time limits on how long you can take to spend the money and complete any and all required paperwork for closing out the grant. Make sure you have documented and set up reminders for these deadlines.

Be sure to assign separate grant revenue and expense lines to journalize grant-related transactions.

GENERAL PAYROLL AND TAX REPORTING INFORMATION

Payroll Taxes

Payroll involves numerous types of taxes and deductions, all with specific rules and deadlines. Both taxes and deductions can be fully paid by the employee, fully paid by the employer, or both parties pay a part of it.

The most common taxes are:

- Social Security Tax (FICA)
- Federal Withholding
- State Withholding
- Federal Unemployment
- State Unemployment

Social Security Tax (FICA)

This includes Social Security and Medicare Tax. A portion is deducted from the employee and the employer also pays a portion. Currently, Social Security is 12.4% with ½ (6.2%) paid by each. Medicare is 2.9% with ½ (1.45%) paid by each.

Social Security has a wage base limit but Medicare does not; therefore when the employee's gross taxable salary reaches the base limit, no more Social Security tax is deducted. Medicare is calculated on 100% of taxable salary. The wage base limit changes every year so it is recommended this is verified annually.

Payment Due: Payment is made monthly or with each payroll, depending on the size of the annual payroll. The payment method is determined by the IRS and is subject to change. It is recommended this tax is paid within three working days of the payroll date to ensure compliance and to eliminate fees for non-payment or late payments. IRS fees can be very hefty.

Payment Method: It is recommended an account be set up with Electronic Federal Tax Payment System (www.EFTPS.gov/) to make the payment online, or set up payment arrangements by telephone. In most instances, the IRS requires this and this method allows for review of payments made.

Other Required Reporting: Quarterly Reporting to IRS with 941 and 941b (unless monthly remittance). Forms and instructions available at www.irs.gov.

Valuable Source: www.irs.gov

Publication: Circular E and Publication 963 Federal/State Reference Guide

Note: Some employees such as elected officials, firemen, or policemen may not have social security and/or Medicare deducted. Please refer to your specific ordinances for clarification. A "218 Agreement" should be filed with the IRS.

For information, call Ardary Taylor, Social Security Division of Arkansas, Public Employees Retirement System, at 1-800-682-7377.

Federal Withholding

Federal Withholding is only paid by the employee. The amount withheld is the amount remitted to the IRS. This tax is remitted with the Social Security Tax. Please refer to the above instructions.

State Withholding

State withholding is only paid by the employee. The amount withheld is the amount remitted to the State of Arkansas.

Payment Due: Payment is made monthly by the 15th of the next month.

Payment Method: Remittance to Department of Finance Administration (DFA) using Form AR-941M. The state usually sends a packet in January of each year with 12 monthly reports, an annual reconciliation, and address labels. Reports can also be filed online at atap.arkansas.gov. This is the recommended method of filing.

Other Required Reporting: Annual reconciliation should be filed using Form AR 3MAR. Due by February 28 of the year immediately following the tax year you are filing

Valuable Source: www.tinyurl.com/dfa-withholding-forms

Federal Unemployment Tax

Federal Unemployment Tax (FUTA) is not currently required by municipalities. Federal Unemployment Tax supplements state if state runs out of funds for benefits.

State Unemployment Tax

State Unemployment Tax (SUTA) is fully paid by the employer. Every January you will receive notification of the annual rate.

The unemployment insurance tax is computed on the wages paid to each employee on a calendar quarter basis. The current taxable wage base that Arkansas employers are required by law to pay unemployment insurance tax on is twelve thousand dollars ($12,000) per employee, per calendar year.

Payment Due: Payment of state unemployment tax is made quarterly by the end of the month following the end of each calendar quarter. Therefore, state unemployment tax reports are due by January 31 (for the fourth quarter of the previous calendar year), April 30, July 31, and October 31.

Payment Method: Once an employer has established an account with the Department of Workforce Services, reporting forms are provided by mail on a quarterly basis.

Valuable Resource regarding how ADWS charges for benefits: www.tinyurl.com/dws-newsletter. A municipality can elect to pay unemployment tax monthly or pay on a reimbursable option. You may choose the reimbursement payment option within thirty (30) days of the date of your liability as an employer by filing a written notice to the Department of Workforce Services, Employer Accounts Services, P.O. Box 8007, Little Rock, AR 72203. If approved, the election will remain in effect at least two (2) calendar years.

Reference: A.C.A. § 11-10-713

- **Factors That Should Be Considered Before Choosing The Reimbursement Payment Option**

1. This option is generally more advantageous for employers with stable employment; the tax-rated basis is usually more advantageous for employers with high employee turnover.
2. Reimbursement payments will vary depending on the number of former employees who are receiving unemployment benefits; however, with this option it is difficult to estimate costs. In contrast, tax-rated employers can more accurately estimate unemployment costs because their tax rates remain constant for a complete calendar year.
3. Employers who have elected the reimbursement payment option may not be relieved of "charges" (payments) for any reason. This includes cases where former employees are paid benefits after a disqualification for quitting or discharge, or in cases where they are paid benefits after subsequent employment and certain other circumstances. Although tax-rated employers may be relieved of charges for specific individuals, the actual cost of the benefits paid to those individuals is shared by all tax-rated employers. For more information *see* dws.arkansas.gov/Employers/PDF/UI_EMPLOYER_HANDBOOK.pdf on page 11.

Reports and payments can be made online at www.employment.arkansas.gov/Tax21/Home.aspx

Valuable Source: dws.arkansas.gov/Employers/

Note: Most accounting software programs offer updates at the end of the year and the beginning of the year to encompass all tax rate changes. Be on the lookout for these updates and make sure to download them in a timely manner.

Other Payroll Deductions

There are many different types of deductions and expenses that must be remitted. These range from health insurance, child support, garnishments, or savings accounts. It is common that health insurance is paid by both parties. Garnishments and child support would only be paid by the employee. Retirement plans are usually paid by both parties, but long-term employees may not be required to contribute. Deductions should be processed according to the specific rules for that deduction.

For example, health insurance is usually paid monthly through an accounts payable check. Retirement payments are also paid monthly, LOPFI (www.lopfi-prb.com) and APERS (www.apers.org) both require online processing. Child support and garnishments are usually paid every payroll but the specific requirements can be found in the court order.

Related Information

New Hire Reporting: All employers must report their new and rehired employees to the state directory of new hires. Federal law mandates the new hires be reported within 20 days of the date of hire. For information contact the Arkansas New Hire Reporting Center at 800-259-2095 or 501-376-2125.

I-9 Forms: Verification that all new employees are eligible to work in the United States. Each employee must fill one out and provide the necessary documentation within three days of employment.

W-4 Forms: The IRS requires a completed W-4 Withholding Allowance Certificate before any employee is entitled to claim withholding allowances. All new employees and those employees whose withholding status has changed should file a new W-4.

Arkansas State Withholding: This form is used to claim withholdings for state tax.

Applications and Job Postings: Applications should remain on file for one year. Job postings and advertisements should be on file for one year.

Employers must treat medical records as confidential information and must be kept separate and apart from the employee's general personnel file. Access should be limited to individuals with a need to know basis.

All employee files must have an application, W-4 and an I-9 on file.

Withholdings: Child support—Remit money immediately. Bankruptcy—Remit as per direction of the court. Garnishment—Remit as per direction of the court.

Employee Termination: Worker who quits—pay the next regular payday. Worker fired—pay within 7 days.

POSTINGS:

- Federal laws require every covered employer to post specific labor information. If your city has any branch offices or separate locations, each must display a complete set of postings.
- State laws require postings for minimum wage, right to know, unemployment insurance, worker's compensation, and sexual harassment.

W-2: Sent to each employee by January 31st. Reports must be filed with a W-3 by February 28th to the Social Security Administration. (These forms should be ordered in October or November).

1099: Form used to report income of vendors that are not incorporated, whom you have paid over $600 and must be sent out by January 31st. Reports must be filed with the IRS with a recap form 1096. (These forms should be ordered in October or November).

W-9: Request for taxpayer identification number and certification—This form is used to get the correct TIN (taxpayer identification number) to report, for example, real estate transactions, transactions with vendors, etc.

Each municipality or county should have an employee handbook. Each job position should have a job description.

This information is general in nature and does not attempt to give all information that might be needed in each municipality or county. We do not cover anything related to ADA (American's With Disability Act), FMLA (Family Medical Leave Act), Worker's Comp, CDL Drivers (Commercial Driver's License), Military Leave, sick leave, vacations, and holidays, etc. The Arkansas Municipal League has a sample employee handbook available.

Common Payroll Errors To Avoid

The following are common errors noted in municipal audit reports:

1. Failure to file federal and state payroll reports;
2. Federal and state payroll reports or forms improperly filed;
3. Failure to properly report compensation to the IRS and the Arkansas Department of Finance and Administration (DFA);
4. Failure to properly remit payroll taxes and withholdings to the IRS and DFA; and
5. Failure to reconcile amounts on payroll reports and forms filed with IRS and DFA to city records.

Payroll – In House Or Outsource?

One of the most complicated functions in municipal accounting may be the payroll function. Getting employees paid correctly and on time while withholding the appropriate amount of taxes or other authorized deductions and remitting those deducted amounts to the various governmental agencies and others can be challenging.

Usually only one or two employees of the municipality are trained and authorized to perform this task. When these individuals are not available to perform payroll duties, the payroll function can be difficult for the municipality. Some medium to small municipalities have chosen to outsource payroll. Outsourcing payroll can place a large part of the payroll burden on an outside payroll accounting firm, which can reduce the stress on a small municipal accounting staff.

The duties of the treasurer found in the Municipal Accounting Law (A.C.A. §§ 14-59-101 through 118) may be assigned to another employee or contractor if (1) the treasurer requests the reassignment or (2) the treasurer fails to perform those duties (A.C.A. § 14-59-115). Note, however, that the law forbids contracting out the collecting of funds. On the other hand, the law's previous prohibition on *disbursing* funds by a non-employee of the municipality was amended by Act 582 of 2015 (amending A.C.A. § 14-59-115). The law now states that "the governing body of a municipality may assign or contract with a private, qualified person or entity for the duties relating to the disbursing of funds for payroll, bonded debt, or construction projects funded with bond proceeds."

Nevertheless, the law places significant limitations on allowing a non-employee to disburse funds. Act 582 states, "[b]efore the governing body of a municipality assigns or contracts with a person or entity for the disbursing of funds, the governing body of a municipality shall establish by ordinance a method that provides for internal accounting controls and documentation for audit and accounting purposes." The Act further provides, "[t]he municipal treasurer shall approve the disbursement of funds before the private, qualified person or entity disburses the funds." Moreover, "[t]he governing body of a municipality shall ensure that the person or entity is adequately insured and bonded and conforms to best practices and standards in the industry."

FINANCIAL RECORD KEEPING

General Requirements

All accounting records should be maintained separately for each fund and stored in that fashion by year. The following records should be maintained for every fund of the municipality:

- Bank statements for each month with cancelled or imaged checks included. Imaged items must comply with A.C.A. §§ 19-2-501 - 509 (legibility, copies of front and back of checks, approval by Legislative Audit, etc.)
- Cash receipt books and printers certificates.
- Cash receipt and disbursement journals or electronic receipts listing and electronic check register with monthly and year-to-date totals (if you maintain manual records). Transaction records and a detail general ledger should be printed out and retained for every month, if computer records are maintained.
- Check stubs.
- Detail of certificates of deposits including interest rates and renewal dates.
- Bank reconciliations for each month and deposit slips that indicate the range of receipts on each deposit ticket.
- Computer files should be backed up daily and a copy of all monthly printed reports should be filed.
- Paid invoices should be filed either alphabetically or preferably by month.
- IRS Forms 1099 for interest earned.

For information on records retention requirements, please refer to *Municipal Law in Arkansas: Questions & Answer*, available from the Arkansas Municipal League.

Additional information required for certain funds:

Trust And Agency Funds

Pension Trust Funds

In addition to the records noted above, these funds are required by Arkansas law to maintain other documents. They are as follows:

- Statements of Participation
- Copy of annual report
- Minutes of Board or Council meetings
- Listing of recipients

Agency Funds

Agency funds are defined as funds that are held for safekeeping for others or that belong to others and will ultimately be remitted to other funds/agencies. Examples of these funds that are common to municipalities are: police bond and fine, district court and payroll funds. The additional records that are required to be maintained for these funds are outlined below.

Police bond and fine

- Arrest reports
- Citation log
- Installment payment records
- Monthly settlements
- NSF checks on hand until check made good and redeposited

District court

- Distribution reports
- Court dockets
- Monthly settlements
- Completed citation books
- NSF checks on hand until check made good and deposited

Payroll fund

- Individual payroll records
- Quarterly payroll reports
- W-2s, W-3s, W-4s, 1099s, LOPFI, and APERS records.

Record Retention

Accounting Records

A.C.A. § 14-59-114 in the Municipal Accounting Law and A.C.A. § 14-237-112 in the Municipal Water and Sewer Department Accounting Law should be referred to for guidance on record retention as to the specific records and information that must be maintained and the length of time that they must be held to be in compliance with Arkansas law. Strict guidelines exist for shredding those archives that take up all the space in your records room; do so with caution. If records can be destroyed according to Arkansas law, create a listing of them under the heading "Affidavit to Destroy Records" and follow the procedures outlined in A.C.A. §§ 14-2-201 and 203.

Other Records

In addition to the records enumerated above, the following documents should also be maintained:

- City Council minutes
- Annual financial statements and proofs of publication
- Insurance policies
- Personnel policies
- Budgets
- Ordinances and resolutions and evidence of publication or posting
- Copies of all audit reports
- For first class cities:
  - Mayor's end of the year report
  - Quarterly financial reports
  - Bids and proofs of publications

Common Record Keeping Errors To Avoid

The following are common errors noted in municipal audit reports:

1. Failure to receipt funds received by use of prenumbered receipts or mechanical receipting devices (A.C.A. § 14-59-109).
2. Failure to properly post receipts by fund to a cash receipts journal or electronic receipts listing, which shall be totaled on a monthly and year-to-date basis and indicate receipt number, date, payer, amount, and classification (A.C.A. § 14-59-110).
3. Failure to properly post disbursements to a cash disbursements journal or electronic check register, which shall be totaled on a monthly and year-to-date basis and indicate check number, date, payee, amount, and classification (A.C.A. § 14-59-111).
4. Failure to reconcile bank accounts. The bank reconciliation must be approved by a municipal official or employee, other than the person preparing the reconciliation, as designated by the chief executive officer of the city (A.C.A. § 14-59-108).
5. Failure to maintain adequate supporting documentation for expenditures (A.C.A. § 14-59-105).
6. Failure to deposit state highway aid into the Street Fund (A.C.A. § 14-59-104).
7. Failure of first class cities to follow bid requirements for purchases exceeding $20,000 (A.C.A. § 14-58-303).
8. Failure of the mayor to submit a budget to the Council by December 1 of the preceding year; failure of the Council to adopt a budget by February 1; and expenditures exceeding budgeted amounts (A.C.A. §§ 14-58-201, 202, 203).
9. Failure of municipalities to publish or post an annual financial statement by April 1 of the following year (A.C.A. § 14-59-116).
10. Failure to provide an adequate Disaster Recovery Plan and Password Controls for information systems (*See* "Arkansas Division of Legislative Audit Information Systems Best Practices" at www.arklegaudit.gov).

Additional Requirements Related To Financial Activity

1. The city council is required to review the audit reports and accompanying comments and recommendations at the first regularly scheduled meeting following the receipt of the report. The city council shall take appropriate action relating to each finding and recommendation, and the minutes of the governing body shall document the action taken (A.C.A. § 10-4-418).
2. No council member, official, or employee shall be interested directly or indirectly in the profits of supplying goods or services to the city unless the council has enacted an ordinance specifically authorizing the council member, official or employee to conduct business with the city and prescribing the extent of this authority (A.C.A. § 14-42-107).
3. Municipal disbursements are generally to be made by prenumbered checks (other than petty cash disbursements). Disbursements of municipal funds used for payments to federal or state governmental entities may be made by electronic funds transfer. Disbursements of municipal funds other than payments to federal or state entities may be made after the municipality adopts an ordinance establishing an electronic funds payment system which has been approved by the Legislative Joint Auditing Committee (A.C.A. § 14-59-105).
4. The governing body may not assign duties relating to the collecting of funds to anyone other than a municipal employee (A.C.A. § 14-59-115).
5. Arkansas Constitution, Amendment 78 prohibits a city from incurring debt that has a repayment period exceeding 5 years.

FIXED ASSET RECORD KEEPING

A.C.A. § 14-59-107 requires that municipalities maintain certain records regarding fixed assets belonging to the municipality as follows:

1. The governing body shall adopt a fixed asset policy, at a minimum, setting the dollar amount and useful life necessary to qualify as a fixed asset.
2. All municipalities shall establish by major category and maintain, as a minimum, a listing of all fixed assets owned by the municipality.
3. The listing shall be totaled by category.
4. The categories shall include the major types, such as:
   A. Land;
   B. Buildings;
   C. Motor vehicles, by department;
   D. Equipment, by department; and
   E. Other assets.
5. The listing shall contain as a minimum:
   A. Property item number, if used by the municipality;
   B. Brief description;
   C. Serial number, if available;
   D. Date of acquisition; and
   E. Cost of property.

***See* Appendix C for Fixed Asset Sample Template.**

UNCLAIMED PROPERTY

What to do with all those aging, outstanding checks?

Arkansas unclaimed properties are forgotten, intangible assets that have met dormancy periods as set forth by the State of Arkansas and the holder has lost contact with the owner. Favorable record keeping will make it easier to complete your yearly unclaimed property report that is due October 31 of every year. The most common types of unclaimed property within a municipality are unpaid wages, uncashed checks, refunds, and occasionally utility or service deposits.

There are three basic steps involved in filing your unclaimed property report:

1. Search your financial records for things like uncashed or returned checks, etc.
2. Due diligence letters must be mailed to the owner(s) of unclaimed property between 60 and 120 days of filing your report. The letters must be mailed if you have an owner address that may be accurate or if the item is for $50.00 or more. *See* Appendix D for Due Diligence Sample Template.
3. Any unclaimed property that you are still holding is now ready to be submitted with your unclaimed property report to the Arkansas Auditor of State.

There are different ways to file your report depending on the number of records you have to submit. You may file your report online, submit a NAUPA formatted file on either a diskette or CD-ROM, or you may download a PDF copy of the form, manually complete it and mail it in.

In the case that your municipality is not holding any unclaimed property it is recommended that you file a negative report. Although state law does not require a negative report to be filed, it helps to establish and maintain a record of compliance with the unclaimed property law.

Timeline for Unclaimed Property Review/Holder Due Diligence Recommended by the Office of the Auditor of the State of Arkansas auditor.ar.gov	
June 15	Generate reports with parameters that reflect all accounts that are inactive and could be reportable as unclaimed property
July 1	Prepare and mail due diligence letters to those customers listed as inactive for whom no other active account has been identified.
September 1	Provide a list of customers with whom contact has been lost, to the person preparing the report due November 1.
October 1	Begin preparing the report, verify report, issue check and mail.
November 1	Report and remittance due at Arkansas Auditor's Office, Unclaimed Property Division.

OTHER FINANCE RELATED TOPICS

Bond Issues

In Arkansas, bond issues are generally characterized as either ***tax supported bonds or revenue bonds***. In most cases, a tax supported bond (such as with sales or property taxes) must be approved by voters whereas revenue bonds can be issued without an election. Two exceptions to the requirement of an election for a tax supported bond are: (1) short term (5 year) obligations repayable with general revenues; and (2) tax increment financings (TIFs).

Examples of revenue bonds include bonds that are repaid by user fees such as water and sewer revenues, or facility revenues such as rental or lease income generated by a building or housing project. Under Arkansas law, certain projects that are financed with revenue bonds will actually require an election, which include hotels, medical office buildings and amusement parks. Franchise fees are considered revenues related to the use of public rights of way and therefore may be used to support a revenue bond without an election.

Industrial development bonds are usually issued as revenue bonds that are repaid by payments from the company that uses and acquires the project that is financed. They are often referred to as Act 9 bonds which refers to the original Arkansas law that authorized such financings in the 1950s. Industrial development bonds might be used as part of a locally approved plan to permit an entity to make a payment in lieu of taxes (PILOT) on a new project that will provide economic benefits to a community. The bond financing is structured with a local government as the owner of the property financed until the debt is repaid thereby permitting a negotiated PILOT payment rather than the regular tax levy.

Short-term obligations that are to be repaid with general revenues were authorized by Amendment 78 of the Arkansas Constitution and can be used to finance real or personal property with a useful life of more than one (1) year. They must be repaid within five (5) years and the total amount of short term debt outstanding may not exceed 5% of assessed property valuation in the municipality.

Sales tax bond financing with a dedicated tax has been the most effective and successful project funding method for cities and counties since authorization in the early 1980s by the approval of Amendment 62 of the Arkansas Constitution. Amendment 62 also provides authority to issue bonds secured by property taxes, but it has had limited usage. Property tax increases are generally unpopular and in Arkansas have been the primary financing resource for school districts. Also, the financing potential of a sales tax is generally much greater than what generally is possible with an acceptable property tax millage.

An important feature of Amendment 62 requires that each specific purpose must be a separate ballot question for a specific amount of bonds. Therefore, a bond proposal for multiple purposes such as a police station, fire station, recreation facility, and street improvements would require at least four (4) ballot questions.

Interest rate limits for publicly issued bonds or other debt were eliminated in 2010 by Amendment 89 of the Arkansas Constitution.

Other sources of project funding include the Arkansas Natural Resources Commission that has loan programs to fund water, waste treatment and waste disposal projects. They are the funding source for the loans which generally are structured as revenue or sales tax bonds as described above. The USDA Rural Development Program is also a source of funding for similar projects as well as community facilities and those loans will also be structured as revenue or sales tax bonds.

An annual report of outstanding revenue bonds must be submitted to the State Board of Finance as required by A.C.A. § 19-9-502. While some cities include sales tax bonds in their report, they are not revenue bonds and need not be reported. Letters and related forms are sent annually to city treasurers in August with reports to be returned in September. If you have any questions regarding this matter, please contact the State Board of Finance's office.

Investments

Investment Authority

Prior to Act 629 of 2011, city investments were generally limited to U.S. Treasury obligations (bills, notes and bonds) for funds not held in bank accounts or the League sponsored Cash Management Trust. Amendments to A.C.A. §§ 19-1-501 through 504 were made by Act 629 to update the general investment authority for cities and counties. Separate but similar provisions for cities and counties were consolidated into a single set of rules for easier reference. The investment authority was also modestly expanded to include US agencies, plus Arkansas governmental obligations that have A or better ratings. With those changes, the investment authority is now similar to the Government Finance Officers' Association (GFOA) model statute and authority in other states. To limit market risk, the maturity of bond investments was limited to 5 years, unless an investment is designated for a specific longer term purpose and a sale before maturity is unlikely. Specific authority and guidelines were also added for establishing a brokerage account that is generally required to purchase, hold and sell today's book entry type investments.

A new A.C.A. § 19-1-505 was added to replace A.C.A. § 14-58-309 (now deleted) that provides broader investment authority for large cities. In order for a city to use this authority it must have total assessed real estate value of $300 million. A provision related to the investment of funds donated to a city was moved from A.C.A. § 19-8-104(c) to A.C.A. § 19-1-504(e).

Bank Deposit Collateralization

Act 619 of 2011 amended A.C.A. § 19-8-107 to add specific requirements for cities and towns related to bank account agreements and the collateralization of bank deposits that exceed FDIC limits, currently $250,000 per depositor. These changes added specific requirements that were already accepted standards necessary to protect public funds. An article appeared in the League's *City & Town* magazine in 2010 that is a good reference tool for the legal requirements that must be observed in order to properly secure your bank deposits. A copy appears as Appendix F to this handbook.

Act 405 of 2013 amended A.C.A. § 19-8-107(c)(2) to require the State Board of Finance to make available to municipal governments sample depository agreements and supplemental agreements required to collateralize deposits. Such forms would be provided through the State Treasurer's office. However, at this time, the State Board of Finance has not provided specific forms that are recommended for use by cities, towns or counties, but it has approved sample documents that appear on the State Treasurer website and also approved a new set of rules and policies in 2012 for state agencies that manage cash funds. A sample Deposit Collateral Agreement and Custodial Services Agreement are provided as part of the new rules and policies.

Below are links to the new State agency rules and sample documents, and the State Treasurer sample documentation.

State agency cash fund policies are found at: tinyurl.com/dfa-policy. Sample documents begin at page 8.

State Treasurer documents are found at: www.artreasury.gov. *See* "Forms" and click on "Custodial Services Agreement" and click on "Security Agreement."

These links provide current information as of the date of this handbook. Please also refer to the League's *Municipal Law in Arkansas: Questions & Answers* publication.

The State agency cash fund policies and documents are the most current and probably the best source for reference information and sample documents. Therefore, we recommend that you use the sample documents included therein as reference for complying with A.C.A. § 19-8-107, particularly when establishing a new bank relationship. However, since many Arkansas banks are familiar with the Treasurer documents, you may have similar documents for your existing bank relationships. The important thing is to make sure your documentation covers the legal requirements necessary to fully protect your bank deposits. Whichever set of sample documents are used as a guide, some editing will be required to change the name of the depositor and related text to your city or town from references to the treasurer or state agency.

It is recommend that you review and discuss this matter at least annually with your banking relationships. When working with a new bank, they will provide proposed security and custodial documents. Make sure they are aware of the requirements of A.C.A. § 19-8-107. Review any proposed or existing documents to make sure they comply. If you have questions about the compliance of your existing documentation, bring this to the attention of your current bank contacts and if necessary, ask that revised documents be prepared.

Contact Cindy Frizzel, Controller for the Arkansas Municipal League if you need assistance.

Internet Security

Internet security is a branch of computer security specifically related to the Internet, often involving browser security but also network security on a more general level as it applies to other applications or operating systems on a whole. Its objective is to establish rules and measures to use against attacks over the Internet. The Internet represents an insecure channel for exchanging information leading to a high risk of intrusion or fraud, such as phishing. Different methods may be used to protect the transfer of data, including encryption. Make sure that your computer system is covered by a reputable product that has comprehensive antivirus protection and easy to use back recovery. Always keep your antivirus protection up-to-date and set your computer to automatically check for updates to the antivirus software. Backup, backup, backup! Your city should have a written Internet policy.

GLOSSARY OF TERMS

Administration of Justice Fund: A specific fund required under Arkansas statutes to record the activities associated with receipts and disbursement of funds received by the city clerk from the district or municipal court.

Agency Fund: One of four types of fiduciary funds. Agency funds are used to report resources held by the reporting government in a purely custodial capacity (assets equal liabilities). Agency funds typically involve only the receipt, temporary investment, and remittance of fiduciary resources to individuals, private organizations, or other governments.

Capital Projects Fund: A fund type used to account for financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including the acquisition or construction of capital facilities and other capital assets (other than those financed by proprietary funds and trust funds).

Credit: An accounting term used to describe an increase in liabilities, fund equity or fund balance, and revenues. A credit will also decrease an asset or expenditure account. A credit is denoted by a minus sign or brackets.

Debit: An accounting term used to describe an increase in an asset or expenditure account. A debit will also decrease a liability account, fund equity or fund balance account, or a revenue account. A debit is denoted by a plus sign or without brackets.

Debt Service Fund: A governmental fund type used to account for financial resources that are restricted, committed, or assigned to expenditure for principal and interest.

Enterprise Fund: A proprietary fund type used to report an activity for which a fee is charged to external users for goods or services.

Fiduciary Fund Type: Funds used to report assets held in a trustee or agency capacity for others and which therefore cannot be used to support the government's own programs. The fiduciary fund category includes pension (and other employee benefit) trust funds, investment trust funds, private-purpose trust funds, and agency funds.

Fund: A fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, that are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.

Fund Classification: One of three broad categories (governmental, proprietary, and fiduciary) used to classify fund types.

Fund Type: One of 11 classifications into which all individual funds can be categorized. Governmental fund types include the general fund, special revenue funds, debt service funds, capital projects funds, and permanent funds. Proprietary fund types include enterprise funds and internal service funds. Fiduciary fund types include pension (and other employee benefit) trust funds, investment trust funds, private-purpose trust funds, and agency funds.

General Fund: The general fund is used to account for all financial resources except those required to be accounted for in another fund. The general fund is one of five governmental fund types and typically serves as the chief operating fund of a government.

Governmental Fund Type: Funds generally used to account for tax-supported activities. There are five different types of governmental funds: the general fund, special revenue funds, debt service funds, capital projects funds, and permanent funds.

Imprest Fund: A type of fund where cash is set aside for a specific purpose, such as payroll or petty cash, and only those specific transactions are processed in that fund.

Internal Service Fund: A proprietary fund type that may be used to report any activity that provides good or services to other funds, departments, or agencies of the primary government and its component units, or to other governments on a cost-reimbursement basis.

Investment Trust Fund: A fiduciary fund type used to report governmental external investment pools in separately issued reports and the external portion of these same pools when reported by the sponsoring government.

LOPFI Assistance Fund: A fund used to accumulate the portion of funds received from the State Insurance Commission to assist the government in providing local match for pensioners in the Arkansas Local Police and Fire Retirement System.

Pension Fund: A fiduciary fund type used to report resources that are required to·be held in trust for the members and beneficiaries of defined pension benefit plans, defined contribution plans, other post-employment benefit plans, or other employee benefit plans.

Permanent Fund: A fiduciary fund type used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government's programs: that is, for the benefit of the government or its citizens.

Private Purpose Trust Fund: A fiduciary trust fund type used to report all trust arrangements, other than those properly reported in pension trust funds or investment trust funds, under which principal and income benefit individuals, private organizations, or other governments.

Proprietary Fund Type: Funds that focus on the determination of operating income, changes in net assets (or cost recovery), financial position and cash flows. There are two different types of proprietary funds: enterprise funds and internal service funds.

Regulatory Basis of Accounting: A.C.A. § 14-58-101 allows municipalities to prepare financial statements on the regulatory basis of accounting as follows:

1. Financial statements of municipalities shall be presented on a fund basis with, as a minimum:
   A. The general fund and street fund presented separately;
   B. All other funds included presented in the aggregate.
2. The financial statements shall consist of the following:
   A. A balance sheet;
   B. A statement of revenues, expenditures, and changes in fund balances;
   C. A comparison of the final adopted budget to the actual expenditures for the general fund and street fund; and
   D. Notes to the financial statements.
3. The report shall include as supplemental information a schedule of general fixed assets, including land, buildings, and equipment.

Special Revenue Fund: A governmental fund type used to account for the proceeds of specific revenue sources that are restricted (legally or by an outside constraint) or committed (by ordinance) to expenditure for specified purposes other than debt service or capital projects.

State Turnback: Monthly the State Treasurer is required to remit certain revenues to cities in Arkansas based on relative population in two distributions: one for general government purposes and one for street maintenance purposes. These monies are referred to as State Turnback.

RESOURCE LIST

Publications:

Arkansas Code Annotated: online www.lexisnexis.com/hottopics/arcode/Default.asp

Arkansas Employers Unemployment Handbook: www.dws.arkansas.gov/wp-content/uploads/2016/05/Employer-Handbook-20151007.pdf

- Audit Reports
- Banks approved for check imaging
- Best Practices

GASB Implementation Guide for Arkansas Governments: www.arml.org/services/publications

Governmental Accounting, Auditing, and Financial Reporting, by Stephen Gautier, copyright 2001. Available from the Government Finance Officers Association, 180 North Michigan Ave., Suite 800, Chicago, IL 60601. www.gfoa.org

Handbook for Arkansas Municipal Officials, current edition (*see* specifically Chapter 59, "Municipal Accounting Law"): www.arml.org/services/publications

Internal Revenue Service: www.irs.gov/

- Circular E of the Internal Revenue Service
- Publication 963 Federal/State Reference Guide
- W-4 Forms
- W-9 Forms

Organizations:

- American Institute of CPAs: www.aicpa.org
- Arkansas City Clerk, Recorders, Treasurers Association: www.accrta.org
- Arkansas Department of Finance & Administration: www.dfa.arkansas.gov
  - ⁎ State Withholding (Payroll Tax)
  - ⁎ Sales Tax
- Arkansas Department of Workforce Services: www.dws.arkansas.gov
  - ⁎ Unemployment
  - ⁎ New Hire Reporting
- Arkansas Government Finance Officers Association: www.arkansasgfoa.org
- Arkansas Municipal League: www.arml.org
- Division of Legislative Audit: www.arklegaudit.gov
- Government Accounting Standards Board (GASB): www.gasb.org
  - ⁎ Financial Reporting

Additional Resources:

- Government Finance Officers Association: www.gfoa.org
- Arkansas State Treasurer: www.artreasury.gov
- Arkansas Assessment Coordination Department: www.arkansas.gov/acd
- Arkansas Public Employees Retirement System: www.apers.org
- LOPFI/PRB: www.lopfi-prb.com

Suspected fraud and/or misuse of public funds - REPORT IT!!!

Organizations:

- Local Prosecuting Attorney
- Division of Legislative Audit

A SAMPLE MUNICIPAL CALENDAR OF EVENTS

Timing is **everything** in accounting. The best method for accurate and timely reporting is to plan wisely; give yourself enough room to compile, calculate, double check, and submit information to state and federal agencies.

JANUARY (QUARTER 1)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (December)

10th - Pay LOPFI and Report (December)

15th - Pay State Income Taxes (December)

20th - Pay Sales Tax on Water Sold (December)

31st W-2's (January - December Previous Calendar Year)

31st 1099's (January - December Previous Calendar Year)

31st - Fourth Quarter 941 Due (October - December Previous Calendar Year Employer Federal Tax)

31st - Fourth Quarter ADWS Due (October - December Previous Calendar Year State Unemployment)

FEBRUARY (QUARTER 1)

1st - Budget must be passed by council.

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (January)

10th - Pay LOPFI and Report (January)

15th - Pay State Income Taxes (January)

20th - Pay Sales Tax on Water Sold (January)

28th - Amend and Close Previous Calendar Year Budget

MARCH (QUARTER 1/END OF QUARTER 1)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (February)

10th - Pay LOPFI and Report (February)

15th - Pay State Income Taxes (February)

20th - Pay Sales Tax on Water Sold (February)

31st - Firemen Pension (Old Plan) Annual Report Due

31st - End of 1st Quarter

APRIL (QUARTER 2)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

1st - Publish Annual Financial Statement before February 1 (Prior Fiscal Year January - December)

10th - APERS Report (March)

10th - Pay LOPFI and Report (March)

15th - Pay State Income Taxes (March)

20th - Pay Sales Tax on Water Sold (March)

30th - First Quarter 941 Due (January - March Employer Federal Tax)

30th - First Quarter ADWS Due (January - March State Unemployment)

MAY (QUARTER 2)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (April)

10th - Pay LOPFI and Report (April)

15th - Pay State Income Taxes (April)

20th - Pay Sales Tax on Water Sold (April)

JUNE (QUARTER 2/END OF QUARTER 2)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (May)

15th - Pay State Income Taxes (May)

20th - Pay Sales Tax on Water Sold (May)

30th - End of APERS fiscal year (July - June)

30th - End of 2nd Quarter

30th - A133 Audit Due (6) months following close of previous fiscal calendar year

JULY (QUARTER 3)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

1st - Beginning of APERS fiscal year (Employer contribution rates usually increase July 1)

10th - APERS Report (June)

10th - Pay LOPFI and Report (June)

15th - Pay State Income Taxes (June)

20th - Pay Sales Tax on Water Sold (June)

31st - Second Quarter 941 Due (April - June Employer Federal Tax)

31st - Second Quarter ADWS Due (April - June State Unemployment)

AUGUST (QUARTER 3)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (July)

10th - Pay LOPFI and Report (July)

15th - Pay State Income Taxes (July)

20th - Pay Sales Tax on Water Sold (July)

SEPTEMBER (QUARTER 3/END OF QUARTER 3)

Submit payroll liabilities after each payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (August)

10th - Pay LOPFI and Report (August)

15th - Pay State Income Taxes (August)

20th - Pay Sales Tax on Water Sold (August)

30th - End of 3rd Quarter

OCTOBER (QUARTER 4)

Submit payroll liabilities after every payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (September)

10th - Pay LOPFI and Report (September)

15th - Pay State Income Taxes (September)

20th - Pay Sales Tax on Water Sold (September)

31st - Unclaimed Property Report (The Great Arkansas Treasure Hunt - Aging Checks 1+ Year Old)

31st - Third Quarter 941 Due (July - September Employer Federal Tax)

31st - Third Quarter ADWS Due (July - September State Unemployment)

NOVEMBER (QUARTER 4)

Submit payroll liabilities after every payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

10th - APERS Report (October)

10th - Pay LOPFI and Report (October)

15th - Pay State Income Taxes (October)

20th - Pay Sales Tax on Water Sold (October)

DECEMBER (QUARTER 4/END OF QUARTER 4)

Submit payroll liabilities after every payroll (Bi-weekly vs. weekly vs. dollar amount, etc. and APERS)

1st - Submit Draft Budget to Council by end of December

10th - APERS Report (November)

10th - Pay LOPFI and Report (November)

15th - Pay State Income Taxes (November)

20th - Pay Sales Tax on Water Sold (November)

31st - End of Fourth Quarter

Appendix A Sample Cash Receipts and Disbursements Journals

CITY/TOWN OF SAMPLE, ARKANSAS
GENERAL FUND
CASH RECEIPTS JOURNAL
FISCAL YEAR ENDING 12/31/2013

Date	Receipt Number	Received from	Total	State Aid	Federal Aid	Property	Sales Taxes	Franchisee Taxes	Fines, Forfei-tures and Costs	Local Permits and Fees	Other
1/5/13	1001	State of Arkansas	3,500	3,500							
1/6/13	1002	County	2,432			2,432					
1/7/13	1003	District Court	1,437						1,437		
1/8/13	1004	State of Arkansas	3,428				3,428				
1/9/13	1005	Entergy	486					486			
1/9/13	1006	John Doe	75							75	
1/17/13	1007	US Dept of Justice	10,000		10,000						
1/18/13	1008	Centerpoint/Arkla	376					376			
1/18/13	1009	Jan Doe	15								15
1/18/13	1010	District Court	1,567						1,567		
		Monthly Totals	**23,316**	**3,500**	**10,000**	**2,432**	**3,428**	**862**	**3,004**	**75**	**15**
		Year-to-date Totals	**23,316**	**3,500**	**10,000**	**2,432**	**3,428**	**862**	**3,004**	**75**	**15**

CITY/TOWN OF SAMPLE, ARKANSAS
GENERAL FUND
CASH DISBURSEMENTS JOURNAL
FISCAL YEAR ENDING 12/31/2013

				Mayor's Office					Police Department		
Date	**Check Number**	**Payee**	**Total**	**Per-sonal Ser-vices**	**Supplies**	**Other Services & Charges**	**Per-sonal Ser-vices**	**Supplies**	**Other Services & Charges**	**Capital Outlay**	**Debt Service**
1/2/13	2001	AT&T	381			257			124		
1/3/13	2002	Regions Bank	651								651
1/4/13	2003	Bill's Police Supply	125					125			
1/8/13	2004	Smith Chevrolet	25,433							25,433	
1/9/13	2005	Payroll Account	3,736	1,368			2,369				
1/10/13	2006	Farmer's & Merchants Bank	324								324
1/17/13	2007	Entergy	221			101			121		
1/18/13	2008	Wal-Mart	26		26						
1/19/13	2009	Payroll Account	3,860	1,368			2,493				
1/30/13	2010	Centerpoint/Arkla	438			153			284		
		Monthly Totals	**35,197**	**2,735**	**26**	**511**	**4,861**	**125**	**529**	**25,433**	**975**
		Year-to-date Totals	**35,197**	**2,735**	**26**	**511**	**4,861**	**125**	**529**	**25,433**	**975**

Note: A.C.**A.** § 14-59-111 states that classifications of expenditures shall include the major type of expenditures (personal services, supplies, etc.) By department (mayor, clerk, treasurer, police, fire, etc.). Only 2 departments are shown above for illustrative purposes.

Appendix B Sample Chart of Accounts

EXAMPLE MUNICIPAL FUND CODES	
General	1000
Street	2000
Special Revenue Funds	
Local Police And Fire Retirement	3001
Fire Equipment And Training - Act 833	3002
Capital Projects Funds	
City Hall Construction	4001
Debt Service Funds	
Sales Tax Bond	5001
Agency Funds	
Police Bond And Fine	6001
District Court	6002
Enterprise Funds	
Landfill	7001
Trust Funds	
Nonuniform	8001
Police	8002
Fire	8003

MUNICIPAL DEPARTMENT CLASSIFICATIONS	
General Government	
Mayor's office	0100
City Clerk's office	0101
City Treasurer's office	0102
City Council	0103
City Attorney	0104
Planning Department	0105
Code Enforcement	0106
Computer Services	0107
Economic Development	0108
Advertising and Promotion	0109
Tourism	0110
Highways and Streets	
Street Department	0200
Law Enforcement	
Police Department	0301
District/City Court	0302
Animal Control	0303
Dispatch	0304
Police Pension	0305
Judge and Clerk Retirement	0306
Drug Control	0307
Public Safety	
Fire Department	0401
911	0402
Fire Pension	0403
Sanitation	
Sanitation Department	0501
Landfill	0502
Recycling	0503
Health	
Ambulance service	0601
Mosquito control	0602
Recreation and Culture	
Parks and recreation	0701
Library	0702
Social Services	
Senior Citizen's Center	0801
Cemetery	0802
Airport	
Municipal Airport	0901

EXAMPLE CHART OF ACCOUNTS	
Assets	1000
Cash	1010
Investments	1020
Accounts Receivable	1030
Interfund Receivables	1040
Liabilities	2000
Accounts Payable	2010
Interfund Payable	2020
Settlements Pending	2030
Fund Balance	3000
Nonspendable	3100
Restricted	3200
Committed	3300
Assigned	3400
Unassigned	3500
Revenues	4000
State Aid	4100
Federal Aid	4200
Property Taxes	4300
Franchise Fees	4400
Sales Taxes	4500
Fines, Forfeitures, And Costs	4600
Interest	4700
Local Permits And Fees	4800
Sanitation Fees	4900
Gas And Oil Company Reimbursements	4910
Other	4950

EXPENDITURES	
Personal services	5000
Supplies	6000
Other services and charges	7000
Capital outlay	8000
Debt service	9000

OTHER FINANCING SOURCES (USES)	0000
Transfers in	0100
Contribution from water department	0110
Transfers out	0150
Contribution to water department	0200

EXAMPLE MUNICIPAL EXPENDITURE CODES CHART

PERSONAL SERVICES: Amounts paid to both permanent and temporary government employees, including personnel substituting for those in permanent positions. This category includes gross salary for personal services rendered while on the payroll of the government and amounts paid by the government on behalf of employees; these amounts are not included in the gross salary, but are in addition to that amount. Such payments are fringe benefits payments and, although not paid directly to employees, are a part of the cost of personal services.

5001	Salaries, Full-Time
5002	Salaries, Part-Time
5003	Extra Help
5004	Contract Labor
5005	Overtime and Other Premium Compensation
5006	Social Security Matching
5007	Retirement Matching
5008	Noncontributory Retirement
5009	Health Insurance Matching
5010	Workmen's Compensation
5011	Unemployment Compensation
5012	Other Fringe Benefits
5013	Car Allowance
5014	Cobraserv
5015	Uniform Allowance
5016	Life Insurance

SUPPLIES: Amounts paid for items that are consumed or deteriorated through use or that lose their identity through fabrication or incorporation into different or more complex units or substances.

SUPPLIES

6001	General Supplies
6002	Small Equipment
6003	Janitorial Supplies
6004	Clothing and Uniforms
6005	Fuels, Oils, and Lubricants
6006	Tires and Tubes

REPAIR AND MAINTENANCE SUPPLIES

6020	Building Materials and Supplies
6021	Paints and Metals
6022	Plumbing and Electrical
6023	Parts and Repairs
6024	Maintenance and Service Contracts
6025	Asphalt
6026	Culvert and Pipe
6027	Gravel, Dirt, and Sand

6028	Lumber and Pilings
6029	Small Tools
6030	Concrete
6031	Bridges and Steel

OTHER SERVICES AND CHARGES

PROFESSIONAL SERVICES: Services that by their nature can be performed only by persons or firms with specialized skills and knowledge. Although a product may or may not result from the transaction, the primary reason for the purchase is the service provided.

7001	Accounting and Auditing
7002	Management Consulting
7003	Computer Services
7004	Engineering and Architectural
7005	Special Legal
7006	Other Professional Services

COMMUNICATIONS

7020	Telephone and Fax - Landline
7021	Postage
7022	Cell Phones and Pagers
7023	Internet Connection

TRANSPORTATION

7030	Travel
7031	Common Carrier

ADVERTISING AND PUBLICATIONS

7040	Advertising and Publications

INSURANCE (OTHER THAN PERSONAL SERVICES)

7050	Official and Employee Bond
7051	Boilers and Machinery Insurance
7052	Fire and Extended Coverage
7053	Fleet Liability
7054	Other Sundry Insurance

UTILITIES

7060	Utilities - Electricity
7061	Utilities - Gas
7062	Utilities - Water
7063	Utilities - Water Disposal

RENTALS AND LEASES (NOT LEASE PURCHASE)

7070	Rent - Land and Buildings
7071	Rent - Machinery and Equipment
7072	Lease - Land and Buildings
7073	Lease - Machinery and Equipment

PUBLIC RECORDS

7080	Public Records

MISCELLANEOUS

7090	Dues and Memberships
7091	Miscellaneous Law Enforcement
7092	Meals and Lodging
7093	Vending Machines - Food/Drinks
7094	Other Miscellaneous
7095	Training and Education
7096	Computer Software, Support, and Maintenance Agreement

CAPITAL OUTLAY

8001	Land
8002	Buildings
8003	Improvements Other Than Buildings
8004	Machinery and Equipment (Other Than Vehicles)
8005	Vehicles
8006	Construction in Progress

DEBT SERVICE

9001	Bond Principal
9002	Bond Interest
9003	Note Principal
9004	Note Interest
9005	Lease Purchase Principal
9006	Lease Purchase Interest

Appendix C Sample Fixed Asset Listing

CITY/TOWN OF SAMPLE, ARKANSAS FIXED ASSET LISTING FISCAL YEAR ENDING 12/31/2013				
Description	**Acquisition Date**	**Property No.**	**Serial No.**	**Amount**
Land				
Lot 5, Section C	7/2/71			$ 5,000
Buildings				
City Hall	7/2/71			$ 54,257
Fire Station	10/24/81			$ 26,482
TOTAL BUILDINGS				**$ 80,739**
Motor Vehicles				
General				
1991 Chevy Truck	7/6/05		BR549	$ 10,502
Fire				
1984 Pumper	12/14/07		V187K816G987	$ 35,864
1972 Fire Truck	8/18/97		V1357M751R321	$ 9,762
Subtotal				**$ 45,626**
TOTAL MOTOR VEHICLES				**$ 56,128**
Equipment				
General				
Dell Computer	9/14/08		CW12589KL654	$ 2,500
Power Washer	12/19/10		WKRP325	$ 2,764
Subtotal				$ 5,264
Fire				
Jaws of Life	4/1/12		682RDL937	$ 2,534
TOTAL EQUIPMENT				**$ 7,798**
TOTAL FIXED ASSETS				**$ 149,665**

Note: A list of deletions and additions must be maintained in order to reconcile beginning balance to ending balance. Beginning balance of the current year (or ending balance of the previous year) plus additions less deletions should equal ending balance of the current year.

Appendix D Sample Due Diligence Letter on Outstanding Checks

Letterhead

Date

Name

Address

City, State, Zip

Re:

Our records indicate that the following check issued to you is still outstanding:

Check #   Date Issued   Amount

Please indicate the disposition of the check on the bottom of this form and return it to us within 10 days.

Disposition of check:

- ❑ I cashed the above-referenced check. Provide date cashed, if known: ___/___/___
- ❑ I am holding the above-referenced check for the following reason:
- ❑ I received the above-referenced check, but it has been lost or destroyed. Please issue a replacement check.
- ❑ I did not receive the above-referenced check. Please issue a replacement check.
- ❑ Other, explain:

Please sign here: ___________________________

Address: ____

Appendix E Sample Annual Revenue Bond Report

STATE BOARD OF FINANCE

REVENUE BOND REPORT

June 30, 2012

REPORTING AGENCY: City of ____

PURPOSE OF ISSUANCE: (Please attach separate form for each issue.)

AMOUNT OF ISSUE $______________ AMOUNT OUTSTANDING $_____________________

PERCENTAGE INTEREST RATE PAYABLE %

PLEDGED REVENUES FOR BONDS

SOURCE	TYPE	AMOUNT
(project, governmental unit, special fund, etc.)	(fees, charges, etc.)	

PLEASE ATTACH REPAYMENT SCHEDULE.

****

THERE WERE NO REVENUE BONDS OUTSTANDING AT JUNE 30, 2012 FOR THIS AGENCY.

Completed by:

NAME____

TITLE____

SECURING BANK DEPOSITS

Reprinted from *City & Town*, May 2010

By Jim Buttry (1940-2013)

Jim Buttry was a partner in the Friday, Eldredge & Clark, LLP law firm until he passed away in 2013. He was a longtime counsel and friend to municipal governments in Arkansas. He practiced municipal bond law from 1967 until his retirement. A graduate of the University of Arkansas (LL.B., 1963) and Georgetown University (LL.M., 1966), he also was a member of the National Association of Bond Lawyers and had been recognized in Best Lawyers in America *and in* Chambers USA 2010 *as among "Leaders in Their Field."*

I last put together an article for *City and Town* on the securing of public deposits in 1993. I thought that I was finished with the matter. Indeed, I announced in the article that it was my "swan song" on the subject. With some trepidation, I have been drawn back into the matter, chiefly because of changes in state law and the request of my friend Paul Young, the League's finance director, who collaborated on and contributed greatly to this article. Also, the General Assembly made significant changes in the Uniform Commercial Code in 2001. I must acknowledge my reliance on Hawkland & Rogers UCC Series (Rev Art 8).

I repeat the disclaimers that I issued in 1993 and add one. Here are the disclaimers:

- The scope of this article is limited. It deals with the "perfection" and "control" of security interests in collateral pledged to secure public deposits. I have, for example, not attempted to deal with the details involved in the liquidation of collateral in the event of a bank failure.
- I have not attempted to deal with whether a particular deposit is of public funds, eligible for collateralization under federal and state law. Nonprofit entities associated with or supporting governmental purposes would be examples of entities that might not qualify.
- Any change in existing law or regulations can affect the conclusions or opinions expressed in this article.
- We are required by IRS Circular 230 to inform all readers of this article that any statements contained in it are not intended or written to be used, and cannot be used, by anyone for the purpose of avoiding any penalties that may be imposed under federal law.

Portions of this article repeat portions of the 1993 article. (I am confident that there is no risk of anyone's remembering the latter.)

I have used the term "municipality" herein to refer to all public bodies. This article is written as addressed to municipalities and, accordingly, the term "you" refers to them. References to the "UCC" are to the Arkansas Uniform Commercial Code. I have referred to "indorse" and "indorsement," as that is how it is spelled in the UCC.

Bond lawyers have been accused of having the mind of a "file cabinet." Being a bond lawyer, I am conservative in the opinions expressed here. Your lawyer may disagree with some of them (and in a lawsuit might be upheld). Bond lawyers look upon an "opinion" as a "conviction." This, basically, amounts to a reasonable doubt standard.

Some background

Securities were used to secure (or "collateralize") loans before there were any uniform or clear statutory rules covering such transactions. Banks lend on the basis of such collateral, of course, every day. In the typical deposit transaction (including a certificate of deposit) the parties are reversed. The bank is borrowing from the depositor, for our purposes here, the municipality. (But the same state laws are applied.) Because more than one person can claim to own a security, or an interest in it, the challenge has always been to determine which claimant has a prior right or interest. In the event of a bank failure, you want your collateral to protect your funds against the claims of other bank creditors, primarily the claims of the FDIC.

Under Arkansas law, a municipality's deposits in excess of FDIC insurance coverage ($250,000 until Dec. 31, 2013, when the amount will revert to $100,000) should be secured by a "perfected" pledge of certain eligible securities. This is set forth in Arkansas Code of 1987 Annotated at § 19-8-107 and § 19-8-203. It is not clear whether the requirement for an "eligible security" as collateral refers to both securities and to "security entitlements," which I will discuss below. This suggests that some consideration might be given to the amendment of our state statutes recognizing and confirming that eligible "securities" may be in the form of security entitlements.

Since 1993 the list of securities which are "eligible securities" for the securing of public funds has grown from a very short one (direct obligations of the United States or obligations guaranteed by the United States) to a very long one as found in A.C.A. § 19-8-203, which by reference includes § 23-47-401. Some of the items to be used by Arkansas banks as deposit collateral are:

- Direct obligations of the United States;
- Obligations of agencies and instrumentalities created by act of the Congress and authorized thereby to issue securities or evidences of indebtedness, regardless of guarantee of repayment by the United States (such as government sponsored entities like Fannie Mae, Freddie Mac or the Federal Home Loan Banks);
- Obligations the principal and interest of which are fully guaranteed by the United States or an agency or an instrumentality created by an act of the Congress and authorized thereby to issue such guarantee;
- General obligations of the states of the United States and of the political subdivisions, municipalities, commonwealths, territories or insular possessions thereof (provided the issuer has not had a default in the past 10 years);
- Surety bonds issued by insurance companies licensed under the laws of the state of Arkansas that meet the statutory rating requirements or are listed on the then-current United States Department of the Treasury Listing of Approved Sureties;
- Irrevocable standby letters of credit issued by Federal Home Loan Banks; or
- Revenue bond issues of any state of the United States or any municipality or any political subdivision thereof.

Some of the above, such as state or municipal revenue bonds, will only be suitable as collateral if they have very strong credit quality and short to intermediate maturity. (The statute which authorizes state bank investments in them limits to 20 percent the portion of a bank's capital base that may be so invested.)

In addition to the changes in eligible securities, the General Assembly enacted major amendments to the UCC, in 2001. These include, in particular, amendments to those provisions dealing with the creation and perfection of security interests.

In order to be protected, a depositing municipality must comply both with (1) the federal Financial Institutions Reform, Recovery and Enforcement Act of 1989 (so called "FIRREA") and (2) the UCC.

A look at FIRREA

Congress enacted FIRREA in response to the savings and loan turmoil of the 1980s. Among other things, it included additional requirements for the validity and enforceability of security interests against the FDIC in a takeover.

The requirements of FIRREA, which are set forth in 12 United States Code § 1823(e), are that there be an agreement, which agreement must be in writing,

(a) executed contemporaneously with the acquisition of the collateral,

(b) maintained, continuously from the time of execution, as an official record of the bank, and

(c) approved

  (i) by the board of directors or loan committee of the bank,

  (ii) which approval must be shown in the minutes of the board or the committee.

It is instantly obvious that, of the FIRREA requirements, (b) is difficult and (a) would be worse. Happily the FDIC has recognized the difficulties with (a), and has announced that it will not seek to avoid a security interest, otherwise perfected and legally enforceable, solely because the agreement does not meet the "contemporaneous" requirement. The FDIC policy was enacted into law in 1994 but the security agreement must still be adopted in the ordinary course of business, and not in the contemplation of insolvency. If you fail to have a security agreement in place prior to when you have reason to fear insolvency of a bank, it will likely be too late.

Also, to be effective, the security agreement should include a description of the eligible collateral and how specific collateral is to be identified at any point in time, such as by a confirmation from the third party custodian of the collateral. After all, one reason for the agreement requirement is to permit examiners to identify any claims against the assets of the bank.

Now we consider state law

When I began practicing law, nearly all securities were in the form of paper certificates which were held (physically) by the true, or beneficial, owner. In order to pledge a security to secure a debt, the certificates were delivered to the lender and endorsed by the owner. There was rarely any doubt about who owned the security or who had a security interest in it. If the security was in registered form, instructions were given to the registrar. In the event of a default, the securities could be instantly liquidated. But there was a terrible problem. By the 1970s the volume of traded certificates was overwhelming the markets. At one point, the New York Stock Exchange closed on Wednesdays in order to allow market participants to catch up with the paperwork.

The Uniform Commercial Code was rewritten to authorize uncertificated securities. The issuer's registrar made an entry on its books reflecting the identity of the owner and reflecting any security interest granted by the owner. But the markets had gotten ahead of the change in the UCC and had already established a system that utilized certificates. But these certificates were "jumbo" or immobilized and held by a single registered owner, today The Depository Trust Company or DTC. If you buy a security today, other than a U.S. treasury or agency obligation, it is almost certainly registered to the nominee of DTC, and DTC reflects on its books not you as the owner but a "securities intermediary" (typically a broker or bank) which holds the security for you. Therefore, today almost all securities are held in one of two ways:

- Uncertificated—For the most part, only U.S. treasury or agency obligations are held in this way. For them the registrar is a Federal Reserve Bank, and there is a direct relationship between the owner and the issuer. That is, the identity of the owner is reflected on the book maintained by the issuer's registrar. Transfers are made by notification to the registrar.
- Certificated but "indirect"—DTC maintains records which reflect ownership by a "participant" which is a "securities intermediary" and what you own is not a security but is a package of rights and interests against your securities intermediary. This package is called a "security entitlement." This is the "indirect system," and it is now the system for the holding and transfer of almost all municipal bonds and corporate securities.

Now, we get to "perfection," which primarily requires "control" of the pledged collateral. The Government Finance Officers Association recommends the use of a custodian, which is typically a bank and is preferably a separate trust or safekeeping department. In most cases, this will be accomplished by having a custodian hold the bank's pledged collateral in its name on your behalf pursuant to an agreement so that nothing can be done with the collateral unless you approve. Also, the agreement should permit you to sell the collateral if necessary to satisfy your deposits without the consent of the bank or the FDIC. Typically, the custodian will be an independent party that regularly holds your bank's securities or security entitlements for this and other business purposes. In order to establish properly the arrangement and protect your interest, you will need to enter into a three party agreement among you, the custodian and your bank in which the parties will acknowledge these terms and that the collateral is held on your behalf. This is in addition to the security agreement required by FIRREA, discussed above.

In the uncertificated system, a security interest can be perfected in a security by having your custodian reflected as the owner of the securities on the books of the registrar. This amounts to perfection even against a "protected purchaser." (More on that below.)

In the indirect system, your custodian will not own a security or an interest in a security. The custodian will own an interest in an account held by your bank. Your security interest in a security entitlement is perfected when the securities intermediary maintaining the account indicates by book entry that the securities entitlement has been credited to an account in the name of your custodian (and you, the bank and your custodian enter into the agreement described above). Based on this arrangement, the intermediary will comply with orders originated by you and your custodian without the consent of the bank. Bear in mind: A security entitlement is not a claim to a specific identifiable thing; it is a package of rights and interests that a person has against the person's securities intermediary (e.g., broker) and the property held by the intermediary. (Uniform Commercial Code Official Text and Comments, § 8-503.) The UCC makes clear the priority of a protected purchaser of a security over the holder of a security entitlement. A protected purchaser is one that acquires a security for value without the notice of another claim. It is theoretically possible for a protected purchaser to trump the interest of a public depositor's claim to a security entitlement that is maintained by the DTC system. However, that would clearly require a very unusual security transfer to a holder other than DTC. Surprisingly, there is little precedent and guidance in that regard. But logic would suggest that the FDIC, as receiver of the depository bank, should recognize a properly perfected security interest in a security entitlement as a perfected security interest in the underlying securities, as the depository bank has lost control of those securities.

No magazine article can cover every transaction or serve as a substitute for consultation with your counsel. For your reference, the GFOA's Recommended Practice on this topic accompanies this article (*see* pages 18 and 19). It has similar information on the requirements of FIRREA and also includes some recommendations on related matters such as collateral valuation. In fact, officials charged with the responsibility of securing deposits in excess of FDIC coverage should, as appropriate, consult with the municipality's banker, lawyer or accountant (or some or all of them). The list of eligible securities is now long and the requirements of both state and federal law are strict. You want to be secure against an FDIC claim and be able to liquidate your securities without FDIC consent. It would be hard to be too careful. Remember that your League is available to assist.

BEST PRACTICE

Collateralization of Public Deposits (1984, 1987, 1993, 2000, and 2007) (TIM)

Background: The safety of public funds should be the foremost objective in public fund management. Collateralization of public deposits through the pledging of appropriate securities or other instruments (e.g. surety bonds or letters of credit) by depositories is an important safeguard for such deposits. The amount of pledged collateral is determined by a public entity's deposit level. Some states have established programs for the pooling of collateral for deposit of public funds.

Federal law imposes certain limitations on collateral agreements between financial institutions and public entities in order to secure public entity deposits. Under certain circumstances, the Federal Deposit Insurance Corporation (FDIC) may void a perfected security interest and leave the public depositor with only the right to share with other creditors in the pro rata distribution of the assets of a failed institution.

Recommendation: The Government Finance Officers Association (GFOA) recommends the use of pledging requirements as protection for state or local government's deposits. GFOA encourages state and local governments to establish adequate and efficient administrative systems to maintain such pledged collateral, including state or locally administered collateral pledging or collateral pools. To accomplish these goals, GFOA recommends the following:

1. Public entities should implement programs of prudent risk control. Such programs could include a formal depository risk policy, credit analysis, and use of fully secured investments. In the absence of a state program for pooling collateral, public entities should establish and implement collateralization procedures, including procedures to monitor their collateral positions. Monitoring informs a public entity of undercollateralization, which may threaten the safety of an entity's deposits, and overcollateralization, which may increase the cost of banking services.
2. State and local government depositors should take all possible actions to comply with federal requirements in order to ensure that their security interests in collateral pledged to secure deposits are enforceable against the receiver of a failed financial institution. Federal law provides that a depositor's security agreement, which tends to diminish or defeat the interest of the FDIC in an asset acquired by it as receiver of an insured depository, shall not be valid against the FDIC unless the agreement:
   - is in writing;
   - was approved by the board of directors of the depository or its loan committee; and
   - has been, continuously, from the time of its execution, an official record of the depository institution.
3. Public entities should have all pledged collateral held at an independent third-party institution, and evidenced by a written agreement in an effort to satisfy the Uniform Commercial Code (UCC) requirement for control. The UCC states that the depositor does not have a perfected interest in a security unless the depositor controls it. Control means that swaps, sales, and transfers cannot occur without the depositor's written approval.
   - The value of the pledged collateral should be marked to market monthly, or more frequently depending on the volatility of the collateral pledged. If state statute does not dictate a minimum margin level for collateral based on deposit levels (e.g., Georgia and Minnesota statutes require 110 percent), the margin levels should be at least 102 percent, depending on the liquidity and volatility of the collateral pledged. State statutes also govern whether minimum margin levels apply to principal only or to accrued interest as well. Public entities should review applicable state statutes and confirm compliance.

  - Substitutions of collateral should meet the requirements of the collateral agreement, be approved in writing prior to release, and the collateral should not be released until the replacement collateral has been received.

4. The pledge of collateral should comply with the investment policy or state statute, whichever is more restrictive.
5. Public entities that use surety bonds in lieu of collateral should limit the insurers to those of the highest credit quality as determined by a nationally recognized insurance rating agency.
6. The public entity should review the terms and conditions of any letters of credit, including those issued by a federal agency or government sponsored enterprise.

Note: As a result of the court case *North Arkansas Medical Center v. Barrett*, 963 F.2d 780 (8th Cir. 1992), the FDIC issued a policy statement in March 1993 indicating that it would not seek to void a security interest of a federal, state, or local government entity solely because the security agreement did not comply with the contemporaneous execution requirement set forth in Section 13(e) of the Federal Deposit Insurance Act 12

U.S.C.1823(e). The policy statement was officially enacted by Section 317 of the Riegle Community

Development and Regulatory Improvement Act of 1994 (Public Law 103-325).

References

- Sample Security Agreement (long and short forms), GFOA, 2001.
- Sample Custodial Trust Agreement, GFOA, 1995.
- *Investing Public Funds*, Second Edition, Girard Miller with M. Corinne Larson and W. Paul Zorn, GFOA, 1998.
- *An Introduction to Collateralizing Public Deposits for State and Local Governments*, Second Edition, M. Corinne Larson, GFOA, 2006.

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