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Unit D.4: GFS Quality Management and Government Accounting

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ABSTRACTS

SESSION 1	The political context – sovereign debt crisis, economic governance, transparency and trust in fiscal data

Fayezul Choudhury, CEO, International Federation of Accountants (IFAC)

Building trust and financial stability through transparency and accountability

With the effects of the sovereign debt crisis still being felt, reducing economic uncertainty and the fallout of unmanageable debt must be a priority. While the underlying causes of the current economic crises are varied and complex, the lack of reliable financial data on economic conditions was clearly a contributing factor. Governments must improve the quality of financial reporting by public sector entities so that rational decisions can be made, and so that they—and taxpayers, investors, and oversight authorities—have complete and reliable financial information to assess economic performance. It is critical that necessary measures are taken now toward establishing significant change.

Accrual-based accounting provides for the full disclosure of all assets, liabilities, and contingent liabilities. This comprehensive approach is vital for decision-making, resource allocation, monitoring, and accountability, no matter what the stage of economic development of the country. International Public Sector Accounting Standards (IPSASs) are the only globally accepted, high quality, accrual-based financial reporting system for the public sector; they enhance the quality and transparency of public sector financial reporting and help assess the true economic implications of public sector financial management. Many governments, jurisdictions, and international institutions have already adopted IPSASs, while others are working toward their implementation.

In their latest communiqué in February, the G-20 Finance Ministers and Central Bank Governors highlighted the importance of transparent and comparable public sector financial reporting, and called on the International Monetary Fund (IMF) and World Bank to further explore the issue. In addition, in late 2012, the IMF issued a paper, *Fiscal Transparency, Accountability, and Risk*, in which it supported IPSASs and underscored the risks of the current inadequacies in governments' fiscal reporting and accountability. These are important reference points as the European Commission moves toward harmonized public sector accounting standards as a tool to build trust and financial stability.

SESSION 2	Fiscal transparency and public accounting

Richard Hughes, Division Chief, Public Financial Management I, International Monetary Fund (IMF)

Fiscal Transparency in the Wake of the Crisis

The presentation will provide an overview of the lessons from the crisis for fiscal transparency standards, practices, and surveillance and discuss their implications for the proposal to develop a set of common public sector accounting standards for the EU.

Olivier Boutellis-Taft, CEO, Federation of European Accountants (FEE)

The need for fiscal transparency and harmonised public sector accounting standards

What should be a surprise is that we ask ourselves whether we need fiscal transparency and harmonised public sector accounting standards in a European Union where government spending accounts for +/- 50% of GDP, in an EU made up of soon 28 highly interdependent economies, in an EU where Member States have committed to fiscal discipline and in an EU where 17 Member States share the same currency.

The Commission's report makes a very strong and legitimate case for fiscal transparency and harmonised public sector accounting standards. The analysis is comprehensive and well thought through; the arguments are convincing and moreover, it is showing something that is most needed: political courage and leadership. True transparency in public finance can only result from the use of full accrual accounting. Only double entry accrual accounting would provide a comprehensive and reliable view of the financial position and performance of the public sector.

To understand how we can make progress, it is important to identify obstacles and learn from experience in private sector accounting. Unfortunately the recent attempt to simplify and harmonise private sector accounting (4th and 7th Directives) is not encouraging.

What we need is a single set of high-quality accrual accounting standards for all public sector entities in the EU. "EPSAS", as proposed by the Commission, could be an appropriate interim solution. However it will be important to prevent counterproductive political battles and tinkering and avoid unnecessary divergence between EPSAS and IPSAS – and thus between EPSAS and IFRS that represent the most complete and sophisticated reporting frameworks. Standard-setting requires independence and robust governance.

Public sector accounting standards are a means to an end; a means to contribute to enhancing political accountability and securing the sustainability of the European social model. It is a critical public interest issue that we all have a responsibility to advance.

Prof. Dr. Berit Adam, Berlin School of Economics and Law, Comparative International Governmental Accounting Research Network, CIGAR - Network

The need for harmonised, accruals-based European Public Sector Accounting Standards from a German perspective

In German local authorities, the majority of financial officers estimate that the benefits of the reform towards a full accrual based budgeting and accounting system will outweigh the costs in the medium to long term. The main benefits associated with an accrual based budgeting and accounting system are seen to be:

- The possibility to present consolidated financial statements
- Ensuring intergenerational equity because the attention is on revenues and expenses instead of cash inflows and cash outflows
- Improved transparency about the financial position and performance of a public sector entity
- The possibility of benchmarking as comparable information is supplied by public sector entities
- Improved efficiency and effectiveness by measuring performances and outcomes instead of financial input

As in Germany the Ministries of Interior of the States are responsible for regulating the budgeting and accounting system of the local authorities, we failed to achieve a budgeting and accounting system on the local level that is materially comparable. Therefore, from a German academic perspective, the main benefit of using IPSASs as a basis to develop harmonised accounting standards within the EU is without an alternative. To be able to generate comparable and consistent financial information on all levels of government within the EU member states that enables more efficient and effective political and administrative decisions, the following needs to be considered:

- Empirical evidence clearly suggests that the benefits of an accrual based accounting system can only be fully realised if and when the budgeting and accounting system are on the same basis
- The main focus in the public sector is not on the output of the accounting system in terms of financial statements, but on the budget; therefore, when developing accounting standards the impact of the regulations on the budget needs to be taken into account
- The primary goal of implementing harmonised accounting standards in the EU should be to enable politicians to make “better” decisions and to enable the administration to become more efficient and effective; to improve fiscal transparency by implementing accrual based accounting standards is only a necessary requirement to be able to take more efficient and effective decisions

- When developing EPSASs, it is important to have in mind that the benefit of information supplied should in all cases exceed the cost of information collected; this implies that simplifications of some IPSASs regulations are urgently required, e.g. regarding impairment of property, plant and equipment, the measurement of revenues from non-exchange transactions, the extent of the notes to the financial statements. Another approach could be to develop a separate set of EPSASs for SME's or to allow exceptions from full EPSASs for small entities.

Dr Danny S. L. Chow, Lecturer in Accounting at Durham Business School, Durham University, UK, Association of Chartered Certified Accountants (ACCA)

Reflections on the costs and benefits of EPSAS

The presentation will discuss why changing to accruals accounting is important for member states at a time when public trust and confidence is low, as well as exploring some of the costs and benefits that can accrue from improved government financial reporting.

It will also tease out some of the practical implications associated with fundamental change and identify the risks relating to accounting compliance, audit and change management.

SESSION 3 Suitability of IPSAS and national experiences of reforms

Prof. Dr. Andreas Bergmann, Chair, International Public Sector Accounting Standards Board (IPSASB)

IPSAS - The international financial reporting standards for the public sector

IPSAS are the international accounting and financial reporting standards for governments and international organizations. Entities using them include the European Commission; EU member states such as Spain, Austria, Slovakia and the Baltic states but also many of the fast growing developing countries. Similar to the ESA they are applying the accrual method, since this is the only way to capture all assets, liabilities, revenues and expenses, as well as off-balance sheet items such as contingent liabilities, which are very common in the public sector. Implementation is challenging and usually takes several years. However, the cost is relatively small compared to the returns and the total budget of the entities. Critical for success is a comprehensive approach, which carefully considers the interfaces with budgeting, audit and statistics.

Ingrida Muckutė, Director, Ministry of Finance, Lithuania

Public sector accounting reform in Lithuania: experience, lessons and challenges

The Public Sector Accounting and Financial Reporting System Reform (hereinafter referred to as the Reform) in Lithuania was initiated by the Ministry of Finance of the Republic of Lithuania in 2005.

The purpose of the Reform was to transfer the public sector accounting system from the modified cash basis to full accrual basis in order to enhance transparency, reliability and use of financial information.

Scope

The big scope approach was chosen for implementation of the Reform. It was decided to prepare the National Public Sector Accounting Standards (NPSAS) that comply with the IPSAS on the accrual basis. Application of the accrual basis and NPSAS were established by the law in 2007 and came into force from 1 January 2010, they covered all public sector entities (more than 4000): budgetary institutions (at government and municipal levels), social funds, State Treasury, state monetary funds, municipalities. Pilot projects were implemented on a voluntary basis and they involved 6 institutions that were allowed to start accrual accounting since 2008.

Proceedings of the Reform

The guidelines for the Reform, its major steps and means were set out in the Concept Paper prepared in 2005 (later supplements to it were made in 2008 and 2011, accordingly). The Reform was implemented in two stages. During the period 2005-2008 (Stage 1) necessary legislation was introduced and became effective, a separate set of 26 NPSAS was created as well as the unified chart of accounts, accounting manuals were prepared. Since 2008 the Concept Paper was supplemented by standardization and optimization guidelines (Stage II). The Ministry of Finance initiated creation and installation of standardised accounting IT system in 150 public sector entities (in 2010-2011) and centralised accounting IT system for public sector consolidation (in 2010-2011), established the consultation desk, organised trainings to public sector accountants. The first State Consolidated Financial Statements for 2010 were published on 1 October 2011. In 2013 the first national set of financial statements (State, municipalities and monetary funds) for 2012 will be published.

Challenges still to face

Further steps to be done involve accounting and financial reporting function optimization, encouraging the use of financial statements amongst the management of public sector entities, analysis of financial statements information, interrelation with budgeting and statistical reporting, use of financial information on decision-making, long-term fiscal sustainability planning.

Lessons

For successful implementation of the Reform, support of politicians, involvement of IT experts, the State Treasury and other ministries as early as possible, very precise coordination and communication of the process during the preparation stage in all levels of management, adequate resources allocated for each step, especially for coordination of the process is of major importance.

Gerhard Steger, Director General, DG for Budget and Public Finances, Austrian Federal Ministry of Finance

Accrual Accounting and Budgeting: Why and How? Austrian Reform Experiences

As a key element of a comprehensive budget reform on the federal level Austria introduced accrual accounting and budgeting as of 2013. The annual budget encompasses a cash flow statement and an operating statement to provide Parliament and public with two different perspectives: liquidity and resources. An annual balance sheet comprises a comparison of assets and liabilities.

Austria switched to accruals because relying exclusively upon a cash-perspective is not sufficient to steer public finances: Fiscal illusions might be created and cash does not answer the very relevant question, if a country is richer or poorer than a year ago. As accrual budgeting supports a true and fair view on public finances, it may enhance fiscal accountability of stakeholders.

Implementation of accrual accounting and budgeting is a significant challenge for civil servants, politicians, media and interested public. In Austria the preparation of the new system took several years. External costs of the entire reform (not just accruals) amount to 30 Mio. €.

To make use of new perspectives and instruments in order to derive additional and valuable information from budget documents based on accruals, extensive communication and training is key. The reform design should avoid too much complexity and therefore balance relevance and accurateness.

As accounting standards ensure reliability and comparability of data, Austria used IPSAS as general orientation, although deviated from IPSAS, if that seemed appropriate. Common accounting standards within the EU (EPSAS) would be very helpful.

David Litvan, Accounting Officer, Deputy Director, DG of Public Finances - Ministry of Finance, France

French accounting reform

The DGFiP presentation is the opportunity to remind the advantages of the French accounting reform and the disclosure of the Central government financial statements. The reform has indeed led to improve transparency in financial reporting and quality of the accounts that have been certified for 7 years. Moreover, the reform has also resulted in the implementation of a new ERP system, Chorus, and the linked process re-engineering that serves the modernisation of the French State.

The continuous decrease of the number of qualifications of our certified accounts is an evidence of the improvement of the quality of the central government accounts.

The presentation will also point out that, if the Central government accounting standards are the same as for business, specific features of its activities should be addressed such as:

- the sovereign power, which is an intangible asset unrecognised in the accounts,
- the transfer expenditures without any equivalent in the private sector, that need a dedicated approach based on fulfilment of granting conditions, and
- the specialised nature of the civil servants' pensions plans, that are largely disclosed in the off balance sheet commitments.

This presentation will be another opportunity to reaffirm French support for the objectives of Eurostat on accrual accounting.

Ian Carruthers, Policy and Technical Director, Chartered Institute of Public Finance and Accountancy (CIPFA) and **Karen Sanderson,** Deputy Director, Public Spending, Government Financial Reporting, HM Treasury, UK

Accrual accounting in the UK

The UK utilises accrual accounting across the whole of public sector at a micro level. The UK contends that accrual accounting is essential to improve transparency and strengthen accountability. It ensures that economic events are recognised when they occur and are reported in the period to which they relate, which gives citizens and other users of financial statements with the ability to hold to account those charged with the governance of public sector finances. This is reinforced by the auditing of "bottom up" financial data.

The UK also contends that accrual accounting also leads to significant improvements in public financial management, ensuring that the true economic cost and benefits of policies for the public finances are understood and providing a more complete picture of the overall financial performance and position of the state.

In the UK financial reporting guidance for the public sector is based on EU-adopted International Financial Reporting Standards (IFRS), subject to such adaptations as are necessary for the public sector context. IFRS was chosen as the basis of public sector reporting so that entities operating in the same economy account for the same transactions using the same accounting framework. This improves transparency, as it allows for a comparison between the performance of public and private sector entities using a single accounting framework that is well understood.

In determining the type and form of any proposed EU adopted IFRS adaptation the UK considers International Public Sector Accounting Standards (IPSAS) as one of the guidance sources. Consequently, the UK public sector already complies with many IPSAS requirements, particularly in respect of the recognition and measurement of assets, liabilities, expenses and revenues.

The UK did not collect the cost of either moving from cash to accruals based accounting, or moving from UK GAAP to IFRS based accounts. In the UK each department/Ministry has been responsible for the cost of implementing changes to systems, and for the cost of gathering relevant data and changes to processes. The preparations for each of the transitions lasted several years, with 'dry runs' before the changeover to allow problems to be identified and resolved. The UK does not operate a single financial system.

The UK experience suggests that systems costs are not in themselves the main issue, but more significant are the necessary changes to processes and cultural change. These are both necessary to improve financial management, but it is a long term process to educate non finance staff to use accrual based systems and processes to best effect. The UK view is that this is easier to achieve if accrual based budgeting is implemented alongside accrual accounting, using the same policies for both, as well as for Parliamentary appropriations.