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Accompanying the document

Report from the Commission to the Council and the European Parliament

Towards implementing harmonised public sector accounting standards in Member States

The suitability of IPSAS for the Member States

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CHAPTER 1

1. BACKGROUND AND RATIONALE FOR THE ASSESSMENT

This staff working document accompanies the Report from the Commission to the Council and the European Parliament responding to the request in Article 16(3) of Council Directive 2011/85/EU on requirements for budgetary frameworks of the Member States that ‘by 31 December 2012, the Commission shall assess the suitability of the International Public Sector Accounting Standards for the Member States’.

In the current context of the financial crisis, the role of fiscal discipline in safeguarding economic and monetary union is evident. The corollary of this is that monitoring fiscal discipline should rely on high-quality measurement of the fiscal situation of each Member State. Financial stability is based on trust, and lack of trust in the way the financial situation of the government of Greece was measured has been one element in the sovereign debt crisis. These concerns are reflected in Article 126 of the Treaty on the Functioning of the European Union (TFEU). More rigorous monitoring of the fiscal situation and building better tools to measure and forecast this fiscal situation are the focus of Directive 2011/85/EU¹, of the so-called 6-pack and the 2-pack legislative packages², and of the present staff working document.

This document discusses how one of these tools, the possible role of harmonised accruals-based EU public sector accounting standards, can be used to build this trust.

1.1. The appropriateness of the accruals principle is indisputable, be it for macro or micro fiscal monitoring

There are two principle methods of accounting — cash and accruals — which differ as to the time at which a transaction is recorded. Cash-based accounts record transactions when the amount is received or paid. Accruals-based accounts record when the transaction occurs, regardless of when the payment is actually received or made. Financial management, whether at the macro level (general government) or at the micro level (the government entity) should be based on the principle of accruals accounting. It is important, nevertheless, to note that moving to accruals-based accounts need not mean that the cash basis is abandoned. Cash data remain important, and in many Member States they are used as the basis for government budgeting.

The macro level is already accruals based ...

Currently, fiscal monitoring at EU macro level uses a statistical framework. Article 126 TFEU states that ‘Member States shall avoid excessive government deficits’ and requires the Commission to monitor the ratio of planned or actual government deficit, and the ratio of government debt, to gross domestic product. Neither of these indicators should in principle exceed the reference values specified in Protocol No 12 on the excessive deficit procedure, annexed to the Treaties. The Protocol defines these values

¹ [Council Directive 2011/85/EU on requirements for budgetary frameworks of the Member States.](#)

² http://ec.europa.eu/economy_finance/articles/governance/2012-03-14_six_pack_en.htm.

as 3% and 60%, respectively, for deficit and debt, and lays down the requirement that they follow the definitions of the European System of Integrated Economic Accounts (ESA 95), which is the statistical framework for describing the economy.

ESA 95 records flows on an accruals basis, which it defines as ‘when economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled’. Data based on accruals accounting are indispensable for macro-economic analysis, and in particular for analysing the fiscal situation of general government as a macro agent. GDP, the principal indicator in national accounts, is the aggregate sum of all the outputs of the economy. Output in national accounts is measured on an accruals basis as the economic value created during the reference period, whether or not this output was actually sold during the period. Thus, rather than record output as equal to sales (cash basis), market output is measured as sales plus changes in inventories (accruals basis). Starting with this fundamental way of recording output, the accruals-based approach to measurement is followed throughout the system of national accounts, including for general government.

Accruals accounting is indispensable to the sound monitoring of macro-economic fiscal policy, as it links the accounting recording to the moment the policy is decided and implemented. For example, a VAT rate increase implemented in December will most probably lead to a rise in government cash revenues only in January, taking into account the delay in collecting the tax. However, in accruals accounting this increase in revenue will already start to be recorded in December, to reflect the fact that taxpayers will have already started to pay the higher tax in December. Also, as for a private company, accruals accounting makes it possible to assess the correct balance sheet position of a government at the end of the period, because it takes into account all obligations and claims due at this date, as well as other assets. In the VAT example above, the asset side of the balance sheet at end-December is boosted by the potential VAT to be paid in January. Accruals accounting also makes it possible to relate the change in the balance sheet to revenues and expenses generated during the period. Moreover, accruals accounting in the public sector is a useful tool to avoid some of the window-dressing that is made possible by cash accounting, where payments can be advanced or postponed in order to record them in the period of the government's choosing. Finally, the important advantage of accruals over cash accounting is that both assets and liabilities are consistently recorded, making it possible to have a complete and consistent picture of the real financial position and of whether it is sustainable.

It is because of these advantages that policymakers opted to use ESA 95 as the accounting framework for fiscal monitoring under the Maastricht Treaty, and why this document takes it as given that macro fiscal reporting should be accruals based.

... and accruals accounting is also essential at micro level ...

Whatever is true for macro-economic accounts for the entire general government sector, which is composed of thousands of micro-entities, should also apply to those micro-entities (or at least those of economic significance). Compiling accruals-based accounts for central government budget entities, or for government agencies or large municipalities, is essential to enable the managers of these entities to monitor their economic and balance sheet performances.

There have been a number of initiatives around the world over recent decades, seeking to improve the way public money is used, and to make public entities more accountable. Using accruals accounting to measure the assets and liabilities of government entities can provide answers to essential questions, such as: What are the important assets and liabilities of government entities and how effectively are they managed? Has the financial position improved or deteriorated during a certain period? How vulnerable are government entities to changing economic conditions and financial adversity?

In the interests of accountability, government entities should report on their use of public resources. This should include information that enables citizens and their representatives to assess (a) how the entity has carried out its responsibilities for managing public resources, (b) how those resources have been used to deliver the entity's objectives, and (c) compliance with the necessary controls regulating the use of public money. Such reporting informs economic, political and social decision-making. While individual citizens, and other non-expert users of general purpose financial reports, may have little or no direct capacity to make resource allocation decisions concerning individual government entities, their elected representatives may do.

In summary, the implications of not having robust and transparent accruals accounting for financial reporting and financial management may include an increased risk that government services are being delivered ineffectively or inefficiently, and that investment decisions do not take full account of the potential costs and benefits, for example because they are made with a short-term focus, without paying due regard to their full future costs and benefits. Robust accounting standards are important to ensure that, in difficult financial times, the reported financial information remains both reliable and credible (i.e. trustworthy and accepted as such). Strong standards reduce the scope and the temptation to manipulate information in order to hide problems. The sooner a problem is recognised the sooner it can be addressed. Having early warning of problems often means that their impact is much less than otherwise.

Accruals accounting which conforms to robust accounting standards provides the transparency needed for markets to function properly, without which investors in government securities might enter into transactions without a proper understanding of the level of associated risk. This in turn could create a contagion risk, acting as a significant impediment to financial stability. Transparent financial reporting leads to greater market confidence and lower interest costs.

... finally, micro and macro can converge on the principle of accruals accounting

Accruals accounting is the basis for all macro statistical accounting, such as in the ESA, since it is best suited for analysis, surveillance and policy advice. But the ESA is a macro statistical framework. It is not applicable at the micro level of individual entities. Thus, compiling ESA accounts means using the available entity-level accounts, which have themselves been compiled according to national government accounting standards, and transforming them into ESA terms. When these national government accounting standards are cash-based there is a need to transform them into accruals data, and this can create many difficulties³. Having entity-level audited financial reporting data on an

³ ESA accounts are produced in a many EU countries from cash-based public accounting systems, to which a series of 'accruals adjustments' are made. These adjustments are estimated on a macro basis, and as a consequence they are approximations. Where there are no accruals

accruals basis would substantially reduce the risk of systematic errors in the data used for preparing government finance statistics and hence in the data used for policy-making.

Overall, the case for the ‘principle’ of accruals accounting at macro and micro levels is clear. This document will therefore dwell no further on the ‘principle’ of accruals but rather consider the question ‘which accruals-based system?’

1.2. Towards a harmonised accounting standard?

Member States are legally bound to adhere to the statistical principles and quality criteria laid down in Article 338(2) TFEU. However, even where accruals-based public accounting data are available, there is currently a lack of comparability and coherence between the government accounting standards applied in different Member States, and even within individual Member States. Having common accounting standards would ensure higher-quality and more transparent financial reporting, giving reassurance that government accounts provide a complete and comparable view of the financial position and performance of each Member State, and imparting international acceptance and legitimacy. In the context of enhanced budget integration within the EU, common high-quality accruals standards could be an essential tool for achieving the necessary reliability and comparability of the reported information.

The Excessive Deficit Procedure (EDP) ‘macro’ statistics would be considerably improved by requiring all government entities to use the same accounting standards. It would enable a common bridge table to be used between the upstream accounts and the ESA accounts; this would greatly facilitate the work needed to produce data of the highest quality, as well as the verification process. Having integrated revenue/expenditure and balance sheets would make it easier to eliminate statistical discrepancies. There would be in-built information on contingent liabilities. It would facilitate the emergence of a network of European auditors, able to share their resources, training, and experience in applying a single set of accounting standards. These developments would advance the internal market in financial services, including ancillary services related to public sector auditing. Last but not least, it could pave the way, in the medium term, to a fully integrated public finance system, in which macro accounts could finally be built by aggregating harmonised micro accounts.

This document therefore focuses on the case for harmonised public sector accounting standards in the EU. What it boils down to is ‘Are the IPSASs a suitable set for these future harmonised public accounting standards for the EU Member States?’

1.3. Overview of the staff working document

1.3.1. Description of IPSAS

Chapter 2 describes the International Public Sector Accounting Standards (IPSAS). The links between the private and public sectors in all EU countries create a strong need for connected financial reporting between these sectors, and accruals accounting systems

accounts at the micro level, financial transactions and balance sheets have to be derived from a mix of different sources, leading to a ‘statistical discrepancy’ between the deficit compiled via non-financial accounts and the deficit compiled via financial accounts.

such as IPSAS are very strongly connected to private sector accounting standards. Governments need to achieve the same high quality and transparency of financial reporting as the private sector. IPSASs are developed by the International Public Sector Accounting Standards Board, which is a standing committee of the International Federation of Accountants. They aim ‘to enhance the quality and transparency of public sector financial reporting’. The process of standard setting, the governance of IPSAS and the 32 accruals-based standards are described, along with one cash-based standard.

1.3.2. Current state of play in public accounting and auditing in the EU

ESA data are derived from Member States’ public accounting data, which vary from purely cash-based to full accruals, passing through many intermediate mixed modes. In practice a wide range of accounting systems are used across the EU and even in different government entities within individual countries. Chapter 3 of this document gives an overview of government accounting and auditing practices in the EU Member States.

1.3.3. The relationship between GFS and IPSAS

The United Nations System of National Accounts (SNA) 2008 discusses the links between national accounts and business accounting practices and recognises ‘the increasing use of international accounting standards by corporations and in the public sector’⁴. In particular it frequently refers to ‘the International Public Sector Accounting Standards Board (IPSASB) norms. In several cases, notably on pension liabilities and intangible assets, the feasibility of including certain items in the SNA is dependent on the application of the international accounting standards’⁵. The ESA, which is the European version of the SNA, also considers that ‘In order to extract information from business accounts, national accountants should understand the international accounting standards for private corporations and for government bodies. The standards for private corporations are drawn up and maintained by the International Accounting Standards Board (IASB), and for government bodies, by the International Public Sector Accounting Standards Board (IPSASB)’⁶.

However, the accruals standards that have been developed for the SNA or the ESA are not fully consistent with the accruals standards developed under IPSAS. Chapter 4 of this document gives an overview of the relationship between IPSAS and SNA/ESA-based government finance statistics.

1.3.4. IPSAS and accruals implementation processes

Chapter 5 gives an overview of previous work by the IPSAS Board to facilitate the transition to the accruals basis of accounting, and of their ongoing project on ‘First-time adoption’.

This chapter also summarises the views expressed on the adoption process and on the timetable in the Commission’s public consultation on the suitability of IPSAS for

⁴ [System of National Accounts, 2008](#), page 10, chapter 1.F. ‘Links with business accounting’.

⁵ [System of National Accounts, 2008](#), page 11, chapter 1.F.1. ‘International accounting standards’.

⁶ Proposal for a Regulation on the European system of national and regional accounts in the European Union, COM(2010) 774 , §21.04.

adoption by Member States⁷, which was held in the context of this assessment, and which provides an overview of the costs experienced by countries and entities which have undertaken an accruals implementation project.

1.3.5. Advantages and disadvantages of IPSAS adoption

In practice IPSAS has some important advantages and disadvantages as a reference for the general government entities of EU Member States. The pros and cons of each of the 32 accruals-based standards and of adopting the suite as a whole are discussed in Chapter 6. This part of the document draws on the results of a public consultation and on the focused discussions within a task force composed of experts and practitioners from the Member States.

There is an annex detailing the process used for adopting IFRS accounting standards for the private sector in the EU, and a description of the process used to adopt the accounting rules applicable to the Institutions and other bodies of the EU, which are based on IPSAS⁸.

1.3.6. Conclusions, proposals and timetable

Chapter 7 of this document presents the Commission's conclusions. It sets out the expected benefits, summarises the available information on costs, and discusses the conditions and a possible timetable for adopting harmonised accounting standards for all entities of general government in the EU Member States.

⁷ See http://epp.eurostat.ec.europa.eu/portal/page/portal/public_consultations/consultations/ipsas.

⁸ The process used to set the accounting standards for the EU Institutions and bodies and its relationship with IPSAS is described in Annexes 6.2, 6.3 and 6.4.

CHAPTER 2

2. DESCRIPTION OF IPSAS STANDARDS

2.1. Introduction

The International Public Sector Accounting Standards (IPSASs) are accounting standards developed by the International Public Sector Accounting Standards Board, a standing committee of the International Federation of Accountants (IFAC). IFAC is an international body representing 167 member bodies in 127 countries. Its aim is ‘strengthening the accountancy profession around the world by developing high quality professional standards’. IFAC established the Public Sector Committee, the predecessor of the IPSAS Board, as the standard-setting body for public sector entities in 1987; it initiated the standard-setting programme in 1996.

IPSAS are a set of accounting standards that, according to the IPSAS Board’s mission statement, aim ‘to enhance the quality and transparency of public sector financial reporting’. This objective is to be achieved by:

- ‘Establishing high-quality standards for use by public sector entities;
- Promoting the acceptance, and the international convergence to, IPSASs;
- Providing comprehensive information for public sector financial management and decision making; and
- Providing guidance on issues and experiences in financial reporting in the public sector’⁹.

The standards are accruals based, with the exception of one standard which addresses cash-based accounting¹⁰.

They set out recognition, measurement, presentation and disclosure requirements in relation to ‘General Purpose Financial Reporting’ (GPFR), and related financial disclosures, in a government’s annual reporting.

GPFR comprises not only financial statements (referred to as General Purpose Financial Statements [GPFS]) but also refers to all financial reports intended to provide information that is relevant to the needs of users¹¹.

In some cases the IPSAS Board may issue non-binding guidance on general purpose financial reporting. It may include non-financial, post and prospective financial, compliance, and additional explanatory information¹².

⁹ <http://www.ifac.org/public-sector/about-ipsasb>.

¹⁰ Much of this chapter is focused on the accruals standards; however a description of the cash basis standard is also given at the end of section 2.3.

¹¹ See Conceptual Framework ED 1 Par.1.3.

The core of financial reporting under IPSASs consists of:

- The statement of financial position (IPSAS 1);
- The statement of financial performance (IPSAS 1);
- The cash flow statement (IPSAS 2);
- The statement of changes in net assets/equity (IPSAS 1); and
- The notes to the financial statements, or annex (IPSAS 1).

IPSASs are applicable by governments at national and regional level (e.g. state, provincial, territorial governments), as well as at local level (e.g. municipalities, towns) and related government entities (e.g. agencies, funds, extra-budgetary entities). IPSAS standards are also used by some intergovernmental organisations, but are not designed to apply to government business enterprises (GBEs)¹³.

2.2. Suite of standards

Currently there are 32 IPSAS standards on the accruals basis of accounting. They are numbered by order of issuance. Further standards are being developed.

The majority of these accruals-based standards, where there are no public sector specificities to take into account, are based primarily on existing International Financial Reporting Standards (IFRS), in line with the explicit and overarching aim of convergence between IPSAS and IFRS¹⁴. This is intended to ensure that most transactions common to the private and the public sector are accounted for in the same way.

Public sector-specific standards

In some cases adaptations to IFRSs are needed to meet the specific requirements of the public sector. Where there is no corresponding IFRS to meet a particular public sector requirement, the IPSAS Board issues a new specific public-sector-oriented IPSAS.

¹² The IPSAS Board has issued recommended practice guidelines that are not part of IPSAS (e.g. reporting on the long-term sustainability of an entity's finances). Moreover, the IPSAS Board has issued 14 studies on issues related to public sector financial reports, as well as a number of occasional papers.

¹³ A government business enterprise, that is a financial and non-financial public corporation, is defined as a public sector entity that (a) has the power to contract in its own name, (b) has been assigned the financial and operational authority to carry on a business, (c) sells goods and services in the normal course of its business to other entities at a profit or full cost recovery, and (d) is not reliant on continuing government funding to be a going concern. The standards applied by GBEs are the International Financial Reporting Standards (IFRS) or the private sector accounting standards under their national jurisdiction.

¹⁴ In the private sector the development of IFRS started with GAAP (generally accepted accounting principles) addressing the need to agree common generally accepted principles underpinning financial reporting. IAS (International Accounting Standards) were developed between 1973 and 2001 by the Board of the International Accounting Standards Committee (IASC). In 2001, the newly created International Accounting Standards Board (IASB) took over responsibility for setting International Financial Reporting Standards from the IASC.

IPSASs which have been issued on public sector-specific topics so far and which do not have an equivalent in IFRS are:

IPSAS 21 Impairment of non-cash-generating assets

IPSAS 22 Disclosure of information about the general government sector

IPSAS 23 Revenues from non-exchange transactions (taxes and transfers)

IPSAS 24 Presentation of budget information

IPSAS 32 Service concession arrangements (public-private partnerships).

To enhance initiatives of common interest, the International Accounting Standards Board (IASB) and IFAC signed a memorandum of understanding in 2011 which defined their respective roles in the standard-setting process and in terms of communication and cooperation between them, including in the area of public sector accounting standards.

Any entity wishing to declare itself ‘IPSAS compliant’ must apply all IPSAS standards.

IPSAS measurement bases

Since measurement bases for the different types of assets and liabilities are a key aspect of many IPSASs, a brief description of them precedes the summary of the standards.

The measurement basis determines the value or amount at which an asset or liability is stated at initial recognition and subsequently in financial statements. The principal measurement bases used in IPSAS correspond to those of IFRS¹⁵. They are:

- (a) historical cost (cost); and
- (b) fair value and, related to that, market value.

Historical cost represents the amount of cash or cash equivalents paid to acquire the asset (it is an entity-specific rather than market-based price). In the context of property, plant and equipment, historical cost includes the transaction costs and any directly attributable costs associated with bringing the asset to the location and up to the condition necessary for it to be capable of operating in the manner intended by management.

Where assets are purchased in exchange transactions, a historical cost measurement is easily obtainable and simple to apply. Issues arise when assets are not purchased in a single straightforward transaction or when they are constructed by the entity, where many costs (e.g. labour, materials, energy) have to be allocated. Where several assets are acquired in a single transaction, the price paid must be allocated to the individual assets. Moreover, where assets are subsidised or contributed, a transaction price, even if available, would not faithfully represent historical cost. IPSAS therefore specify that

¹⁵ IFRS 13, applicable from 1 January 2013, defines fair value as ‘the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date’.

where an asset is acquired through a non-exchange transaction, its cost is deemed to be its fair value at the date of acquisition.

Liabilities measured on the historical cost basis are stated at the amount received in the transaction under which the obligation is assumed.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's-length transaction. The definition applies equally to buyers and sellers.

In the absence of market-based evidence, because of the specialised nature of certain items of plant and equipment, fair value may need to be estimated by using a surrogate such as depreciated replacement cost or reproduction cost.

Similar to fair value, IPSAS also defines **market value** as the amount obtainable from the sale, or payable on the acquisition, of a financial instrument in an active market. It therefore reflects the economic and financial environment prevailing at the reporting date.

Fair value is used as the initial measurement basis for financial instruments¹⁶. It is also the subsequent measurement basis for many financial instruments, especially financial assets (most financial liabilities are subsequently measured at amortised cost using the effective interest method). IPSAS 17 — Property, plant and equipment — allows both the cost model or fair value under the revaluation model, for measurement after initial recognition.

Where markets are active and liquid, fair value measurement is likely to be straightforward to apply.

However, in some cases, a market price may not be directly observable. In such cases, observable market-based information may, where available, be used to estimate fair value, but there are cases where valuation models do not rely on observable data. For example, the fair valuation of highly specialised assets (which are encountered frequently in the public sector) or of heritage assets may require more challenging valuation techniques.

In the case of non-exchange transactions (where an asset is acquired for free or at a very low price or where the asset is donated) IPSAS takes the approach that fair value (as at the date of acquisition) is more faithful, representing the actual value received by the entity as a result of the transaction.

Other measurement bases and measurement approaches in IPSAS include amortised cost, current replacement cost (for inventories), net realisable value, settlement amount,

¹⁶ For financial assets or financial liabilities not 'at fair value through surplus or deficit' transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability are added.

recoverable amount, and present value, the definitions of which are, in the IPSAS glossary:¹⁷

Amortised cost of a financial asset or financial liability: The amount at which the financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectability.

Current replacement cost: The cost the entity would incur to acquire the asset on the reporting date¹⁸.

Net realisable value: The estimated selling price in the ordinary course of operations, less the estimated costs of completion and the estimated costs necessary to make the sale, exchange or distribution.

Settlement amount: The best estimate required to settle the present obligation in recognition of provisions, and defined as the amount that an entity would rationally pay to settle the obligation at the reporting date or to transfer it to a third party at that time.

Recoverable amount (of an asset or a cash-generating unit): The higher of an asset's or a cash-generating unit's fair value less costs to sell and its value in use.

Recoverable amount (of property, plant, and equipment): The higher of a cash-generating asset's fair value less costs to sell and its value in use.

Recoverable service amount: The higher of a non-cash-generating asset's fair value less costs to sell and its value in use.

Present value: The discounted cash flows expected to be generated by the asset in the ordinary course of operations. Accordingly, the present value of a liability comprises the discounted cash flows required to be paid to settle the liability in the ordinary course of operations. This measurement basis is used, for example, for measuring provisions where the effect of the time value of money relating to the settlement of the obligation is material. Specific examples of present value are given by IPSAS 21 and 26 for measuring value in use of non-cash-generating assets and cash-generating assets respectively.

More details on these measurement bases and approaches can be found in the description of the standards in the next section of this document.

The IPSAS Board has recently issued an Exposure Draft, Measurement of Assets and Liabilities in Financial Statements, which considers appropriate measurement bases for assets and liabilities, dependent on the economic circumstances. When finalised, this

¹⁷ Discussions held so far on the IPSAS Board's conceptual framework project (see section 2.5.4) have suggested that it will be inappropriate to adopt one single measurement basis for all the elements of financial reporting.

¹⁸ Current replacement cost is only used in IPSAS 12, *Inventories*, in the current suite of IPSASs. A number of features of replacement cost are under discussion in the conceptual framework.

might lead to a change in the measurement bases used in IPSASs. Any change in existing requirements will be preceded by a thorough due process¹⁹.

2.3. The features of the standards

The 2012 edition of the *Handbook of International Public Sector Accounting Pronouncements*, which contains the text of each IPSAS and other explanatory material, is available at:

<https://www.ifac.org/publications-resources/2012-handbook-international-public-sector-accounting-pronouncements>

Short summaries of the accruals standards are provided below. They draw on the information on the IPSAS Board website, in the IPSAS Board handbooks and in other published summaries, to which references are given at the end of this chapter.

IPSAS 1: Presentation of financial statements

IPSAS 1 occupies a key position among the current 32 IPSAS standards in that it sets the objective and the elements required for the presentation of general purpose financial statements (GPFS) by public entities under the IPSAS accruals basis of accounting²⁰.

IPSAS 1 requires a fair representation of the financial position, financial performance and cash flows of an entity. This implies the faithful representation of the effects of relevant transactions, other events and conditions in accordance with IPSAS definition and recognition criteria.

In order to comply with this requirement an entity must comply with general qualitative characteristics which derive inspiration from generally accepted accounting practices and which apply to all IPSAS.

The standard also specifies that an entity can only claim IPSAS compliance when it complies with the requirements of all IPSASs.

The IPSAS qualitative characterises are:

- understandability
- relevance
- materiality
- reliability
- faithful representation

¹⁹ Conceptual Framework Exposure Draft 3, Measurement of Assets and Liabilities in Financial Statements, published in November 2012.

²⁰ The entity on which the set of IPSAS reports (the 'reporting entity') is defined as a government or other public sector organisation, programme, or identifiable activity that prepares GPFRs. A reporting entity may be a 'group reporting entity'.

- substance over form
- neutrality
- prudence
- completeness
- comparability (across time and between entities)²¹.

The standard expressly recognises constraints and trade-offs concerning the relevance and the reliability requirements and more specifically with regard to:

- timeliness
- balance between benefit and costs
- balance between qualitative characteristics.

It also gives definitions of key accounting terms, such as assets, liabilities, future economic benefits or service potential, net assets/equity, revenue, expense, economic entity, government business enterprise, and materiality. It gives general guidelines on how to apply the going concern concept, the consistency of presentation, materiality and aggregation, offsetting and comparative information.

GPFS must comprise the following components:

- a statement of financial position (balance sheet)
- a statement of financial performance
- a statement of net assets/equity
- a cash-flow statement
- a comparison of budget and actual amounts, if the budget is published
- notes on the basis of the preparation of the statements, accounting policies, disclosures, supplementing and explanatory information.

IPSAS 1 lays down minimum requirements on the presentation of financial position and financial performance line items. It also specifies further minimum requirements on the presentation of financial statements, notably with respect to periodicity (at least annual), the coverage of the main financial statements and the classifications to be used within them. With regard to classifications, the items on the statement of financial position (balance sheet) should be classified by maturity (as an exception, classification by liquidity applies when this provides more reliable and relevant information), and there is

²¹ Qualitative characteristics are under discussion as part of the conceptual framework project.

a choice of how to break down expenses in the statement of financial performance (income statement): between nature and function²².

An illustrative financial statement structure is appended to the implementation guidance.

IPSAS 2: Cash flow statement

This standard requires the reporting of changes in the entity's cash and cash equivalents during a given period.

The statement of cash flow must identify the sources of cash inflows, the items on which cash was expended during the period (outflows), and the cash and cash equivalents balance as of the reporting date.

It should classify activities as operating (i.e. from taxes, sales of goods and services, etc.), investing (i.e. cash flow related to property, plant, equipment and other long-term assets, equity or debt instruments, loans, futures contracts, etc.), or financing (i.e. flows related to short or long-term borrowing).

Two methods for compiling the cash flow statement from operating activities are allowed: the direct method (recommended), and the indirect method.

Under the direct method major classes of gross cash receipts and gross cash payments are disclosed. Entities reporting cash flows from operating activities using the direct method are also encouraged to provide a reconciliation of the surplus /deficit from ordinary activities with the net cash flow from operating activities.

Illustrative examples of cash flow-statements are appended to the standard.

IPSAS 3 Accounting policies, changes in accounting estimates and errors

This standard sets the criteria for selecting and changing accounting policies, together with the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates, and corrections of errors.

Accounting policies are the principles, bases, conventions, rules and practices applied by an entity in the preparation and presentation of financial statements. Changes in accounting estimates are adjustments to the carrying amount of assets and liabilities or changes in the useful life of an asset which result from new and more reliable and relevant information and that, accordingly, do not constitute corrections of errors.

The standard provides for a situation where there is no applicable IPSAS available for a transaction, other event or condition.

It prescribes a basis for management judgment in choosing accounting policies — to comply with the qualitative characteristics set out in IPSAS 1 — including the following elements:

²² IPSASs set out minimum requirements and specified statements, but without a mandatory format.

- (1) IPSASs and any relevant implementation guidance dealing with similar and related issues;
- (2) The definitions, and recognition and measurement criteria, for assets, liabilities, revenue and expenses described in other IPSASs; and
- (3) The most recent pronouncements of other standard-setters, notably IFRS, and accepted public and private sector practices.

The standard also deals with the correction of material prior-period errors. These are to be corrected retrospectively in the financial statements for one or more prior periods after their discovery, by restating the comparative amounts for the prior periods in which the error occurred, or by restating the opening statement of financial position if the error occurred before the earliest period presented. There are recognised limitations and constraints in respect of retrospective application and retrospective restatement.

IPSAS 4 The effects of changes in foreign exchange rates

This standard prescribes how entities should account for their foreign currency transactions and foreign operations in their financial statements, and how an entity may translate financial statements into a ‘presentation currency’ (the currency in which the financial statements are presented). This differs from the functional currency, which is the currency of the primary economic environment in which the entity operates. The standard sets the rules for general issues such as the exchange rates to be used (in general spot rates at the time of transaction or position) and the accounting treatment of changes in exchange rates.

IPSAS 5 Borrowing costs

This standard prescribes the accounting treatment for borrowing costs, which include interest and other related expenses (i.e. amortisation of discounts or premiums on borrowings) incurred by an entity in connection with the borrowing of funds.

Two accounting treatments are allowed:

- (1) The expense model (benchmark treatment) under which all borrowing costs are recognised as expenses in the period when they are incurred; and
- (2) The capitalisation model (alternative treatment) under which borrowing costs directly attributable to the acquisition or construction or production of a qualifying asset as part of the cost of the asset are capitalised, but only when it is probable that these costs will result in future economic benefits or service potential to the entity, and the costs can be measured reliably. Examples of qualified assets include office buildings, hospitals, and infrastructure assets.

IPSAS 6 Consolidated and separate financial statements

This standard sets requirements for preparing and presenting consolidated financial statements for an economic entity under the accruals basis of accounting. Together with IPSAS 7 and 8 it also prescribes how to account for investments in controlled entities, jointly controlled entities and associates in separate financial statements.

The standard defines ‘control’ as the power to govern the financial and operating policies of another entity so as to benefit from its activities.

Consolidated financial statements are financial statements of an economic entity defined as a group that includes one or more controlled entities, based on a line-by-line aggregation of similar or identical financial and non-financial items (proportionate method). The only exception is for controlled entities where control is intended to be temporary and held for disposal within 12 months and for which management is actively seeking a buyer.

Minority interests are accounted for separately in net assets/equity.

IPSAS 7 Investments in associates

This standard provides the basis for accounting by an investor where the investment in the associate takes the form of a shareholding or other formal equity investment.

It applies to all investments in which an investor has significant influence (except for a venture capital organisation or a mutual fund, unit trust or similar entity, such as an investment-linked insurance fund, which are measured at fair value).

Significant influence is defined as the power to participate in the financial and operating policy decisions of the investee, but not to exercise control or joint control over those policies. It is presumed to be present if the investment held, directly or indirectly, is 20% or more of the voting power over the associate.

The equity method is used for all investments in such associates. Under the equity method, the investment is initially recorded at cost. It is subsequently adjusted according to the investor’s share of the investee’s post-acquisition change in net assets/equity. The investor’s statement of financial performance reflects in its surplus/deficit its share of the investee’s surplus or deficit.

IPSAS 8 Interests in joint ventures

This standard prescribes the accounting treatment required for interests in joint ventures, regardless of the structures or legal forms within which the joint venture takes place. It applies to all investments in which the investor has joint control, which is defined as the agreed sharing of control of two or more parties over an activity by a binding arrangement.

Joint ventures may be classified as jointly controlled operations, jointly controlled assets and jointly controlled entities.

Different accounting treatments apply for each of these types of joint venture. For jointly controlled entities, two accounting policies are permitted: the proportionate consolidation method (see the description under IPSAS 6) and the equity method (see the description under IPSAS 7).

IPSAS 9 Revenue from exchange transactions

This standard prescribes the accounting treatment for revenue arising from exchange transactions and events.

Exchange transactions are defined as transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to the other party in exchange.

The general principles are that revenue is recognised when it is probable that economic benefits or service potential will flow to the entity, and the amount of the revenue can be measured reliably. Revenue is measured at the fair value of the consideration received or receivable.

When revenue is from the rendering of services and the outcome can be reliably estimated, the reference is to the stage of completion of the transaction at the reporting date. For practical reasons, the standard allows recognition on a straight-line basis over the specified timeframe.

Revenue from the sale of goods can be recognised, subject to the general principles, when: significant risks and rewards have been transferred to the purchaser; there is a loss of effective control by the seller over the good sold; the amount of revenue and the costs incurred or to be incurred in respect of the transaction can be reliably measured; and it is probable that the economic benefits or service potential associated with the transaction will flow to the entity.

Interest is to be recognised on a time proportion basis that takes into account the effective yield on the asset; royalties are recognised as they are earned in accordance with the substance of the relevant agreement; and dividends or their equivalents are to be recognised when the shareholder's or the entity's right to receive payment is established.

IPSAS 10 Financial reporting in hyperinflationary economies

This standard concerns entities reporting in the currency of a hyperinflationary economy, to ensure that the information provided in any financial statement (including the consolidated financial statement) is meaningful.

Any non-monetary items that are not carried at amounts current at the reporting date (such as net realisable value and fair value) must be restated to amounts which are current at the reporting date by applying a general price index. The surplus or deficit from the net monetary position must be disclosed separately in the statement of financial performance.

IPSAS 11 Construction contracts

This standard prescribes the accounting treatment for revenue and costs associated with construction contracts for cases where the public sector entity acts as a contractor. It gives guidelines on items to include in contract costs and contract revenue.

When the outcome of a construction contract can be reliably estimated, the standard rules are for accounting under the 'stage of completion' method, according to which revenue and costs are to be recognised by reference to the stage of completion of contract activity at the reporting date (percentage of completion method). If the outcome cannot be reliably estimated, revenue is recognised only to the extent of contract costs which have been incurred and that will probably be recoverable, and contract costs are recognised as expenses in the period in which they are incurred.

IPSAS 12 Inventories

This standard prescribes the accounting treatment of inventories, notably the amount of costs to be recognised as an asset and carried forward until the related revenues are recognised. The inventories to be covered include goods specifically related to the public sector, such as goods purchased or produced for distribution for 'no charge or for a nominal charge', as well as strategic stockpiles and weapons.

Inventories outside the scope of this standard include work in progress under construction contracts (covered by IPSAS 11), financial instruments (covered by IPSAS 28 and 29), biological assets and agricultural produce (covered by IPSAS 27), work in progress of services to be provided for no or a nominal charge directly in return from the recipients.

Initial measurement is in general at cost. Inventories are subsequently to be measured at the lower of cost and net realisable value. Where inventories are acquired through a non-exchange transaction, their cost is to be measured as their fair value at the date of acquisition. However, inventories are required to be measured at the lower of cost and current replacement cost where they are held for distribution at no charge or for a nominal charge or for consumption in the production process of goods to be distributed at no charge or for a nominal charge.

When inventories are sold, exchanged or distributed, the carrying amount is to be recognised as an expense in the period in which the related revenue is recognised. If there is no related revenue, the expense is recognised when the goods are distributed or related services have been rendered.

IPSAS 13 Leases

This standard prescribes, for lessees and lessors, the appropriate accounting policies and disclosures to apply in relation to finance and operating leases.

The classification of leases depends on the substance of the transaction rather than the form of the contract. A lease is classified as a finance lease if it transfers substantially all risks and rewards incidental to ownership of an asset. The title may or may not be eventually transferred. Examples of criteria that lead to such a classification are:

- The lease covers the major part of the asset's life, or the lessee has the option to purchase the asset at a price sufficiently lower than fair value so that it is reasonably certain that the option will be exercised;
- The ownership is transferred at the end of lease term;

- The present value of lease payments is substantially equal to or greater than the leased asset's fair value.

All other leases are classified as operating leases.

The standard does not cover leases related to exploring non-regenerative resources, licensing agreements for intellectual property and copyrights, investment property covered under IPSAS 16, and certain leases related to biological assets covered under IPSAS 27.

The standard sets the rules of accounting for the leased asset, the outstanding liabilities, the lease payments and the finance revenue in the financial statements of the two parties, for each of the two categories of lease.

IPSAS 14 Events after the reporting date

This standard concerns events, favourable or not for the entity, that occur between the reporting date and the date when the financial statement is authorised for issue.

Events after the reporting date that provide evidence of conditions that existed at the reporting date are considered to be 'adjusting events'; events after the reporting date that indicate conditions arising only after the reporting date are considered to be 'non-adjusting events'.

The reporting date is the last day of the reporting period to which the financial statements relate. The date for authorisation for issue is the date on which the financial statements have to be finalised for issue. The audit opinion is provided on those finalised financial statements.

Only adjusting events should be taken into account in reported financial statements.

This standard also deals with the 'going concern' concept. The standard requires that an entity should not prepare its financial statements on a going concern basis if events after the reporting date indicate that the going concern assumption is not appropriate.

IPSAS 15 Financial instruments

This standard will be superseded by IPSAS 28 to 30 from 1 January 2013, and is therefore not described here. IPSAS 15 nevertheless remains applicable until the new standards apply or become effective.

IPSAS 16 Investment property

This standard prescribes the accounting treatment for investment property and related disclosures.

An investment property is property held (whether by the owner or under a finance lease) to earn rentals or for capital appreciation or both.

The standard does not cover property for use in the production or supply of goods or services or for administrative purposes, or property for sale in the ordinary course of

operations, and does not apply to owner-occupied property or property that is being constructed or developed for future use as investment property.

Investment property is to be recognised as an asset when and only when:

- It is probable that the future economic benefits or service potential that are associated with the investment property will flow to the entity; and
- The cost or fair value of the investment property can be measured reliably.

The standard requires investment property to be measured initially at its cost, including transaction costs. Where an investment is acquired through a non-exchange transaction at no cost, or for a nominal charge, its cost is to be measured at its fair value at the date of acquisition. After recognition an entity may choose to measure the property using either a fair value model or a cost model. If a cost model is chosen, the fair value of the investment property must also be disclosed.

IPSAS 17 Property, plant and equipment

This standard prescribes the accounting principles for property, plant and equipment assets.

These assets include infrastructure assets, such as road networks, sewer systems, and communication networks, special military equipment, heritage assets, and natural, technological and environmental assets.

According to this standard, items of property, plant and equipment are to be recognised as assets only if it is probable that the future economic benefits or service potential associated with the item will flow to the entity, and the cost or fair value of the item can be measured reliably.

The initial recognition of such an asset is generally at cost, with the components of cost described by the standard. For assets acquired through a non-exchange transaction, the cost to be recorded is their fair value at the date of acquisition.

For measurement after recognition, IPSAS 17 allows a choice of accounting models to apply to an entire class of property, plant and equipment:

- Cost model: the asset is carried at cost less any accumulated depreciation and any impairment losses; or
- Revaluation model: the asset is carried at a revalued amount, which is its fair value at revaluation date less subsequent depreciation and impairment losses.

Depreciation is charged systematically over the asset's useful life and separately for each part of the asset's class. The depreciation method must reflect the pattern in which the entity is expected to consume the asset's future economic benefits or service potential.

Subsequent related expenditure on these assets should be added to an asset when they improve the condition of the asset and it is probable that the future economic benefits in excess of the originally assessed value of the existing asset will flow to the entity.

Under this standard the recognition of heritage assets is optional. An entity which recognises heritage assets is required to comply with the standard's disclosure requirements with respect to those heritage assets that are recognised and may, but is not required to, apply the standard's measurement requirements.

IPSAS 18 Segment reporting

This standard establishes principles for the disclosure of financial information by segment, which may be either service or geographical segments.

Each entity is required to analyse its organisation and reporting system to determine each distinguishable activity or group of activities as separate segments where this is appropriate for the purpose of evaluating the entity's past performance and of making decisions about the future allocation of resources.

An entity must then disclose for each individual segment the segment revenue, expense, assets and liabilities, based on the accounting policies applied for the whole group. The standard gives guidelines on how such items can be defined and measured.

IPSAS 19 Provisions, contingent liabilities and contingent assets

This standard defines these items, prescribes appropriate recognition criteria and measurement bases for them, and sets out related disclosure requirements.

The scope of the standard excludes social benefits provided by an entity for which it will not receive consideration that is approximately equal to the value of goods and services provided, directly in return from the recipients of the benefits (i.e. for free or at a 'not significant price'). Other exceptions from the scope of the standard are, notably, provisions arising from financial instruments carried at fair value, provisions arising in relation to income taxes and employee benefits, and provisions covered by other IPSAS.

Contingent assets and liabilities are defined as possible assets and obligations arising from past events whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity. A contingent liability may also be a present obligation that arises from past events but is not recognised because an outflow of resources is not probable or the amount of the obligation cannot be measured with sufficient certainty.

Contingent assets and liabilities are not recognised by an entity in its financial statement, but are disclosed.

By contrast, provisions are a liability which result from present obligations and for which it is probable that an outflow of resources will be required to settle the obligations, but whose timing or amount are uncertain. Provisions are recognised by the entity when a reliable estimate is available and measured at the best estimate of settlement amount of the expenditure needed to settle the obligations. When a large population of items is involved in measuring the amount of provision, the expected

value method of estimation should be used, by weighting all possible outcomes by their associated probabilities.

IPSAS 20 Related party disclosures

This standard aims to ensure that financial statements disclose the existence of related party relationships, where control exists, and provides for the disclosure of information about transactions between the entity and its related parties (for example agency arrangements, leases, licence agreements, finance arrangements, provision of guarantees).

Related parties include parties which control or have significant influence over the reporting entity, such as controlling entities, associates, owners and their close family members, major investors, key management personnel, and entities controlled by the reporting entity.

Disclosure of remuneration of key management personnel and their close family members (including an analysis by type of remuneration) is also required.

IPSAS 21 Impairment of non-cash-generating assets

This standard, which was specifically developed for the public sector, prescribes the procedures that an entity applies to determine whether a non-cash-generating asset — not held with the primary objective of generating a commercial return — is impaired and to ensure that impairment losses are recognised.

Assets that are excluded from the scope of the standard include assets arising from construction contracts and financial assets, inventories, investment property that is measured using the fair value model, and property, plant and equipment and intangible assets that are regularly revalued in accordance with the revaluation models in IPSAS 17 and 31.

The standard states that an entity must assess whether there is an indication that such an asset may be impaired. An impairment loss should be recognised immediately in surplus or deficit when the carrying amount of the asset exceeds its recoverable service amount, which is itself determined as the higher of (a) the asset's fair value less costs to sell and (b) its value in use. In impairment testing it is not always necessary to determine both fair value and value in use; where either of these amounts exceeds the asset's carrying amount, the asset is not impaired.

The standard describes possible alternative approaches to determining fair value less cost to sell for the (frequent) cases of public sector assets not traded in an active market, and defines the value in use of a non-cash-generating asset as the present value of the remaining service potential as determined by a suitable approach (to be chosen from a depreciated replacement cost approach, a restoration cost approach, and a service units approach).

IPSAS 22 Disclosure of financial information about the general government sector

This standard, which was specifically developed for the public sector, establishes disclosure requirements for those governments that elect to present information about

the general government sector (GGS) in their consolidated financial statements. This IPSAS specifically sets aside the application of IPSAS 6, thereby allowing an aggregate presentation which can reconcile the statistical reporting boundary for the general government sector with the IPSAS reporting boundary.

The standard requires a different treatment for investments in the public corporations sectors to what is normally required by IPSASs. IPSAS 6 requires full consolidation of all controlled entities on a line-by-line basis; IPSAS 22, on the other hand, requires the public financial corporations sector and the public non-financial corporations sector to be presented as investments (i.e. in the form of shares or other equity) of the general government sector in other sectors.

The standard specifies the disclosures to be made in respect of the general government sector, which include:

- (a) Major classes of assets, liabilities, revenue, expenses, and cash flows;
- (b) The significant controlled entities that are included in the general government sector and any changes in those entities;
- (c) A reconciliation of the general government sector disclosures and the consolidated financial statements of the government, showing separately the amount of the adjustment to each equivalent item in those financial statements.

IPSAS 23 Revenue from non-exchange transactions (taxes and transfers)

This standard, which was specifically developed for the public sector, prescribes requirements for the financial reporting of revenue arising from non-exchange transactions, other than non-exchange transactions that give rise to an entity combination.

Non-exchange transactions are transactions in which an entity either receives assets or services or has liabilities extinguished, without directly giving approximately equal value in exchange to the other party. Notable examples of non-exchange transactions are taxes and transfers.

The standard recognises as assets (and therefore as revenue, except where a related liability is recorded) the inflow of resources from non-exchange transactions when:

- the definition of assets (from IPSAS 1) is met, and
- the asset is recognised (when it is probable that the future economic benefits or service potential associated with the asset will flow to the entity; and the fair value of the asset can be measured reliably).

An asset acquired through a non-exchange transaction should initially be measured at its fair value as at the date of acquisition. Revenue from non-exchange transactions should be measured as the amount of the increase in net assets recognised by the entity.

On the specific matter of taxes, the standard establishes a general principle that an entity is to recognise an asset in respect of taxes when the taxable event occurs — to be determined by individual jurisdictions on a tax-by-tax basis — and the asset recognition criteria are met. The assets should be measured at fair value, which may mean using an estimation based on historical experience in cases where there is a separation between the timing of the taxable event and the collection of taxes. If necessary, this estimation may be revised in accordance with IPSAS 3.

IPSAS 24: Presentation of budget information in financial statements

This standard, which was specifically developed for the public sector, requires a comparison of (original and final) budget amounts and actual amounts to be disclosed in the financial statements of entities (for those entities which are required or elect to make their approved budgets publicly available). The comparison must be made either as a separate additional financial statement or as additional budget columns in the primary financial statement (the latter only where the financial statements and the budget are prepared on a comparable accounting basis). All comparisons of budget and actual amounts must be presented on a comparable basis to the budget (i.e. accruals or cash).

An explanation of material differences between the budget and actual amounts, and certain other disclosure items, are also to be presented. Notably, where the financial statement and the budget are not prepared on the same basis, there must be a reconciliation at an aggregate level of (a) the actual amounts on a comparable basis to the budget as presented in the ‘statement of comparison of budget and actual amounts’, and (b) the amounts presented in the financial statement.

IPSAS 25 Employee benefits

This standard prescribes the accounting and disclosure for employee benefits. It requires an entity to recognise accrued employee benefits as an expense and liability. The principle underpinning the accounting treatment is that the cost of providing employee benefits is to be recognised in the period in which the benefit is earned by the employee (service rendered), rather than when it is paid or payable.

All forms of consideration provided by an entity to its employees in exchange for services rendered are treated under the standard (i.e. short-term benefits, post-employment benefits, other long-term benefits, and termination benefits), other than share-based transactions and employee retirement benefit plans.

Post-employment benefit plans (predominantly pensions) are further classified as either:

- (a) Defined contribution plans; or
- (b) Defined benefit plans,

and the accounting treatment of these benefits depends on this sub-classification.

Under a defined contribution plan, the entity’s obligation for each period is determined by the (generally undiscounted) contribution; consequently no actuarial assumptions are required to measure the liability and the expense and there is no actuarial gain or loss to be recorded.

Under defined benefit plans, the actuarial obligations are more complex to calculate and there is held to be a probability of actuarial gain and loss.

The standard examines the main parameters needed to calculate the actuarial cost, notably:

- (1) The present value of defined benefit obligations and the fair value of any plan assets (net pension liabilities);
- (2) Current service cost (the annual pension contribution required to cover future liabilities);
- (3) Using the projected unit credit method to measure its obligations and costs;
- (4) Attributing benefits to periods of service under the plan's benefit formula, unless an employee's service in later years will lead to a materially higher level of benefit than in earlier years;
- (5) Using unbiased and mutually compatible actuarial assumptions concerning demographic variables (such as employee turnover rate and mortality of recipients) and financial variables (such as discount rate, future salaries level, future medical costs). Financial assumptions should be based on market expectations at the reporting date, for the period over which the obligations are to be settled. The rate used to discount post-employment benefit plans should reflect the time value of money.

Extensive note disclosures are required for post-employment benefits (for example on the actuarial assumptions used).

IPSAS 26 Impairment of cash-generating assets

This standard sets out the procedures that an entity applies to determine whether a cash-generating asset is impaired and to ensure that impairment losses are recognised. The standard also specifies when an entity should reverse an impairment loss and prescribes the necessary disclosures.

Cash-generating assets are defined as assets held with the primary objective of generating a commercial return.

Assets that are excluded from the scope of IPSAS 26 include assets arising from construction contracts and financial assets, inventories, investment property measured using the fair value model, property, plant and equipment and intangible assets regularly revalued in accordance with the revaluation models in IPSAS 17 and 31, and deferred tax assets and assets arising from employees' benefits.

Under this standard, an entity must assess at each reporting date whether there is any indication that an asset may be impaired. In that case, the entity must estimate the recoverable amount.

An impairment loss of a cash-generating asset is the amount by which the carrying amount of an asset exceeds its recoverable amount.

The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.

The impairment test is performed under criteria listed in the standard.

IPSAS 27 Agriculture

This standard prescribes the accounting treatment and disclosures for agricultural activity.

It applies to biological assets and agricultural produce at the point of harvest when they relate to agricultural activity, with the definition of agriculture activity determining which of those assets fall within the scope of the standard (i.e. the standard does not deal with biological assets used in activities such as research, education or transport).

The standard requires an entity to recognise a biological asset or agricultural produce when:

- (a) The entity controls the asset as a result of past events;
- (b) It is probable that future economic benefits or service potential associated with the asset will flow to the entity; and
- (c) The fair value or cost of the asset can be measured reliably.

Biological assets (including those acquired through non-exchange transactions) and agricultural produce are measured at fair value less costs to sell. The standard establishes initial and subsequent measurement requirements for biological assets and agricultural produce at the point of harvest. Generally, the quoted market price in an active market represents the best measure of the fair value of a biological asset or of agricultural produce. If an active market does not exist, the standard provides guidance on choosing another measurement basis.

IPSAS 28 Financial instruments: Presentation

IPSAS 29 Financial instruments: Recognition and measurement

IPSAS 30 Financial instruments: Disclosures

Taken together, standards 28, 29, and 30 deal with the different aspects of reporting for financial instruments.

IPSAS 28 establishes principles for presenting financial instruments as liabilities or equity, and for offsetting financial assets and financial liabilities.

IPSAS 29 establishes principles for recognising and measuring financial assets, financial liabilities, and some contracts to buy or sell non-financial items.

IPSAS 30 prescribes disclosures that enable financial statement users to evaluate the significance of financial instruments, an entity's financial position and performance, the nature and extent of the risks of financial instruments to which an entity is exposed, and how the entity manages the risks.

The following gives an overview of each standard on financial instruments but is not intended to give a comprehensive description of their requirements.

IPSAS 28

This standard establishes a number of definitions, including financial instruments, financial asset and financial liability, and requires financial instruments to be classified from the perspective of the issuer, according to the substance of the arrangement.

It prescribes principles for classifying and presenting financial instruments as liabilities or equity instruments, for related interest, dividends, losses and gains, and for offsetting financial assets and liabilities. It also deals with more specific instruments such as puttable instruments, treasury shares, and members' shares in cooperative entities, and with specific public sector instruments such as concessionary loans and financial guarantee contracts entered into at nil or nominal consideration.

The standard does not cover interests in controlled entities (IPSAS 6), associated (IPSAS 7) or joint ventures (IPSAS 8), employer rights and obligations under employee benefit plans (IPSAS 23), obligations arising from insurance contracts (except for derivative and financial guarantee contracts), insurance contracts that contain a discretionary participation feature, and share-based payment transactions. It does, however, include insurance contracts that involve the transfer of financial risks.

IPSAS 29

This standard establishes principles for the recognition, derecognition and measurement of financial assets and financial liabilities.

The accounting treatment depends on the category of financial instrument, based on a classification specified in the standard.

Financial assets are classified (for the purpose of measuring a financial asset after initial recognition) in four categories:

- (1) Financial assets at fair value through surplus or deficit;
- (2) Held to maturity investments;
- (3) Loans and receivables; and
- (4) Available for sale financial assets.

Financial liabilities are classified in two categories (for the same purpose):

- (1) Financial liabilities at fair value through surplus or deficit; and
- (2) Other financial liabilities.

An entity is required to recognise a financial asset or a financial liability in its statement of financial position when that entity becomes a party to the contractual provisions of the instrument.

When a financial asset or financial liability is initially recognised, the entity is to measure it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss (surplus or deficit), any transaction costs that are directly attributable to the acquisition or issue of the asset or liability.

An entity may opt to recognise normal purchases and sales of securities in the market place consistently either at trade date or settlement date.

After initial recognition, the entity should measure:

- Financial assets at fair value through surplus or deficit at fair value without any deduction of cost, and available-for-sale financial assets, including derivatives that are assets, at their fair value without any deduction for any transaction cost they may incur on sale or other disposal;
- Loans and receivables and held-to-maturity investments at amortised cost, using the effective interest method;
- Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured, and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments; these are to be measured at cost.

Fair value is defined as the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's-length transaction. The standard also establishes requirements on how to determine fair value (i.e. quoted prices in an active market).

Subsequent measurement of financial liabilities also depends on their classification. Financial liabilities at fair value through surplus or deficit, including derivatives that are liabilities, are measured at their fair value (gains and losses are recognised in surplus or deficit). Other financial liabilities are measured at amortised cost.

The standard also provides guidance on accounting for concessionary loans. These are loans granted to or received by an entity on below-market terms. In this case there is a difference between the fair value of the concessionary loan and the loan proceeds. In the case of a concessionary loan received by a public sector entity, any difference between the fair value of the loan and the transaction price (the loan proceeds) is accounted for in accordance with IPSAS 23. The exchange component is recognised and initially measured in accordance with IPSAS 29. In the case of a concessionary loan granted by a public sector entity, the standard requires that the difference between the fair value of the loan and the transaction price (the loan proceeds) be treated as an expense.

IPSAS 30

This standard establishes disclosure requirements, which include general information about financial assets and financial liabilities by category, and special disclosures when

the fair value option under IPSAS 29 is used. It also covers reclassifications, de-recognitions, pledges of assets, embedded derivatives, and breaches of terms of agreements. Specific disclosures are required for concessionary loans, information and accounting policies, hedge accounting, the fair values of each class of financial assets and financial liabilities, and qualitative and quantitative disclosures about exposures to risks and the management of those risks (the three types of risks identified as credit, liquidity and market risks).

IPSAS 31 Intangible assets

This standard prescribes the accounting treatment for intangible assets that are not covered by other standards, including certain public-sector-specific issues such as intangible heritage assets.

An intangible asset, whether purchased or self-created, is recognised if it is probable that the future economic benefits or service potential that are attributable to the asset will flow to the entity, and the cost or fair value of the asset can be measured reliably.

The definition of an intangible asset includes a requirement that the asset be identifiable (in other words, the asset must be separable from the entity, or arise from a binding arrangement including contractual or legal rights).

Examples of intangible assets that may be recognised by public sector entities in accordance with the standard include acquired computer software, databases, acquired patents and copyrights in areas such as tourism, research, education, and health, and research and development activities.

This standard does not cover powers and rights conferred by legislation, a constitution, or by equivalent means; nor does it cover goodwill arising from an entity combination.

All research costs are expensed when incurred (there is no intangible asset created). Development costs are capitalised only after the entity can demonstrate that the technical and commercial feasibility of the resulting product or services has been established, that the entity intends to complete the intangible asset and use it or sell it, and that it is able to use it or sell it.

The initial measurement is at cost. The standard allows a choice for the subsequent measurement of intangible assets, which may be accounted for using a cost model or a revaluation model. Under the cost model, assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. If an intangible asset has a quoted market price in an active market, the use of a revaluation model is permitted.

IPSAS 32 Service concession arrangements: Grantor

This standard, which was specifically developed for the public sector, prescribes the accounting and reporting requirements for service concession arrangements by the grantor, where the grantor is a public sector entity.

Service concession arrangements are defined as binding arrangements between a grantor and an operator that involve the delivery of public services related to the service concession asset.

Where there is a service concession arrangement, the grantor recognises a service concession asset (and a liability) if:

- (a) The grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them, and at what price; and
- (b) The grantor controls — through ownership, beneficial entitlement or otherwise — any significant residual interest in the asset at the end of the term of the arrangement.

For a ‘whole-of-life’ asset, only the conditions under (a) need to be met.

For initial measurement the grantor must recognise the asset at fair value. Subsequently the asset will be accounted for as a separate class of asset, as either a non-financial asset or an intangible asset, and thereafter measured using the appropriate standard.

Financial reporting under the cash basis of accounting

Although IPSAS is an accruals-based accounting standard, there is also an IPSAS cash basis standard.

The objective of this standard is to provide guidance on financial reporting under the cash basis of accounting, which recognises transactions and events only when cash is received or paid by the entity.

The information required under this standard covers the sources of cash raised during the period, the purpose for which the cash was used and the cash balance at the reporting date. Cash is considered to be controlled by an entity when it can use it to achieve its objectives or can benefit from the cash and exclude or regulate the access of others to that benefit.

The standard gives a definition of cash, including cash equivalents: defined, as in IPSAS 2, as short maturity (i.e. three months or less from the date of acquisition) investments that are readily convertible to a known amount of cash and which are subject to an insignificant risk of change in value.

The financial statements under this standard comprise a statement of cash receipts and payments, accounting policies and explanatory notes. When the entity makes its approved budget publicly available, it may include a comparison of budget and actual amounts either as a separate additional financial statement or as an additional budget column (where the budget and financial statement are prepared on a comparable basis).

The statements of cash receipts and payments disclose the opening and closing cash balances of the entity, the total cash receipts and payments and an appropriate sub-classification thereof, which are normally reported on a gross basis. The standard requires entities to report in a separate column of the statement of cash receipts and payments the total payments and the sources and uses of expenditures made by third parties on behalf of the entity, directly settling obligations or purchasing goods and services for the benefit of the entity, and separating payments made by third parties which are not part of the reporting economic entity which it belongs. General purpose financial statements under the cash basis are to be presented at least annually.

The standard also gives general guidelines on the application of consistency of presentation, aggregation and materiality, comparative information and correction of errors.

Total external assistance (defined as all official resources which the recipient can use or otherwise benefit from in pursuit of its objectives) received in cash should be disclosed separately in the statement of cash receipts and payments. The entity should also disclose separately, either in the financial statement or in the note, total external assistance paid by third parties. The standard also provides for disclosures of external assistance received in the form of loans or grants.

There is also guidance on consolidated financial statements of cash receipts and payments.

Moreover, the standard encourages (but does not make mandatory) additional disclosures. Notably, notes to the financial statements may provide additional information about liabilities, such as payables and borrowings, and some non-cash assets such as receivables, investments and property, plant and equipment.

2.4. The process of IPSAS standard-setting

The IPSAS Board (formerly the ‘Public Sector Committee’ [PSC]) issues standards, exposure drafts for future standards, guidelines, studies and other documents²³.

The IPSAS Board develops a ‘multi-year’ work plan on which the Board reports annually²⁴ as part of the IFAC annual report. The latest work plan for 2013-14 is currently under public consultation for the first time. The work plan defines the projects and initiatives the Board will undertake for the themes for which it considers there is a need to formulate guidance.

The IPSAS Board members, in performing their role, are required to act independently of the organisations which employ them, thereby providing independent standard-setting for the public sector.

2.4.1. The due process

The IPSAS Board adopts a formal process for the development of IPSAS that seeks input and feedback from its constituents²⁵ on important projects, strategic priorities and technical issues in relation to its work programme. The process provides the opportunity for comment from a large base of interested parties: auditors, preparers (including treasuries and finance ministries), standard-setters, professional accounting bodies,

²³ The development of IPSAS was an initiative of the International Federation of Accountants (IFAC) creating (and funding) a ‘Public Sector Committee’ (1997). The PSC has been dealing with public sector accounting since 1987 with guidelines, studies and research report, but only in 1996 was a project launched that was a turning point, with the PSC starting to formulate IPSAS with the aim of improving and harmonising the accounting of public authorities. In 2004 the name of PSC was changed to the IPSASB. The IPSAS Board also issued guidance on the implementation of accruals accounting (‘Study 14’, now in its third edition, dated January 2011).

²⁴ So far, but the results of the current public consultations run by the IPSAS Board, on the work plan and reform of governance of the Board itself, may lead to a revision of the procedure.

²⁵ A Consultative Advisory Group is planned to be created to provide a forum in which the IPSAS Board can consult with representatives of different groups of constituents.

academics, lawyers, and other individuals. The meetings of the Board are open to the public. Agenda papers, including the minutes of the Board's meetings, and meeting highlights are published on the Board's website: <http://www.ifac.org/public-sector>.

As regards the IPSAS standards themselves, the due process starts with a decision by the Board on whether a standard on a certain matter should be developed or not, or if an existing standard should be revised. If the Board approves, a project will be initiated. Depending on the topic, the process for projects normally includes the following major components:

- Consideration of relevant pronouncements (i.e. those issued by IASB, national standard-setters, professional accounting bodies);
- Consultation paper and/or exposure draft for public comment;
- Consideration of comments received on consultation paper and/or exposure draft within the comment period;
- Approval of the standard and its issuance²⁶, which includes a 'basis for conclusion' to explain how the Board reached its position.

The same procedure applies for the withdrawal of a standard.

A consultation paper may be issued in some cases to explore the subject in detail, providing the basis for further discussion and development. Then, or possibly without a consultation paper phase, an exposure draft of the proposed IPSAS is developed, commonly with the input of a task force or task-based group. All exposure drafts and consultation papers are published on the IPSAS Board website with a fixed comment period, typically a minimum of four months. Comments received are discussed by IPSAS Board members, and are also published on the IPSAS Board website.

The approval of consultation papers, exposure drafts, and IPSASs requires the affirmative vote of at least two-thirds of the IPSAS Board members (which corresponds currently to at least twelve of those present at the meeting).

The IPSAS Board has established 'rules of the road' which describe the process for reviewing and modifying IFRS (and in some cases the interpretations of the International Financial Reporting Interpretations Committee (IFRIC)²⁷). This process was established with the aim of converging the IPSASs with the International Financial Reporting Standards. The IPSASB's staff provides the analysis for the Board's discussion of whether or not an IFRS should be adapted for the public sector, i.e. whether there are public-sector-specific reasons for departing from those standards. This

²⁶ In certain cases, there will not be an IPSAS, but some other form of document, for example a 'reporting practice guideline' or other 'non-binding' document. IPSASs are sometimes published in languages other than English; however the English language version is authoritative.

²⁷ The IFRS Interpretations Committee is the interpretative body of the IASB. It has 14 voting members appointed by the trustees and drawn from a variety of countries and professional backgrounds. The mandate of the Committee is to review on a timely basis widespread accounting issues that have arisen within the context of current IFRSs and to provide authoritative guidance (IFRICs) on those issues. Cf. <http://www.ifrs.org/The-organisation/Pages/IASCF-and-IASB.aspx>.

convergence process has an indirect effect in that the current IPSASs are based on concepts and definitions of the IASB's conceptual framework, modified where necessary for a public-sector-specific approach. The current development of the independent IPSAS conceptual framework therefore addresses the recognised need to focus specifically on the public sector perspective.

IPSASs which are 'converged with IFRS' are IFRSs adapted to the public sector context. This requires changes to the style and terminology, and the addition of public-sector-specific examples, but may also involve simplification, clarification, better definition, or amendment arrangements for initial adoption/transitional provisions, to reflect the different public sector environment.

If there are public-sector-specific reasons to depart from IFRS then a second step is applied. This involves either modifying an IASB document and adapting the terminology and style, or initiating a new public-sector-specific project, for example if a topic has not been addressed by IASB or if the public-sector-specific issue is deemed to be so fundamental as to warrant a departure from the IFRS.

2.4.2. *Structure and format of IPSASs*

Guidelines are used to structure IPSASs as follows:

- Overall structure of IPSASs;
- Objective;
- Definitions;
- Basis for conclusions;
- Consequential amendments and effective date;
- Appendices.

In addition a paragraph is dedicated to the scope of the standards.

IPSASs usually contain both authoritative and non-authoritative material. This is indicated in the relevant standards.

Authoritative guidance normally includes the following sections: Objective, Scope, Definitions, Accounting requirements, Disclosure requirements, and Transitional provisions (where additional to IPSAS 3), Effective date and Appendices on application guidance, other authoritative guidance, and amendments to other IPSASs.

The Basis for conclusions, Illustrative decision trees, tables and examples, and Implementation guidance are normally non-authoritative.

The Objective section is the core text of each standard and summarises its purpose. Definitions are provided for terms which are central to the standard. The Basis for conclusions provides background information on the issue and the rationale for adopting a particular approach in a standard where alternatives have been discussed and rejected.

The basis for conclusions should also explain the public-sector-specific reasons why the IPSAS differs from the underlying IFRS²⁸.

2.5. Structure, organisation and governance arrangements of the IPSAS Board

The IPSAS Board operates under the umbrella of the IFAC, which also supports other independent standard-setting boards:

- International Auditing and Assurance Standards Board
- International Accounting Education Standards Board
- International Ethics Standards Board for Accountants

The IFAC, through its standard-setting boards, establishes international standards on ethics, auditing and assurance, accounting education, and public sector accounting, and promotes convergence to the standards issued by the boards as well as to the IFRSs set by the IASB.

IFAC member bodies and associates are professional accounting organisations (in public practice, education, government service, industry, and commerce). A list of IFAC members and associates is available on the IFAC website²⁹.

2.5.1. Membership

The IPSAS Board is composed of 18 volunteer members including a chair and a deputy chair. Members are appointed by the IFAC Board, with 15 members nominated by IFAC member organisations and three members appointed as public members. A public member is expected to reflect the wider public interest³⁰. The IFAC Board has agreed an amendment to the membership criteria effective January 2014 to withdraw the right for IFAC member bodies to be the sole groups who can nominate members for 15 seats. Instead these 15 members can be nominated from a broader constituency, for example governments, public agencies, international organisations, or the general public in addition to IFAC member bodies.

The selection process for the IPSAS Board encompasses factors such as the personal and professional qualifications of a nominee and representational constraints, including gender balance and geographical representativeness of the IPSAS Board, sector of the accountancy profession, knowledge of institutional arrangements, size of the organisation, and level of economic development.

²⁸ For more details see 'International Public Sector Accounting Standards Board Guidelines for Structure and Format of IPSASs' - June 2010 - www.ipsasb.org.

²⁹ <http://www.ifac.org/about-ifac/membership>.

³⁰ IPSAS Board members may be accompanied at meetings by a technical adviser possessing the technical skills to participate in the debate, and who has the privilege of the floor and may participate in projects. The IPSAS Board may grant observer status to representatives of appropriate organisations that have an interest in financial reporting in the public sector and in endorsing and supporting IPSASs, and that possess the technical skills to participate in the debate and provide ongoing input to the work of the IPSAS Board. Observers may attend IPSAS Board meetings, have the privilege of the floor, and may participate in projects. See www.ipsasb.org.

In 2012 the geographical composition of the Board was as follows:

Europe: France, Germany, Italy (public member), UK, Romania, Switzerland (chair and public member)

The Americas: USA, Canada (two members, one of whom is a public member), Uruguay

Asia: Japan, China, Pakistan

Africa: Kenya, Morocco, South Africa

Australasia: Australia, New Zealand

Members currently include representatives from ministries of finance (four members), government audit and accounting institutions (eight members), public practice (two members), academia (three members), and industry (one member). Membership does not include major international bodies, which attend IPSAS Board meetings as official non-voting observers (including Eurostat and the Budget DG for the European Commission, and the International Monetary Fund and the United Nations). The standard term for IPSAS Board members is three years, but a member may serve one additional consecutive term, up to a maximum of six years. The chair may serve three consecutive terms, for a total of nine years. Members' commitment is part-time³¹. The IPSAS Board is currently assisted by 8.5 full-time equivalent staff (one FTE is a visiting fellow), around a third of whom are European nationals, mainly based in Canada³².

2.5.2. *Funding*

The current funding scheme of the IPSAS Board is strongly dependent on IFAC (International Federation of Accountants), Government of Canada, CICA (Canadian Institute of Chartered Accountants) and some multilateral development banks (World Bank, Asian Development Bank). Other sources of revenue include other international, national and regional government entities, for example the governments of China, New Zealand and Switzerland, as well as the United Nations in the past. Some support in the form of personnel may also come from national standard-setters, audit firms and national authorities (currently Governmental Accounting Standards Board USA, UK Accounting Standards Board (past), Ernst & Young and the New Zealand External Reporting Board).

As regards finance, the 2011 IFAC report sets out the latest figures for 2011 for IPSAS Board revenues: Total revenues of \$2 048 093 are financed from external contributions:

³¹ Members contribute about 500 hours per year, whereas the chair contributes about 1 500 hours per year. Cf. response of IPSAS Board to Eurostat public consultation on IPSAS, May 2012.

³² The International Accounting Standards Board (IASB) is an independent group of 15 experts with an appropriate mix of recent practical experience in setting accounting standards, in preparing, auditing, or using financial reports, and in accounting education. Broad geographical diversity is also required. The Board is assisted by a staff of more than 100 professionals, who work with the Board and project teams, conduct research, participate in roundtable meetings, analyse oral and written comments received from the public, and prepare recommendations and drafts of documents for consideration by the Board.

\$ 632 545 (Canada, World Bank, ADB, etc.), IFAC: \$ 1 416 528³³. IFAC (taken together with the Forum of Firms, a voluntary group of 23 large private accounting company networks that support and promote the consistent application of high-quality audit practices and standards worldwide)³⁴ sources account for 69 % of financing.

In the same period, the IFRS Foundation raised £20.6 million for the IASB³⁵. For the latter the European Commission also provided financing in the form of grants (EUR 12.75 million in the 2010-2013 period)³⁶.

Recent work planning has acknowledged the relatively limited resources available to the IPSAS Board at both Board and staff levels, particularly compared with some other standard setting boards (for example the IASB) and there have been calls for a larger and broader funding base.

2.5.3. *IPSAS Board oversight*

At present the IPSAS Board is not overseen by an external body, unlike other IFAC standard setters. Within the IFAC structure, the Public Interest Oversight Board (PIOB) and the Monitoring Group (MG) play a role in oversight of international standard setting in the public interest, specifically for the International Auditing and Assurance Standards Board (IAASB), the International Ethics Standards Board for Accountants (IESBA), the International Accounting Education Board (IAESB), and the Compliance Advisory Panel (CAP)³⁷. Two of the ten members of the PIOB are nominated by the European Commission which is also a member of the Monitoring Group.

In those cases, even if the PIOB does not oversee the technical content of the standard-setting process³⁸ it does provide public interest oversight of due process. As such, it reviews and approves the composition and the roles of the Board, evaluates the procedures, oversees the organisational aspects and suggests projects to be added to the Board's work programmes.

The current funding of the PIOB scheme is extremely dependent on IFAC. The European Commission also contributes up to a maximum of EUR 300 000 per year, which represents around 22 % of total PIOB eligible expenses.

The IPSAS Board has been discussing its structure and governance arrangements over recent months. Many stakeholders perceive these arrangements as inadequate to safeguard the public interest and unresponsive to the independence of the standard-setting process. IFAC has consulted with some governments and other stakeholders and has confirmed this perception. The Board recognises the importance of strengthening its credibility and independence through a more appropriate system of governance, notably with respect to external public interest oversight. Two models have been proposed in this respect:

³³ <http://viewer.zmags.com/publication/ed4395af#/ed4395af/90>.

³⁴ <https://www.ifac.org/about-ifac/forum-firms>.

³⁵ http://www.ifrs.org/The-organisation/Governance-and-accountability/Annual-reports/Documents/AR_2011.pdf.

³⁶ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:253:0008:01:EN:HTML>.

³⁷ The three boards set international standards in their respective areas.

³⁸ See www.ipiob.org for more information.

- A model based on the oversight regime of the existing Public Interest Oversight Board (PIOB, see above). This model would require the appointment of two additional members to the PIOB in order to better serve public sector interests. This model would require additional resources to address the extra costs of the new public sector members as well as increase in PIOB staff resources.
- Oversight carried out by a dedicated body with high public sector involvement. This model would also require additional resources and it is likely that these would be at a significantly higher level than the PIOB model since no such structure currently exists.

At this stage, work is oriented towards the first model. In March 2012 the Monitoring Group launched a public consultation aimed at enhancing the oversight and governance of IFAC, including the IPSASB. It covered a range of topics, including organisational aspects, funding, and the composition and roles of the monitoring group, the PIOB and the standard-setting board. The consultation was closed on 28 June 2012 and the results and analysis of the responses should be available before the end of 2012.

Other proposals under consideration by the Board to strengthen its governance are the appointment of a full-time chair, ideally by 2016 at the latest, the formation of a consultative advisory group by 2014 to 2015, a change in composition of the Board to introduce more public members (applicable for 2014), and greater resources³⁹.

2.5.4. *Latest work programme*

As previously mentioned, the IPSAS Board is developing a conceptual framework for general purpose financial reporting (GPFR) in order to make explicit the definitions and concepts applied by the IPSAS Board in developing IPSAS and the core principles underpinning GPFR by public entities when they adopt accruals accounting. It features the following issues:

- Objectives of financial reporting;
- Scope of financial reporting;
- Qualitative characteristics of financial information;
- Characteristics of the reporting entity;
- Definition and recognition of the elements of financial statements;
- Measurement;
- Presentation.

The conceptual framework is not in itself a new rule-creating standard. Its objective is to provide a guide to developing and interpreting the standards.

³⁹ Further discussion on governance and resources issues in Chapters 5 and 6.

In 2011 the IPSAS Board approved three new projects in which the statistical community (including Eurostat) is actively participating: first-time adoption, IPSAS and GFS, and government business enterprises. These projects have a particular interest for the conceptual and practical issues of IPSASs for statistical needs. They are seen by many statisticians as opportunities to strengthen the link between public sector accounting standards and the statistical bases of financial reporting, and would facilitate the preparation of fiscal statistics, with significant gains in terms of efficiency and information quality.

Other important ongoing projects in the current IPSAS Board work programme include public sector combinations, financial statement discussion and analysis, and reporting service performance.

In July 2012, the IPSAS Board initiated a consultation on its work programme for 2013-14 to seek views on how it should allocate its resources over this period. It will then undertake a broader public consultation of its broad strategic direction in 2014.

ANNEX 2.1: SCHEMATIC REPRESENTATION OF THE IPSAS STANDARDS, GROUPED BY THEIR MAIN FOCUS

Presentation of accounts:

IPSAS 1 - Presentation of financial statements
IPSAS 2 - Cash flow statements
IPSAS 3 - Accounting policies, changes in accounting estimates and errors
IPSAS 10 - Financial reporting in hyperinflationary economies
IPSAS 18 - Segment reporting

Income, and expenditure:

IPSAS 4: - The effects of changes in foreign currency exchange rates
IPSAS 9: - Revenue from exchange transactions
IPSAS 11 - Construction contracts
IPSAS 23 - Revenue from non-exchange transactions (taxes and transfers)

Employee benefits (pensions):

IPSAS 25 - Employee benefits

Financial position:

IPSAS 5 - Borrowing costs
IPSAS 12 - Inventories
IPSAS 13 - Leases
IPSAS 14 - Events after the reporting date
IPSAS 16 - Investment property
IPSAS 17 - Property, plant, and equipment
IPSAS 19 - Provisions, contingent liabilities and contingent assets
IPSAS 21 - Impairment of non-cash-generating assets
IPSAS 26 - Impairment of cash-generating assets
IPSAS 31 - Intangible assets
IPSAS 32 - Service concession arrangements: Grantor

Financial instruments:

IPSAS 28 - Financial instruments: Presentation
IPSAS 29 - Financial instruments: Recognition and measurement
IPSAS 30 - Financial instruments: Disclosures
IPSAS 15 - Financial instruments: Disclosures and presentation (superseded)

Consolidation and controlled entities:

IPSAS 6 - Consolidated and separate financial statements
IPSAS 7 - Investments in associates

Other specific standards (for completeness):

IPSAS 24 - Presentation of budget information
IPSAS 22 - Disclosure of information about the General Government Sector

ANNEX 2.2: REFERENCES CONCERNING THE IPSAS STANDARDS

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CHAPTER 3

3. CURRENT STATE OF PLAY IN PUBLIC ACCOUNTING AND AUDITING IN THE EU

3.1. Diversity within and across the Member States

This chapter summarises current practices in public sector accounting and auditing in the Member States.

Eurostat asked a consultancy to collect detailed information on public accounting and auditing practices for each Member State⁴⁰. The study was designed as a stocktaking exercise and focused on the systems in place in 2012, but some additional information was collected on planned or on-going accounting and auditing reforms, and on how close existing accounting regimes were to IPSAS.

This information was gathered with two objectives: to provide information to support the assessment of this staff working document and to support Eurostat's work on the verification of debt and deficit data reported under the Excessive Deficit Procedure.

In practice, the overview of public sector accounting and auditing practices below shows a rather complicated, disparate picture. Without going into full detail, it shows that current public sector accounting and auditing practices vary widely, not just between Member States but, in many cases, also across different levels of government within Member States.

In the case of some countries, it may be that the information gathered for this study is either incomplete or could benefit from further explanation. In other cases, on-going reforms mean that information will soon become outdated. Eurostat is making available the full report so that it can be further developed over the coming years.

Below is a summary of the main results of the study.

3.2. Overview of public sector accounting practices

Table 3.1 below gives a summary of the main types of public sector accounting practice used in sub-sectors of general government in the Member States.

The study shows that a majority of Member States have public sector accounting practices that can be characterised as accruals or modified accruals accounting across all levels of government. Although accruals or modified accruals public accounting data is available in these Member States, in many cases, parallel cash accounting systems are also maintained, and with few exceptions, budgeting is conducted on a cash basis.

The countries that reported having mixed public sector accounting systems were Austria, Cyprus, Denmark, Germany, Hungary, Ireland, Italy, Luxembourg, Portugal, the Netherlands and Slovenia. These Member States either use differing public sector

⁴⁰ Contract reference 20405.2011.001-2011.219: [An overview and comparison of public accounting and auditing practices in the 27 Member States](#).

accounting practices for differing levels or sub-sectors of government, or, for example, in the case of Slovenia or Hungary, different financial statements are prepared on different accounting bases.

In **Austria**, the new accounting system implements accruals accounting for the federal government, but the states and municipalities operate cash-based systems.

In **Cyprus, Ireland, Portugal and the Netherlands**, central government applies cash or modified cash accounting, while local government uses accruals accounting. In **Portugal and Ireland**, accounting reform, moving to accruals accounting, is underway for central government, and in **Cyprus**, reform is in the planning phase.

In **Germany**, current reforms focus on the modernisation of the cash-based system at central and state levels. A minority of the federal states, and most of the municipalities, have introduced accruals accounting.

In **Denmark**, the central government and regional accounting systems are accruals based, whereas for the municipalities, accounting is mainly cash based.

In **Luxembourg**, central and local government entities, with the exception of public establishments (e.g. research centres, state foundations) and public corporations follow cash accounting principles. Similarly, social funds also use accruals accounting rules based on the general accounting principles following the national GAAP.

In **Hungary, Italy and Slovenia**, a cash/modified cash accounting system applies for all sub-sectors of government, although accruals/modified accruals accounting is also used when financial statements are prepared.

Table 3.1: Summary of the accounting model applied by sub-sectors of government in the Member States

	Central	State	Local	Social funds
Accruals	12	2	14	13
Modified accruals	5	-	4	4
Combination of accruals and cash	5	1	7	4
Cash	4	-	-	1
Not applicable	-	23	-	1
No answer or pending reply	1	1	2	4
Total	27	27	27	27

The overview of Member States' public sector accounting practices shows that they are very heterogeneous. No two countries have the same system or apply the same

standards. Moreover, within many Member States, different accounting regimes may apply for different types of government entities.

Member States with a state government sector tend to have the most complex accounting arrangements, since state governments usually follow their own accounting standards, which may differ from one state to another. More of the newer Member States follow an accruals accounting model than is the case for older Member States. In particular, the Baltic countries seem to have accruals-based standards close to IPSAS. Local governments are more likely to have an accruals accounting model than central governments.

Financial audits

Financial audits are performed in almost all Member States, though the scope of these varies. The approach to financial audit is not necessarily consistent across the EU but, overall, audit arrangements appear to be less heterogeneous than accounting arrangements. With a few exceptions, ISA or ISSAI standards are applied on a voluntary or mandatory basis.

Accounting and auditing reforms

Many Member States are engaged in minor or major reforms, depending on the current status of their accounting and auditing arrangements. One group of countries — mainly those which have recently implemented accruals accounting — are continuously improving and fine-tuning their public accounting systems, while another group is still in the process of implementation. There is also a smaller group of countries in which no reforms are scheduled or in which reforms are at an early stage of preparation. Finland, Poland and Luxembourg have projects underway to enhance their auditing systems.

3.3. Links to IPSAS in the government accounting systems of the Member States

IPSAS is a relatively recent set of accounting standards. The first core set of IPSASs was developed between 1996 and 2002, with major work to add further new standards and achieve substantial convergence with IFRS completed in the decade since then. This means IPSAS was a work-in-progress when many Member States last reformed their public sector accounting systems. As a result, links between IPSAS and national public sector accounting systems tend to be relatively recent.

Nevertheless, the study shows that IPSAS is a point of reference or guidance for public sector accounting standards in just over half the Member States. Table 3.2 summarises how the different accounting standards used by Member States relate to IPSAS.

IPSAS is reported to be referred to or used as a basis for inspiration where deemed relevant for national public sector accounting standards in more than half the Member States (Austria, Belgium, Bulgaria, Czech Republic, Denmark, Estonia, France, Greece, Latvia, Lithuania, Malta, Romania, Slovakia, Spain and Sweden).

The remaining Member States do not refer to IPSAS in their public sector accounting framework, but this does not necessarily mean that they are not aware of it, and, indeed, some of their national standards may nevertheless conform to IPSAS.

Table 3.2: Relationship with IPSAS of the national public sector accounting systems of Member States

IPSAS relation	Total	Percentage
National standard based on or orientated by IPSAS	9	33%
Some IPSAS references	5	19%
IPSAS for some Local Government entities	1	4%
None	12	44%
Grand Total	27	100%

In the study, Eurostat’s consultants developed an indicative measurement of how close each Member State’s national public sector accounting standards were to IPSAS. Such an analysis can of course only give an indication of this, and the main value of the results may actually be the dispersion of the scores, rather than scores for individual countries.

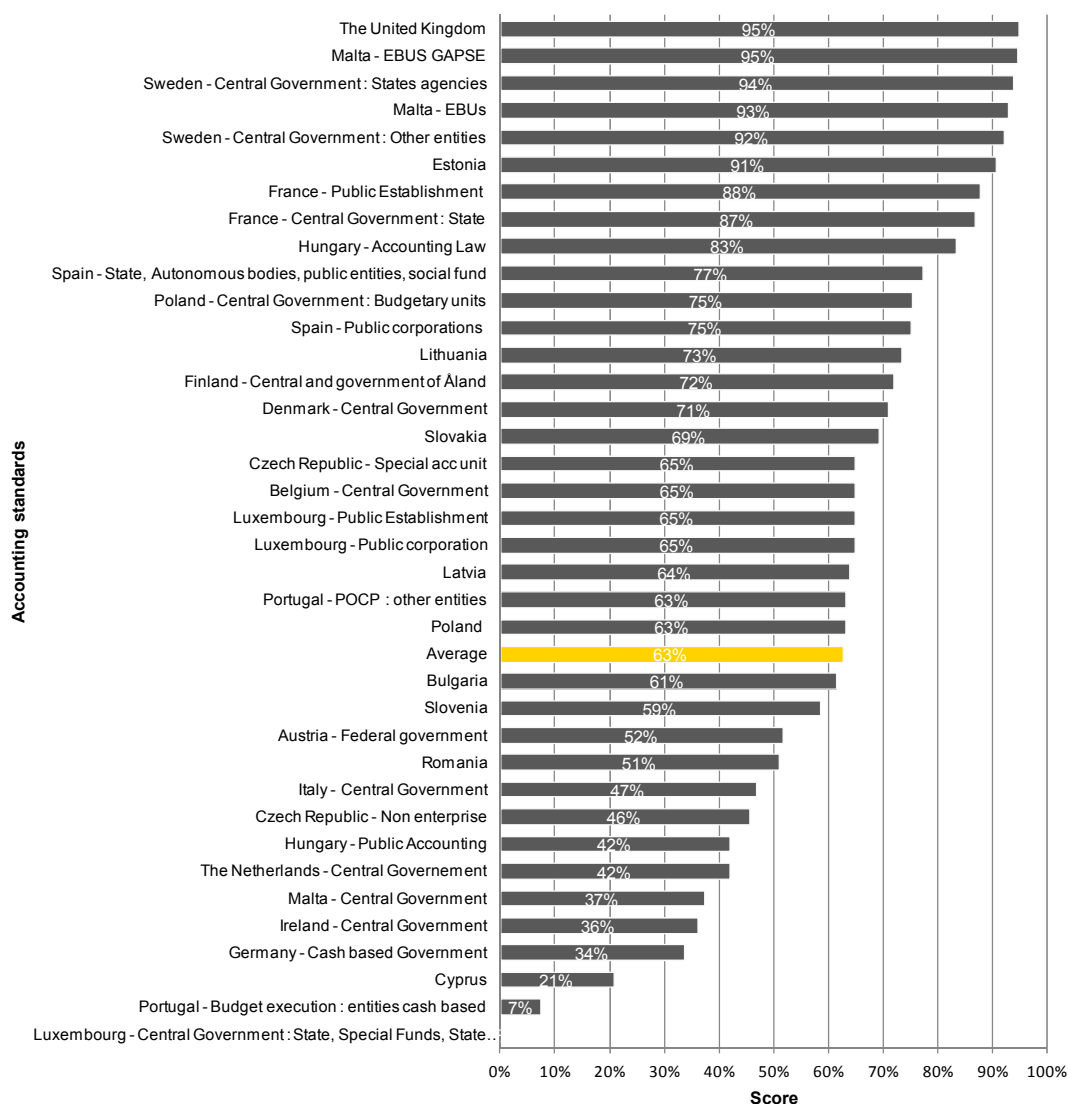
To perform this analysis, four characteristics were considered:

- Presentation of Financial Statements. This dimension seeks to assess whether all components of the Financial Statement required by IPSAS (according to IPSAS 1) are published;
- Time of recording. This dimension indicates whether the accounting system is on a cash or an accruals basis, or modified cash or modified accruals basis;
- Property plant and equipment measurement and recognition. This dimension seeks to understand whether the measurement and recognition of plant and equipment is similar in spirit to the IPSAS principle (in particular IPSAS 17);
- Provision measurement and recognition. This dimension seeks to understand whether the measurement and recognition of provision is similar in spirit to the IPSAS principle (in particular IPSAS 19).

As the analysis only takes into account these four dimensions, a score of 100%, does not necessary mean that a Member State applies IPSAS in full. Given that a system of accounting standards involves more issues than those specified above, this scoring method does not give a full picture of the actual heterogeneity in accounting practices across Member States.

Figure 3.1 shows the outcome of the analysis of the central government accounting practices. The equivalent charts for the other sub-sectors can be found in the complete version of the study.

Figure 3.1: Closeness of Member States' central government accounting practices to IPSAS



Based on this scoring system, the following conclusions may be drawn:

There is great heterogeneity in terms of accounting practices across Member States. Indeed, taking IPSAS as a benchmark, public accounting standards used in Member States range from over 90% similarity to less than 10%.

Member States that apply cash-based accounting standards obviously have the lowest scores for similarity with IPSAS. However, the score is not always close to zero, for example if, despite most or all public sector accounting being on a cash basis, sub-sectors of government publish statements of financial position and performance.

Across the EU as a whole, local government generally scores closer on average to IPSAS than central government.

According to the study, UK public sector accounting standards appeared to be closest to IPSAS. Indeed, the UK public sector accounting standards parallel IPSAS in that they are based on IFRS, adapted to the needs of the UK public sector. This similarity in the origins of the standards explains why UK standards are so close to IPSAS.

It appears that the more complex the national public sector accounting requirements (in the sense that differing requirements apply to different parts of government), the less similar that Member State's accounting standards are to IPSAS. Member States with the least complex accounting arrangements seem to be closest to IPSAS. For example, the UK and Estonia — which apply consistent standards across all sub-sectors of government — scored more than 90% in their similarity to IPSAS.

3.4. Public sector accounting and auditing in each Member State

Below is an overview of public sector accounting and auditing in each Member State. As well as noting the different accounting practices followed in the public sector, the links between IPSAS and national public sector accounting standards are mentioned, as are on-going or planned accounting reforms. There is also a brief description of the scope of the financial audit framework applied in each Member State for general government.

This overview is based on more detailed information gathered within the study.

Austria

In Austria, taking into account the new legal requirements coming into force in 2013, accounting practices are as follows:

- Federal Government accounting
- Budgets and Closed Accounts Regulation
- Internal accounting rules
- Austrian commercial code
- Accounting Regulation

The Federal Government applies the 'Federal Government Accounting Law'. Länder and municipalities apply the 'Budgets and Closed Accounts Regulation'. There are Chambers in the central and state sub-sectors and they apply internal accounting rules. Social funds⁴¹ follow the Accounting Regulation, which is broadly similar to the 'Budgets and Closed Accounts Regulation'. Other entities and government business entities apply general national/international rules (like the Austrian Commercial Code or IFRS).

⁴¹ Detailed information has not been provided on social funds.

The new accounting system takes account of the special needs of the Federal Government and is modelled on IPSAS standards to ensure international comparability.

Austria: Nature of accounting practices in the sub-sectors

Financial statements	Federal government	Länder and municipalities
Statement of financial position (balance sheet)	Accruals accounting	Not applicable
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting
Statement of changes in net asset	Modified cash accounting	Not applicable
Cash flow statement	Cash accounting	Cash accounting

The Court of Auditors performs a financial audit on all sub-sectors. The audit is mandatory and funded through the federal budget. The auditing standards applied are the International Standards on Auditing (ISA) and the International Standards of Supreme Audit Institutions (ISSAI).

Belgium⁴²

Belgium is a federal state in which the regions, communities and municipalities are relatively independent, so there are many different public sector accounting practices.

Belgium: Nature of accounting practices in the sub-sectors

Financial statements	Central government	Flemish local government	Walloon and Brussels-Capital regions local government
Statement of financial position (balance sheet)	Accruals accounting	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting	Accruals accounting
Statement of changes in net asset	Accruals accounting	Modified accruals accounting	Accruals accounting
Cash flow statement	N/A	Accruals accounting	N/A

At Flemish local government level, IPSAS has provided significant inspiration and guidelines for the legislator in developing the reformed accounting and reporting system for local governments.

The local governments of Wallonia and the Brussels-Capital Region have been using a dual accounting system involving a financial accounting (double entry) and a budgetary accounting system (single entry) since 1995.

⁴² Information for state governments and social security funds is not provided.

A project named FEDCOM is currently underway to reform and implement accruals accounting for federal public services.

The Court of Auditors' financial audits include the federal and state levels and the provinces at local level. Municipalities and public corporations are not audited by the Court, but by private audit firms.

Bulgaria

In Bulgaria, public sector accounting practices fall within two broad categories:

Central and local government and social funds apply the same set of rules. These are defined in the Accountancy Act, which is closely linked to ESA and which lays down that the reporting of assets, liabilities, income, expenses and transactions of all budget entities are to be consolidated by the Ministry of Finance on the basis of trial balances and other information submitted under the rules established by the Minister of Finance;

Public hospitals, the National Railway Infrastructure Company, and the Fund for Local Authorities and Governments prepare financial statements under IFRS or the Bulgarian National Financial Reporting Standards for Small and Medium-Sized Enterprises.

Bulgaria: Nature of accounting practices in the sub-sectors

Financial statements	Central, Local government and Social Funds	Public hospitals, NRIC and FLAG
Statement of financial position (balance sheet)	Accruals accounting ⁴³	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	N/A	Accruals accounting
Statement of changes in net asset	N/A	Accruals accounting
Cash flow statement	Modified cash accounting	Accruals accounting

IPSAS is referred to in the Accountancy Act. There are currently no plans for further reforms.

The Bulgarian National Audit Office performs financial audits for central government, local government and social funds.

⁴³ In fact, the budget entities apply accruals accounting. The only exceptions in the consistency of applying the accruals basis are: in budget entities, depreciation is not accrued at the moment and taxes and social contributions are reported on a cash basis (for notification purposes the time-adjustment approach is applied).

Public hospitals, the National Railway Infrastructure Company, and the Fund for Local Authorities are audited by statutory auditors, a Bulgarian-certified public accountant or by a registered auditing company. The National Audit Office follows the International Standards of Supreme Audit Institutions (ISSAI), which are mandatory.

Cyprus⁴⁴

Central government is composed of ministries and independent authorities, special funds and other not-for-profit organisations.

Cyprus: Nature of accounting practices in the sub-sectors

Financial statements	Central government (Ministries, Special Funds) and Social Security Funds	Central government: Not-for-profit organisations	Local government: Municipalities
Statement of financial position (balance sheet)	Modified cash accounting	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Cash accounting.	Accruals accounting	Accruals accounting
Statement of changes in net asset	Modified cash accounting	Accruals accounting	Accruals accounting
Cash flow statement	N/A	Accruals accounting	Accruals accounting

Village authorities, which form a small part of local government, use cash accounting.

The Treasury of Cyprus is currently conducting a study to identify the changes that would be needed and likely effects of a move to accruals accounting following implementation of IPSAS.

An audit by the Auditor General is mandatory for all sub-sectors. An annual work programme covers the financial, compliance, performance and technical audits to be performed. A small number of special funds are also subject to a statutory audit by private audit firms. In addition, the Auditor General may conduct further audit work (financial, performance or other) as deemed necessary.

Czech Republic

In the Czech Republic, public sector accounting practices fall within two broad categories:

‘Special accounting units’ are Government and Parliament, budgetary organisations (ministries, central offices and the Land Fund), state extra-

⁴⁴ Detailed information is provided only for the central government.

budgetary funds, semi-budgetary organisations and local budgetary organisations (regional offices, municipalities, etc.);

‘Non-enterprise units’ include non-profit institutions (public universities, public research institutions, Vine-Grower Funds, schools, associations, etc.).

The social funds are composed of health insurance companies and non-profit institutions. The former are regulated by the Special Accounting Decree for health insurance companies and the latter by accounting decrees for non-profit institutions.

Czech Republic: Nature of accounting practices in the sub-sectors

Financial statements	Special accounting units	Non-enterprise units
Statement of financial position (balance sheet)	Accruals accounting	Modified accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Modified accruals accounting
Statement of changes in net asset	Accruals accounting	N/A
Cash flow statement	Cash accounting	N/A

A reform of public sector accounting was implemented in 2010 by central government, moving to accruals accounting. The objective was to provide accurate, timely, complete and consolidated information regarding the country’s public finances. This reform will affect all levels of government and aims to implement modern accruals accounting in all sub-sectors of government. The national public sector accounting standard is based on IPSAS.

The Supreme Audit Office (SAO) performs audits combining financial and performance audit elements on all central level entities and on entities which manage the property of the State. It has no mandate to audit regional, local entities and municipalities. Auditing standards used by the SAO are close to ISA.

Denmark

Danish public sector accounting practices fall within three categories:

The central government and extra-budgetary entities apply the Government Accounting Law⁴⁵;

The regions apply the Budget, Accounting and Auditing Order for Regions;

⁴⁵ Some deviations from the Government Accounting Law exist for different institutions. For instance, the National Bank accounts for financial assets and debt based on fair value, market value, discounted cash flows, etc. Infrastructure assets and palaces and other cultural properties, for instance, are not accounted for under the accruals-based method. All investments and maintenance are listed and the state of plant and buildings are evaluated.

The municipalities apply the Budget, Accounting and Auditing order for Municipalities.

The social funds follow private sector standards. Financial statements for unemployment funds are prepared according to the legislation that private companies follow if they are not using IAS/IFRS.

The central government and regions use accruals-based accounting, whereas the municipalities use mainly cash-based accounting.

Denmark: Nature of accounting practices in the sub-sectors

Financial statements	Central government	Regions	Municipalities
Statement of financial position (balance sheet)	Accruals accounting	Accruals accounting	Cash and accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting	Cash and accruals accounting
Statement of changes in net asset	N/A	N/A	N/A
Cash flow statement	N/A	Accruals accounting	Cash and accruals accounting

For the central government authorities, the application of IPSAS is an issue that has been and continues to be under discussion. Danish accounting standards were implemented prior to the development of IPSAS, but when changes are considered for certain standards, IPSAS is used as inspiration and, if considered appropriate, implemented in line with other changes. No accounting reforms are planned in Denmark in the near future.

It is mandatory for financial statements of all public sector entities in Denmark to be audited. A financial audit is performed by the National Audit Office for Central Government. Other government institutions, such as universities, high schools, etc., are audited by authorised public accountants, under instruction and review by the National Audit Office. The financial audits of the regions, municipalities and other public entities, such as private schools, public corporations, etc., are performed by authorised public accountants. Auditors apply ISSAI and ISA standards.

Estonia

All sub-sectors of the general government apply the Estonian Generally Accepted Accounting Principles (GAAP), which are based on the Accounting Act, General Rules for State Accounting (based on IPSAS) and Guidelines of the Accounting Standards Board (based on IFRS).

Estonia: Nature of accounting practices in the sub-sectors

Financial statements	All sub-sectors
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Statement of financial position (balance sheet)	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting
Statement of changes in net asset	Accruals accounting
Cash flow statement	Accruals accounting

Profit-oriented corporations can choose to use IFRS. The differences between IFRS and the Estonian GAAP are eliminated in the consolidation process.

There are currently no plans to reform auditing and accounting in Estonia.

For the central government, the National Audit Office performs the financial audit. Local government, the social funds and public corporations are audited by private auditors. The National Audit Office follows ISSAI standards, while private auditors follow ISA.

Finland

The accounting framework for the public sector consists of two separate standards:

The Law on the State Budget for the Central Government (except universities and the limited company Solidium, fully owned by the State of Finland);

The Accounting Act for all other public sector entities. The Accounting Act is the financial framework covering the private sector and complies with the EU Fourth and Seventh Company Law Directives regarding the preparation and presentation of financial statements.

Social security services also belong to this group.

Finland: Nature of accounting practices in the sub-sectors

Financial statements	Central government	Other public entities
Statement of financial position (balance sheet)	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting
Statement of changes in net asset	Accruals accounting	Accruals accounting
Cash flow statement	Accruals accounting	Accruals accounting

The accounting principles are based on Generally Accepted Accounting Principles and do not refer to IPSAS. There are no current plans to implement IPSAS in Finland.

One current reform initiative in Finland relates to auditing, and it concerns the planned consolidation of public sector auditors (chartered public finance auditor) and private sector auditors (authorised public accountants).

It is mandatory for the financial statements of all public sector entities in Finland to be audited annually. For central government entities, in most cases, a financial audit is performed by the National Audit Office. Municipalities and related entities are audited by chartered public finance auditors. All other public sector entities, such as social funds and public corporations, are audited by private sector auditors (authorised public accountants). The auditors of central government entities follow guidelines based on ISSAI and ISA standards. The auditing guidelines are set out in national manuals for local government and the private sector.

France

Public sector accounting practices fall within four broad categories:

The central government, where the Central Government Accounting Standards apply. These accounting standards comprise a set of Orders following the Constitutional By-law on Budget Acts 2001-692 of 1 August 2001. This text refers to the French Private Sector Standards (Plan Comptable General — PCG), IFRS, IPSAS and other specific standards applied to specific issues such as social benefits, tax revenues and heritage assets;

National public establishments — in general⁴⁶ — apply the M9 Order in terms of general accounting and budget. This order was legislated by the Directorate-General for Public Finances (last updated on December 2011) and also refers to the French Private Sector Accounting Standard;

Local government entities follow the M Orders (M14, M52, M71 ...). These accounting standards are enacted by the relevant ministries. The main accounting rules refer to the French Private Sector Accounting Standards;

All systems and entities in the social funds, including social security statutory schemes, apply accounting rules embedded in the French Private Sector Accounting Standards — PCG — (reference applicable to entities in the competitive sector) and are on the whole similar. Concerning social security schemes, there is only one type of accounting (accruals accounting; no budget accounting) and the specific accounting standards derived from the private sector accounting standards (Plan comptable unique des organismes de sécurité sociale — PCUOSS) was adopted in 2001

France: Nature of accounting practices in the sub-sectors

Financial statements	Central government	National public establishments	Local government	Social security funds
Statement of financial	Accruals	Accruals	Modified accruals	Accruals

⁴⁶ Some national public agencies such as the City of Architecture and National Heritage apply the French private accounting standards.

position (balance sheet)	accounting	accounting	accounting	accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting	Modified accruals accounting	Accruals accounting
Statement of changes in net asset	Accruals accounting	Accruals accounting.	N/A	Accruals accounting
Cash flow statement	Accruals accounting	Accruals accounting	N/A	Accruals accounting

While the accounting arrangement may seem complex in terms of the number of accounting laws, French private sector standards are the current root of these, except when the specific characteristics of the public sector require the standards to be adapted. Even if all the orders and accounting laws stem from the Chart of Accounts and could be considered as similar, there are key differences between them on some essential issues.

The French Public Sector Accounting Standards Board (CNoCP: Conseil de normalisation des comptes publics) continuously works to improve the accounting standards of central government, public establishments, regional and local authorities, and social security.

The Court of Auditors performs an annual financial audit on the central government and the most important compulsory health care and pension schemes (General system). Local government accounts are not subject to a financial audit, but a legal audit is performed by the Regional Court of Auditors every four to five years (indicative). The Court of Auditors seeks to follow ISA standards of auditing as closely as possible.

Germany

In Germany, the Haushaltsgesetz, which applies to the central and the state sub-sectors, allows either a cash-based or an accruals-based accounting approach. The Federal Government and the 16 federal states are autonomous and mutually independent in their budget management.

The central government and the majority of the federal states use cash-based accounting and only a minority of states (Hamburg, Hessen, Bremen and Nordrhein-Westfalen) use or have started to implement a full accruals-based approach.

Each federal state has the power to regulate the accounting system for the municipalities located on its territory. In three states, the municipalities may choose a cash-based accounting system. However, most municipalities have introduced accruals accounting. Even if the accounting standards differ between individual states, local governments that prepare accruals-based financial statements follow the German Commercial Code (HGB) to a large extent.

The social funds are composed of statutory pension insurance funds, statutory accident insurance funds, statutory health insurance funds, nursing care insurance funds and statutory unemployment insurance funds:

Pension insurance uses modified cash accounting. The guidance is designed specifically for this entity.

Accident insurance (about 13 entities for private sector employees and about 27 entities for public sector employees) also uses a modified cash basis of accounting (with slightly different guidance for the two sectors).

The health insurance funds (more than 150 entities) and the nursing care insurance funds prepare accruals-based financial statements. The regulations are inspired by the German Commercial Code and therefore show major similarities with this private-law standard.

Unemployment insurance uses cash accounting. The standard is inspired by the Federal Government's accounting law.

The situation of government accounting reforms in Germany is rather diverse. Whereas at local level, accruals accounting has recently been implemented or reforms are ongoing, at federal level, there is commitment to reforming the accounting system within the cash basis of accounting.

Germany: Nature of accounting practices in the sub-sectors

Financial statements	Central government/ majority of State govern- ment (cash based)	Minority of State govern- ments (accruals based)/local governments
Statement of financial position (balance sheet)	N/A ⁴⁷	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Cash accounting	Accruals accounting
Statement of changes in net asset	N/A	N/A
Cash flow statement	N/A	Cash accounting

Financial audits are performed by the Federal Court of Auditors for the central government, by state courts of auditors for state governments, and by regional and local audit offices for local government. The guidelines developed by the International Organisation of Supreme Audit Institutions (INTOSAI) are not mandatory, but accepted as best practice.

*Greece*⁴⁸

The modernisation of public accounting in central government is under way, but for the time being, modified cash accounting is in place.

All sub-sectors of government are audited by the Hellenic Court of Auditors. The Court is responsible for conducting ex-ante and ex-post audits. The former involves the audit of state and public corporation expenditure under specifically-issued laws. The second type of audit concerns the accounts of public accounting officers and the statements of public bodies and local administration agencies.

Hungary

Accounting is uniform for all reporting units within the perimeter of government defined by law and called the 'Legal Government Sector'. Public sector accounting practices fall within two categories:

Public accounting: Public accounting rules for all units that are part of the Legal Government Sector and that follow a government decree with crucial departures from general business accounting. Social funds follow the same accounting principles;

⁴⁷ Only a few, incomplete accruals-based statements of financial position (balance sheet) are available.

⁴⁸ Due to the current Greek crisis, government representatives were for the most part unavailable to contribute to the study. Information on the nature of accounting practices in the sub-sectors is not provided.

Accounting law: The institutional coverage of the ‘Accounting law’ corresponds to units following the general accounting principles either directly in Act C 2000 on Accounting, or in Government Decree 224/2000 (XII. 19.) on the special provisions for book-keeping and preparation of financial statements of other entities.

Hungary: Nature of accounting practices in the sub-sectors

Financial statements	Public accounting	Accounting law
Statement of financial position (balance sheet)	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Cash accounting	Accruals accounting
Statement of changes in net asset	N/A	Accruals accounting
Cash flow statement	Cash accounting	Accruals accounting

In Hungary, there are neither any references to IPSAS, nor any plans to further implement accruals accounting practices.

Financial audit is performed by the State Audit Office for central government, the social funds and local government. Certain types of local government, local government entities⁴⁹ and public corporations⁵⁰ above a certain threshold are audited by private audit firms. The work of the State Audit Office is based on INTOSAI standards.

Ireland

Public sector accounting arrangements fall within two categories:

Central government, which includes the departments of State, extra-budgetary funds, other non-market agencies, other voted expenditure and voluntary and joint board hospitals. Social funds in Ireland are part of central government and are subject to the same accounting law;

Local government, which comprises city councils and educational entities.

Ireland: Nature of accounting practices in the sub-sectors

Financial statements	Central Government	Local Government
Statement of financial position (balance sheet)	Cash accounting	Accruals accounting

⁴⁹ Counties, towns with rights of counties, capital, and capital districts, local governments with annual budgets over HUF 300 million (≈ EUR 1 million) and having debt liabilities or with intention of borrowing are audited by private audit firms.

⁵⁰ This concerns all public corporations, public trust funds, and enterprises that maintain a double-entry bookkeeping system and simultaneously fulfil two criteria: average net sales revenue is higher than HUF 200 million (≈ EUR 0.667 million) and average number of employees is higher than 50 in two preceding years.

Financial statements	Central Government	Local Government
sheet)		
Statement of financial performance (Income statement/profit and loss statement)	Cash accounting	Accruals accounting
Statement of changes in net asset	N/A	N/A
Cash flow statement	N/A	N/A

At central government level, there is a reform agenda to move departments from cash accounting to accruals-based accounting. By the end of 2005, all departments had installed new (separate) information systems. The IPSAS standards are not well known in Ireland, but there are plans to research their applicability as an element of phase two of the accruals implementation reform.

The Comptroller and Auditor General perform financial audits on central government. For local government audits, the Local Government Audit Service provides independent scrutiny of the financial stewardship of local authorities and other local bodies. Auditors apply ISA standards.

Italy⁵¹

Central government uses a modified cash-based accounting system called the ‘legal accruals’ system, which assigns resources in the budget when the obligations with third parties arise. Accruals accounting is also used, but not as the primary accounting system for some components of the financial statement.

According to two recent legislative decrees, the principle for the cash-based ‘legal accruals’ has been modified for local government and a few other kinds of entities into the so-called ‘enhanced legal accruals’. Under this principle, obligations are still recorded when the obligation arises, but the amount is imputed only in the year when payments are due. This innovation has been authorised for three years on an experimental basis. After this, a decision will be made concerning the basis on which harmonisation in public accounting will proceed.

Italy Nature of accounting practices in the sub-sectors

Financial statements	Central Government	Local Government
Statement of financial position (balance sheet)	Modified accruals/modified cash accounting	Modified accruals/modified cash accounting
Statement of financial performance (Income statement/profit and loss statement)	Modified accruals/modified cash accounting	Modified accruals/modified cash accounting

⁵¹ Information for social security funds has not been provided.

Financial statements	Central Government	Local Government
Statement of changes in net asset	N/A	N/A
Cash flow statement ⁵²	Cash accounting	Cash accounting

Major reforms are planned over the coming year that will significantly change the accounting and auditing framework. The fundamental aspect of the current reform is the provision for an enabling act to harmonise the accounting systems and budget formats of general government bodies; therefore a single, consistent normative framework is laid down for all entities forming part of general government. The reform of the general accounting framework does not currently contain any reference to IPSAS principles.

The Court of Auditors is responsible for the *a priori* audit of the legality of Government acts, and also for the *a posteriori* audit of the State Budget's management. Ultimately, all state spending falls within its remit. Audit work is carried out by the Court's central and regional chambers, with specific audit offices examining, at central level, each ministry. On a voluntary basis, the Court of Auditors seeks to follow European Standard of Auditing standards as closely as possible.

Latvia

All general government entities, except public corporations and units, reclassified by the Central Statistical Bureau from the non-financial corporation sector to the general government sector, apply the same Government Regulation on Budgetary Institutions Accounting, which refers to IPSAS, and the general principles of the national law on accounting. Public corporations and reclassified units apply the national law on accounting and national accounting rules.

Latvia: Nature of accounting practices in the sub-sectors

Financial statements	All sub-sectors of government
Statement of financial position (balance sheet)	Accruals accounting, cash accounting for recoverable, modified accruals accounting for taxes and transfers payable
Statement of financial performance (Income statement/profit and loss statement)	Modified accruals accounting
Statement of changes in net asset	Modified accruals accounting
Cash flow statement	Accruals accounting and cash accounting

To ensure the further development of national legal bases for accruals accounting, a project to develop national IPSAS-based accruals accounting standards is expected to take place within the next three to five years, with possible further reconciliation with ESA and EDP statistics requirements.

⁵² Cash flows are recorded for GFS purposes only as neither central government nor local government prepare a cash flow statement.

The institution in charge of the financial audit at both central and local government level is the State Audit Office. For government and municipal entities, there is also a financial audit, which is carried out by private firms. Auditors apply ISA standards.

Lithuania

There is a single accounting principle, defined by law, which is accruals accounting for all levels of government. In addition to accruals accounting, all entities have to prepare budget execution reports, which are based on cash. The accounts are kept according to national requirements of public sector financial reporting and accounting standards, which are based on IPSAS.

Lithuania: Nature of accounting practices in the sub-sectors

Financial statements	All sub-sectors of government
Statement of financial position (balance sheet)	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting
Statement of changes in net asset	Accruals accounting
Cash flow statement	Accruals accounting

The National Audit Office is responsible for performing financial and performance audits on central government, social and health funds. Local governments are audited by local government controllers that are subordinate to the Council of local government and apply the methodology of the National Audit Office. Public audit requirements have been established by the Law on State Control and approved by the Order of the Auditor General and were replaced by direct application of ISA and ISSAI for financial audits from 1 June 2012.

Luxembourg

Public sector accounting practices fall into five categories:

Entities following the ‘Law of 8 June 1999 on government accounting’: The financial reporting of the Head of State, Parliament, Government, ministries, special funds and state services (such as high schools and museums) is cash based;

Public establishments (such as research centres and state foundations) have used a standard Chart of Accounts PCN since 2011. The generally accepted accounting principle is based on the national LUX GAAP⁵³;

Public corporations follow private sector accounting standards;

Municipalities and cooperations of municipalities use the ‘modified local accounting law’;

Social funds use uniform social security accounting rules based on LUX GAAP, the generally accepted accounting principles.

⁵³ Although a Chart of Accounts can also be tailored to an organisation’s specific needs, e.g. Law 28 February 1994.

Luxembourg: Nature of accounting practices in the sub-sectors

Financial statements	Entities following the government accounting law	Public establishments	Public corporations	Municipalities, cooperations of municipalities	Social funds
Statement of financial position (balance sheet)	N/A	Accruals accounting	Accruals accounting	N/A	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	N/A	Accruals accounting	Accruals accounting	N/A	Accruals accounting
Statement of changes in net asset	N/A			N/A	
Cash flow statement	N/A			N/A	

Luxembourg applies a uniform presentation of the annual accounts for each sector. It does not comply with IPSAS. A reform introducing a new standardised Chart of Accounts for the budget is underway, concerning municipalities and cooperations of municipalities.

The accounting of central government entities is subject to legal, financial and performance compliance audits from the Court of Auditors. Some are also subject to financial audit from private audit companies. Local government entities are subject to legal and financial audit performed by the Ministry of the Interior and some are also subject to financial audit from private audit companies. The social security funds are subject to legal and financial audit from the General Inspection of Social Security. The approach of the Court of Auditors does not currently follow international audit standards. A project is underway to develop auditing practices for public entities.

Malta

Public sector accounting practices fall within the following categories:

Central government. Social security forms also part of central government;

Extra-budgetary units (EBUs) and public corporations applying IFRS;

Smaller extra-budgetary units applying General Accounting Principles for Smaller Entities;

Local councils.

Malta's central government (Government/ministries and departments) reporting is laid down in the Financial Administration and Audit Act (Chapter 174), where, under Article 67, one finds the reporting requirements that the Accountant General has to present for each financial year. Such information as required by law is presented in the Financial Report published annually and presented to Parliament no later than six months after the close of the fiscal year. This Financial Report includes a detailed analysis of the financial transactions on a cash accounting basis.

Malta: Nature of accounting practices in the sub-sectors

Financial statements	Government / ministries and departments	EBUs and public corporations	Smaller EBUs	Local councils
Statement of financial position (balance sheet)	Modified accruals accounting	Accruals accounting	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting	Accruals accounting	Accruals accounting
Statement of changes in net asset	N/A	Accruals accounting	Accruals accounting	Accruals accounting
Cash flow statement	Accruals accounting	Accruals accounting	Accruals accounting	Accruals accounting

In 2002, the Treasury Department started preparing accruals-based Financial Statements. To date, these have only been used for reporting purposes and have never been published. Currently, such Statements are not statutory. Thus it follows that they are neither presented to the Parliament nor comprehensively audited.

While ministries and departments use the Central Government Chart of Accounts, extra-budgetary units, public corporations and local councils use their own Chart of Accounts.

Some IPSAS standards are partially implemented. There are plans to implement IPSAS as the accounting standards to be used by central government, although the plan is still in the initial stages and no timescale is yet available.

The National Audit Office performs the financial audit of the government, ministries and departments and extra-budgetary units. Extra-budgetary units, public corporations and local councils are subject to a private financial audit. The auditing standards used are ISA and ISSAI.

Netherlands

Accounting standards differ between central government, local government and social funds:

Central government applies the standards in the ‘Comptabiliteitswet’; the law which sets the rules for budgeting and reporting. The more detailed outlines and models are written down in the ‘Rijksbegrotingsvoorschriften’, a regulation from the Finance Minister.

Local government uses an accounting standard for local governments (‘Besluit Begroting en Verantwoording’), which refers to the Dutch private sector accounting standards laid down in the Dutch Civil Code Book 2, part 9;

Social funds include only social security services, which apply the national GAAP (the ‘RJ’) and Dutch Civil Code Book 2, part 9.

Netherlands: Nature of accounting practices in the sub-sectors

Financial statements	Central government	Local government	Social funds
Statement of financial position (balance sheet)	Cash accounting ⁵⁴	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	The income statement is a mix of cash accounting (receipts and expenditures) and an oversight of liabilities	Accruals accounting	Accruals accounting
Statement of changes in net asset	N/A ⁵⁵	Accruals accounting	Accruals accounting
Cash flow statement	Cash accounting	N/A	Accruals accounting

Central government applies a cash accounting system, while local government and social funds use accruals accounting. However, local government is not fully on an accruals basis, as some items are on a cash basis, or not recorded. There are currently no plans for accounting reform or for implementing IPSAS.

⁵⁴ The state balance is in accordance with ESA standards. The ESA standards are accruals based.

⁵⁵ The statement of changes in net assets is included in the disclosure of the state balance.

The Court of Auditors performs financial audits for central government. The financial audit of local government and social funds is performed by private accounting firms, except for the municipalities of The Hague and Amsterdam. These two cities have their own audit service. The auditing standards are based on, and in line with, ISA as far as possible.

Poland

Public sector accounting practices fall within two categories:

Public entities with legal personality (including social funds) — applying the Accounting Act;

Budgetary units — applying the Accounting Act and Minister of Finance Regulation

In Poland, all entities, whether public or private, apply the Accounting Act. The budgetary units also apply the Accounting Act provisions. However, in addition, they also follow the special provisions of the Regulation of the Minister of Finance of 5 July 2010 on special accounting rules and charts of accounts for the state budget, and for some other units of the public sector. These provisions help the budgetary units to issue the (cash-based) statements on budget execution. They also provide for a special Chart of Accounts and a template of the financial statement adjusted to the specific character of the public sector.

Poland: Nature of accounting practices in the sub-sectors

Financial statements	Entities applying the Accounting Act	Entities applying the Accounting Act and Minister of Finance Regulation (Budgetary units)
Statement of financial position (balance sheet)	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting
Statement of changes in net assets	Accruals accounting	Accruals accounting
Cash flow statement	Cash method	N/A

IPSAS is neither applied nor referred to in Poland.

The Supreme Audit Office audits budget execution for central government, the National Bank of Poland, state legal entities, and other state organisations. The Office does not audit financial statements. It applies national audit standards. Currently, there is a reform of audit procedures underway in accordance with the amendment to the Act on the Supreme Audit Office of 22 January 2010. The objective is to streamline and legally consolidate the audit process.

Portugal

While the government accounting arrangement may seem very complex in terms of number of accounting laws, the current root of all of these laws is the Official Plan of Public Accounting (POCP). This is an accruals-based accounting system, and integrates three interconnected subsystems in one accounting system:

Budgetary accounting (modified cash basis) — linked to patrimonial accounting by accounts 251 and 252 — debtors and creditors

*Patrimonial*⁵⁶ accounting — accruals basis

Analytical accounting — costing by functions and by product/area — accruals basis

Some specific sub-sectors, such as education, social security, local government and the health sector, also use a system similar to POCP, the philosophy, principles and rules of which are almost identical (sectoral plans).

We can, however, distinguish two accounting practices:

Entities of the State, non-profit institutions of central government and regional government only use budget execution accounting (cash basis), although this will change over the next few years. For these entities, statements of financial position and performance are not applicable;

Other entities applying the POCP, and therefore using accruals accounting, integrating accruals and budget execution accounting operations.

Most of the public corporations at different levels of government apply private sector standards greatly inspired by IFRS.

Portugal: Nature of accounting practices in the sub-sectors

Financial statements	Entities on cash basis	Other entities
Statement of financial position (balance sheet)	N/A	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	N/A	Accruals accounting
Statement of changes in net asset	N/A	N/A
Cash flow statement	Cash accounting	Cash accounting

The POCP was approved by the Decree-Law 232/97 of 3 September and was a major step in the reform of the public accounting and financial administration in Portugal. The starting point for reflection on the need for accounting reform was the objective of modernising public accounting and providing essential tools to support management of

⁵⁶ Business accounting.

public entities and performance evaluation. The reform is still in progress and changes are to be expected in standard-setting accounting, namely, IPSAS adoption. However, no timeline has been set.

The ‘Inspecção-Geral de Finanças’ (IGF) performs the financial audit for the central and local government, social services and public corporations. But it is the ‘Tribunal de Contas’, the Supreme Audit Office, which is the independent body with a nationwide audit remit and with the most substantial area of work in ex-post audits, including performance audits. It is mandatory to apply the Audit and Procedures Manual. ISSAI is followed on a voluntary basis.

Romania

All general government entities apply the same accounting standards.

Romania: Nature of accounting practices in the sub-sectors

Financial statements	All sub-sectors
Statement of financial position (balance sheet) ⁵⁷	Modified accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Modified accruals accounting
Statement of changes in net asset	Modified accruals accounting
Cash flow statement ⁵⁸	Cash accounting

At the time of writing, only certain provisions of some IPSASs have been implemented. Over the next three years, national norms will be improved with other provisions. Beyond that period, additional provisions from IPSAS will be implemented if they are deemed necessary. Although certain regulations are inspired by IPSAS principles, no explicit reference is made to IPSAS as such.

The Romanian Court of Auditors performs financial audits on central government, local government and social services. The Court has developed its own standards in accordance with generally-accepted international audit standards. The standards are close to ISA.

Slovakia

A single accounting law applies to all sub-sectors of government, i.e. central government, local level government and social funds.

⁵⁷ As regards the system used for the financial position time of recording, according to the applicable legislation no obligations are provided for pensions, impairment is optional, depreciation is partially provided for.

⁵⁸ Concerning the cash flow statement, the direct method — receipts and payments — is used. The cash flow includes flows from operational, investment and financing activities, for each evidencing receipts, payments and net cash. Details are presented in the implementation account.

The Ministry of Finance has adopted accruals-based accounting principles, based on, but not fully compliant with, IPSAS principles. The Ministry of Finance intends to apply all IPSAS principles in the near future, as there are still some differences between current public sector standards and IPSAS.

Slovakia: Nature of accounting practices in the sub-sectors

Financial statements	All levels of government
Statement of financial position (balance sheet)	Modified accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Modified accruals accounting
Statement of changes in net asset	N/A
Cash flow statement	N/A

There is a project intended to implement a single state reporting and accruals accounting system. This project, initiated by the Ministry of Finance, will affect central and local government. The objective is to improve the accounting and reporting system in the public sector to enhance macroeconomic performance and fiscal transparency of public finances.

The Supreme Audit Office is responsible for legal audits. Internal financial audits are conducted by the Ministry of Finance in compliance with the Act on accounting rules. Audit reports will start to be publicly available from 2013. The SAO complies with auditing standards issued by INTOSAI.

Slovenia

The Law on Accounting provides accounting rules for any entity that uses public funds from the State Budget. It does not make a distinction between central government and local government (municipality) entities⁵⁹.

Slovenia: Nature of accounting practices in the sub-sectors

Financial statements	All levels of government
Statement of financial position (balance sheet)	Modified accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Modified accruals accounting/ cash accounting

⁵⁹ The difference in accounting arises between entities that use public funds but are not registered corporations and those that are normal registered corporations but are owned effectively by central government or local government. The entities that use public funds but which are not registered corporations follow more of a cash-based accounting system. The registered corporations that are effectively owned or controlled by central government or local government need to follow the same accounting rules (Slovenian Accounting Standards, which are similar to IFRS in most cases) as all registered corporations (publicly or privately owned).

Statement of changes in net asset	Modified accruals accounting
Cash flow statement	Cash accounting

None of the financial statements are purely accruals based, contrary to IPSAS, but a modified accruals accounting is generally used. Cash flow statements are drawn up on a cash accounting basis. No changes are planned and no reform is currently underway.

The Court of Auditors performs an annual legal and financial audit of the final account of the central government budget and social security funds. The final reports of other general government units (municipalities, public extra-budgetary funds, public agencies and public institutions of the central and local governments) are occasionally subject to legal, financial, performance compliance and IT audits by the Court of Auditors. The implementation of ISSAI standards is mandatory for the Court of Auditors.

Spain⁶⁰

Public sector accounting practices fall within the following categories, representative of the heterogeneity of accounting practices in Spain:

Entities applying the Public Accounting General Plan and Accounting Rules, including the State, autonomous bodies, public entities and social security funds;

Public corporations (financial and non-financial) following the Accounting General Plan, including non-profit institutions;

Autonomous communities applying the Regional Financial Laws and their own regional public accounting plans;

Local government applying the Local Financial Law and Public Accounting Plan for Local Bodies;

The Central Bank applies the Eurosystem standards.

Spain: Nature of accounting practices in the sub-sectors

Financial statements	Entities following Public Accounting General Plan and accounting practices	Public corporations
Statement of financial position (balance sheet)	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting
Statement of changes in net asset	Accruals accounting	N/A

⁶⁰ Information for autonomous communities, local governments and the central bank has not been provided.

Cash flow statement	Cash accounting	Accruals accounting
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In 2010, the Spanish administration adopted a new, IPSAS-based Accounting General Plan and Accounting Rules, and is currently working on adapting the public consolidation regulation to IPSAS principles. The nature and scope of the existing plan for reform is the consolidation process; to define the framework applicable to the State, the autonomous and local public sector; and to adapt the Spanish public accounting regulation to IPSAS.

The Court of Auditors and the regional courts of auditors perform a financial audit on all sub-sectors (ex-post control). On a voluntary basis, the Court of Auditors seeks to follow ISA standards of auditing as closely as possible. The General Control and Audit Office (IGAE) and the General Control delegations at agencies level play the role of internal controllers.

Sweden

Public sector accounting practices fall within four broad categories:

Central government authorities;

Other central government entities;

Local government (municipalities, municipal associations and county councils);

Social security funds.

Sweden: Nature of accounting practices in the sub-sectors

Financial statements	Central government authorities	Other central government entities	Local government	Social security funds
Statement of financial position (balance sheet)	Accruals accounting	Accruals accounting	Accruals accounting	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting	Accruals accounting	Accruals accounting	Accruals accounting
Statement of changes in net asset	N/A	N/A	N/A	N/A
Cash flow statement	Accruals accounting	Accruals accounting	Accruals accounting	N/A

The Swedish accounting system is accruals based. On a basic level, there are strong similarities between the State's accounting principles and IPSAS definitions and principles, as national standards are influenced by IPSAS and other standards. At present, no major accounting or audit reforms are being considered.

Central government authorities, including the Swedish Pension Agency, come under the scope of the financial audit of the Swedish National Audit Office. Municipalities, municipal associations and county councils are audited by auditors appointed by the municipal or county council. Other central government entities and the Swedish National Pension Insurance Funds are audited by private audit firms. The auditors aim to follow ISA standards of auditing as closely as possible.

UK

Accruals accounting was introduced for central government departments and other entities in 2000 (local government entities have accounted on an accruals basis since the 19th century). Initially, UK GAAP was applied, but since 2009, accounting has been on the basis of IFRS, adapted as necessary for the public sector. Budgeting rules are also on an accruals basis, aligned as far as possible with IFRS, but with some differences to reflect ESA 95 statistical accounting standards. Technical accounting standards are provided through financial reporting manuals issued by the relevant authorities. These manuals are prepared with advice given by the Financial Reporting Advisory Board, an independent body of experts whose role is to promote the highest possible standard in financial reporting by government and to help ensure that any adaptations of, or departures from, EU-adopted IFRS are justified and properly explained.

UK: Nature of accounting practices in the sub-sectors

Financial statements	All sub-sectors of government
Statement of financial position (balance sheet)	Accruals accounting
Statement of financial performance (Income statement/profit and loss statement)	Accruals accounting
Statement of changes in net asset	Accruals accounting
Cash flow statement	Accruals accounting

Public sector entities in the United Kingdom apply EU-adopted IFRS, adapted for the public sector. Overall, the system is similar to IPSAS principles. Where EU-adopted IFRS is adapted and interpreted for the public sector, IPSAS is among the standards that can be used as a reference in developing these interpretations and other adaptations.

The National Audit Office performs financial audits of UK-wide central government departments and a wide range of other public bodies. The devolved governments are audited by Audit Scotland, the Wales Audit Office and the Northern Ireland Audit Office respectively. At present, the institution in charge of commissioning audits for English local government is the Audit Commission, with private sector firms undertaking the audit work. Audit Scotland, the Wales Audit Office and the Northern

Ireland Audit Office either audit or commission audits of local government within their remit. Public corporations are audited by private auditors. All financial audits are conducted according to national auditing standards issued by the Financial Reporting Council, which comply with EU requirements and with the standards of the International Federation of Accountants.

CHAPTER 4

4. THE RELATIONSHIP BETWEEN GOVERNMENT FINANCE STATISTICS AND IPSAS

4.1. Introduction

EU governments produce two main types of financial data on their activities — Government finance statistics for fiscal policy purposes (including statistics for the Excessive Deficit Procedure), and accounting and budgeting reports for accountability and decision-making purposes relating to individual entities or groups of entities.

The relationship between the two types of report is important, in respect of both transparency (explaining to users the differences between the data in the respective reports) and efficiency, since public accounting systems are generally the fundamental source of data for compiling government finance statistics (GFS). This chapter analyses the relationship between EU GFS and IPSAS.

EU Government finance statistics are based on the methodological rules of the European System of Accounts (ESA 95), set out in Council Regulation (EC) No 2223/96. The ESA 95 is based on the worldwide System of National Accounts (SNA 1993), and is supplemented by further Eurostat decisions and guidance, most notably the ESA 95 Manual on Government Deficit and Debt.

The European System of Accounts is currently being revised to bring it into line with the SNA 2008, and the ‘ESA 2010’ is expected to come into force in 2014. Given that few fundamental changes are being made with respect to GFS, the analysis in this chapter is largely unaffected by the revision; however, it anticipates ESA 2010 changes in some places.

It is also important to note that EU Member States also prepare government finance statistics for reporting to the International Monetary Fund (IMF)⁶¹. Given that the IMF’s Government Finance Statistics Manual is based on the SNA, the conceptual differences between the IMF and EU GFS data are minimal; however, there are some presentational differences. This chapter focuses on the relationship between EU GFS and IPSAS.

4.2. Background

Statisticians and accountants have a long tradition of cooperation over the years, and it is noticeable that the development of the SNA has drawn heavily on the principles and presentation of business accounting. Statisticians recognise that their data sources are often based on financial reports. Nevertheless the SNA recognises that there are some fundamental differences in approach:

The design and structure of the SNA draws heavily on economic theory and principles as well as business accounting practices. Basic concepts such as

⁶¹ Nearly two-thirds of EU Member States cooperate with Eurostat, so that Eurostat prepares their GFS reporting to the IMF from data reported to Eurostat.

production, consumption and capital formation are meant to be rooted in economic theory. When business accounting practices conflict with economic principles, priority is given to the latter, as the SNA is designed primarily for purposes of economic analysis and policymaking.

In the case of government financial data, Eurostat and IMF statisticians have been observers at the IPSAS Board for a number of years, and have worked with IPSAS Board staff on projects to explore the relationship between GFS and IPSAS.

A Task Force on Harmonization of Public Sector Accounting (TFHPSA) was created in 2003. The TFHPSA's major areas of work were to develop proposals for changes to government finance statistics and/or to IPSASs in the context of the 2008 update of the SNA, and in doing so to document the similarities and differences between the two reporting systems. The Task Force published a detailed report in 2005⁶² and an active work programme was initiated, which notably led into the preparation of a new IPSAS 22 (Disclosure of Financial Information about the General Government Sector) in 2006 and to input for the preparation of SNA 2008.

4.3. Conceptual differences between IPSASs and statistical guidelines

There are many similarities between IPSAS (based on business accounting approaches) and GFS (based on national accounting approaches). Both systems seek to prepare an integrated and consistent dataset (with data on both stocks and flows), with accruals as a guiding reporting principle.

However, as mentioned above, the systems have different objectives, and this leads to certain differences of both substance and presentation. Financial statements based on IPSASs are predominantly intended to meet the need for management accountability, providing an evaluation of financial performance and position, and thereby aiding decision-making. GFS are intended to be used in a macroeconomic analysis context, with an emphasis on international comparability of aggregate data on government finances.

This difference in objectives is most evident in the entity on which the dataset reports (the so-called 'reporting entity').

- In the European System of Accounts, institutional units are aggregated (generally on a consolidated basis) into sectors and subsectors. Each individual entity in the economy is analysed with respect to its autonomy of decision making, to determine if it can be considered to be an institutional unit. Those government-controlled units that are primarily engaged in non-market (including redistributive) activities are included within the 'general government sector', which is the headline reporting entity used for Excessive Deficit Procedure purposes⁶³.

⁶² Available at <http://www.ifac.org/sites/default/files/publications/files/international-public-sector.pdf>.

⁶³ One might nevertheless note the growing interest in data on the activities of public corporations in the context of EU economic governance reforms.

- Under IPSAS the ‘reporting entity’ is a government or other public sector organisation, programme or identifiable activity that prepares general purpose financial reports (GPFRs). A key characteristic of a reporting entity is that there are ‘users’ who depend on these reports for information about the entity. The financial information of any bodies controlled by the reporting entity is wholly consolidated in its financial statements. Whilst it is possible to compile a set of IPSAS-based statements for an aggregate of entities, including across government, this is rarely done in practice⁶⁴.

There is, however a standard which covers ‘Disclosure of financial information about the General Government Sector’ (IPSAS 22). This standard specifically sets aside the application of the usual IPSAS consolidation rules (IPSAS 6), thereby allowing presentation of a general government set of IPSAS-based accounts which can be used to reconcile the statistical reporting boundary for the general government sector with the IPSAS reporting boundary⁶⁵.

It is conceivable that statistical boundaries can form a basis for drawing a reporting boundary in public accounting, without (as in IPSAS 22) being the precise boundary. This kind of approach can bring the two systems closer together, whilst leaving some flexibility for reflecting specific national circumstances, though at the cost of introducing a possible lack of harmonisation between jurisdictions.

Whilst there are many further differences in detail between IPSAS and GFS⁶⁶, three major groups of conceptual differences can be found in the recording of stocks and flows.

(3) Treatment of revaluations

GFS record all holding gains and losses (revaluations) in a separate account for ‘other economic flows’, and therefore they are not included in recorded revenues, expenditures, or the net lending/net borrowing of government. This approach reflects the view that revaluations can be considered as not being under government control and are therefore not relevant to fiscal policy analysis.

IPSAS requires the majority of revaluations and changes in value to be recorded in the Statement of Financial Performance (and therefore in the ‘bottom line’) as they are perceived to be relevant to a measurement of government’s activities. The main exceptions to this are foreign exchange gains and losses related to foreign subsidiaries and revaluations of property, plant, and equipment. These value changes are included in a separate financial statement, the Statement of Changes in Net Assets/Equity.

(4) Recognition criteria for assets, liabilities, revenue and expenses

⁶⁴ A notable exception, though on an IFRS and not IPSAS basis, is the Whole of Government Accounts project implemented in the United Kingdom.

⁶⁵ In practice IPSAS 22 has not been fully applied in any country. The closest one may find internationally is probably the presentation by the Australian government of its financial statements, which are closely reconciled with government finance statistics. This is summarised on the Consultation Paper issued under the IPSAS/GFS project (see section 4.5).

⁶⁶ These differences are not covered here, but are described in the IPSAS Board’s Consultation Paper mentioned in section 4.5. Examples include recording of research and development, licences and service concessions.

GFS and IPSAS are both based on the principle of accruals and therefore seek to record economic transactions in the period in which they occur, with a notable caution in anticipating future events. Nevertheless GFS treat uncertainty about future economic outflows differently from IPSAS, recognising fewer liabilities than IPSAS. This may be seen in the following areas:

- Guarantees, and related contingent liabilities, are generally not recognised in GFS until they are called⁶⁷. IPSAS requires that where there is a present obligation and an outflow will probably occur, a reliable estimate of the amount involved should be recognised as a liability.
- IPSAS provides for the recording of provisions defined to be liabilities of uncertain timing or amount (IPSAS 19, paragraph 18). Provisions include obligations for which there is no counterparty, for example provisions for restructuring and environmental restoration. They also include such issues as non-performing loans. GFS do not record provisions because the national accounts system is necessarily symmetric and the values of assets and related liabilities must match.

Differences in the recognition of liabilities will lead to differences in the recording of revenues and expenditures under the two systems (for example, in general, expenditure relating to guarantees will tend to be recorded earlier under IPSAS than under GFS).

(5) Valuation

GFS adopts a general philosophy of using current market prices as the valuation basis for assets and liabilities⁶⁸. IPSAS requires the use of current market prices for many classes of assets and liabilities. However, for some classes, for example property, plant and equipment, IPSAS allows the use of either current market prices or historic cost. For a small group of assets, most notably inventories, IPSAS requires a valuation basis other than current market prices. Both systems allow for proxies to current market prices.

It should nevertheless be noted that IPSAS requires the valuation basis for all assets and liabilities to be disclosed and, where reporting is at historic cost, IPSAS often encourages or requires disclosure of fair value, if there is a material difference between the historic cost and fair value.

Finally, the use of historic cost in the valuation of non-financial assets in IPSAS-based accounts will also lead to differences between the measure of depreciation in these accounts and the measure of consumption of fixed capital in GFS (which is a current prices-based concept). In general, during periods when asset prices rise, measures of depreciation are lower than measures of consumption of fixed capital. It should also be noted that whilst IPSAS treats depreciation as a cost in the Statement of Financial Performance, GFS includes gross fixed capital formation as expenditure when calculating the surplus/deficit.

⁶⁷ ESA 2010 will introduce a concept of ‘standardised guarantees’ which will lead to the recording of liabilities.

⁶⁸ Note, however, that Maastricht debt measures, relevant to the EDP, are based on nominal valuation.

(6) Application of the accruals principle

Whilst the accruals principle is shared by GFS and IPSAS, there are some operational areas of application of the principle which can be identified as potentially leading to differences in recording. One significant area for Europe is the time of recording of tax and social security contribution revenue: where GFS allows the possibility for Member States to record them on a ‘time-adjusted cash’ basis, as an alternative option to an assessment basis (which is consistent with the approach in IPSAS for non-exchange revenue under IPSAS 23). A large majority of EU Member States now use the time-adjusted cash approach for most of their recording of taxes and social contributions. Whilst the overall amount of revenue recorded on aggregate over time should be equal under the two approaches, the distribution of that recorded revenue across time is likely to be different.

4.4. Presentational differences

In addition to conceptual differences between IPSAS and GFS, the way in which the information is presented and the terms that are used (for the same or similar concepts) are often different. It can therefore be difficult to compare GFS data and IPSAS financial statements and disclosures, even if the underlying information is consistent.

Differences in presentation may be found at three levels:

(a) The titles and purpose of statements

The ESA system has a standard presentation of non-financial and financial sector accounts, which is used for both general government and other sector accounts of the economy and rest of the world⁶⁹. In addition, the EU has adopted a specific approach⁷⁰ to presenting the following statistics:

- Government Revenue
- Government expenditure
- Government Deficit/Surplus
- Transactions in Assets
- Transactions in Liabilities
- Other Economic Flows
- Balance Sheets

IPSAS-based statements are described in IPSAS 1, and as a minimum include:

⁶⁹ This is described in more detail on the dedicated Eurostat web pages for sector accounts, to be found at http://epp.eurostat.ec.europa.eu/portal/page/portal/sector_accounts/introduction/.

⁷⁰ See Eurostat’s GFS website, under the link to summary tables:
http://epp.eurostat.ec.europa.eu/portal/page/portal/government_finance_statistics/introduction.

- Statements of Financial Position or Statements of Assets and Liabilities (both equivalent to balance sheets),
- A Statement of Financial Performance (also called Income Statement), Statement of Revenues and Expenses, Operating Statement, or Profit and Loss Statement — which captures the type of transactions which fall into GFS government expenditure, revenue and deficit/surplus⁷¹, and
- A Statement of Changes in Net Assets, which includes some elements which GFS records as other economic flows.

(b) The breakdowns provided

GFS, like most statistical datasets, use a highly standardised set of economic and functional classifications to ensure comparability. For example, GFS relies on a standardised functional breakdown (health, education, etc.) to present government expenditure. These detailed classifications are very useful for the analysis of the financial aspects of government policies by specific domain. Whilst there are certain fixed line items and breakdowns in IPSAS-based financial reports — for example a distinction between current and non-current assets and liabilities — there is also some greater flexibility in presentation, for example reporting on ‘segments’ to fulfil the requirements of IPSAS 18 (segment reporting).

(c) Additional information provided

GFS statisticians are encouraged (and in some cases obliged) to publish their data alongside supporting information on the sources, methods and information on significant transactions or developments as metadata or footnotes to statistical reports. In addition to legally required data (in the European Union, under the EDP reporting procedure and ESA transmission programme), GFS statisticians may also report memorandum series on a voluntary basis. But it must be said that the volume of detailed information which is required and published in the EU is very significant.

IPSAS-based statements have far fewer lines of information and breakdowns than GFS. However, the notes to the financial statements can be particularly detailed since they must include a summary of significant accounting policies, further detailed information about individual items reported on the face of a statement (for example, a break-down of property, plant and equipment into classes), information about items that are not recognised but nonetheless important (for example, contingencies) and risk information related to financial instruments.

GFS, like other main statistical series, serve users by presenting (often long) time-series of comparable data, which means that new source data, methodological changes and errors identified lead to revision of past data. In the case of EU GFS statistics, data are compiled and published both annually and quarterly. IPSAS only requires annual reporting, but allows for the possibility of more frequent reporting. Financial statements presented according to IPSAS require comparative information about only one previous

⁷¹ A major difference is in the treatment of holding gains and losses, which are included in a Statement of Financial Performance but are not treated in GFS as expenditures and revenues.

year, adjustments to prior years can be made (the number of prior years is not specified).

4.5. Latest initiatives

In 2011 the IPSAS Board approved a new project, the Alignment of IPSASs and Public Sector Statistical Reporting Guidance project, to further enhance and promote the reconciliation and harmonisation of IPSAS and public sector statistical reporting guidance. Eurostat and IMF statisticians are actively participating in the project.

The project has a broad approach, dealing with both conceptual issues and practical issues, such as guidance on developing an integrated Chart of Accounts designed to encompass both IPSAS and statistical needs.

A Consultation Paper relating to the project was published on 17 October 2012, seeking comments from constituents by 31 March 2013⁷².

The main points raised in the Consultation Paper — in addition to a detailed description of work undertaken to date and the main methodological comparisons between the systems — are as follows:

- (7) The IPSAS Board notes that in some areas — due to different user requirements and therefore conceptual approach — certain differences will remain between IPSAS and GFS, and will therefore need to be managed. The strategy for managing them rests on three possible (and complementary) approaches, which may be applied according to the type of difference to be managed:
 - (a) Choice of IPSAS accounting policy options. The IPSAS Board notes that where IPSASs offer options to preparers, one option may be aligned or close to the GFS approach. It has proposed that these options be highlighted in documents providing guidance for the adoption of accruals accounting, so that preparers are aware of this when choosing between possible options.
 - (b) Chart of accounts design. The IPSAS Board notes that chart of accounts design can address several types of difference, in particular presentation differences. The IPSAS Board proposes guidance on the development of integrated charts of account.
 - (c) Production of additional data. The IPSAS Board acknowledges that some additional information may need to be prepared for GFS compilers, if it is not built into the chart of accounts.
- (8) The IPSAS Board identifies certain initiatives as possibilities with respect to IPSAS. In addition to general approaches which would raise the profile of GFS issues when standards are developed and discussed, there are also some specific proposals which may relate to ongoing or future projects. For example,

⁷² <http://www.ifac.org/publications-resources/ipsass-and-government-finance-statistics-reporting-guidelines>.

one involves — with the cooperation of GFS compilers and the International Valuation Standards Council — analysing the basis for valuation of assets between the two systems. The IPSAS Board also identifies that the current IPSAS 22 (reporting on the general government sector) has not been taken up by preparers, and considers a number of options to address this. The IPSAS Board asks for comments on its proposals and any further suggestions for opportunities to improve alignment.

- (9) There are also certain initiatives mentioned which GFS compilers could take with respect to alignment. In addition to possible joint work on valuation, specific issues mentioned include extractive industries, service concessions, research and development, and low interest rate loans. The Board asks if any further issues can be identified.

The IPSAS Board has requested comments on the consultation paper by 31 March 2013 and will then analyse responses and pursue the project. In the consultation on its 2013/2014 work programme⁷³, the IPSAS Board set out plans to agree an exposure draft in September 2013 and to conclude the project in September 2014⁷⁴.

4.6. Commission considerations

In contrast to many other regions of the world, the public profile of GFS is very high in the EU because they are directly used in European policy making and fiscal control, and — in the absence of harmonised public accounting standards — have become, *de facto*, a common public accounting standard.

Many Member States take great account of statistical considerations when designing and implementing budgetary policy and in their national budgeting and accounting systems. Data users are particularly interested in the reconciliation between public accounting data published at national level and government finance statistics, and sometimes argue that differences between the two raise quality concerns on the data, even when such differences are purely conceptual in nature.

The underlying prerequisite for compiling high quality government finance statistics is a robust accruals-based public accounting system that is subject to strong internal controls and independent audit. This has become increasingly apparent in Europe, and Eurostat has taken concrete steps in developing its role in this area.

This context explains the importance of the interaction between possible implementation of micro-accounting standards, such as IPSAS, in Europe and the existing GFS-based structure. The two would need to exist side by side in the future.

The IPSAS Board's ongoing project on IPSAS/GFS makes practical suggestions for further convergence between IPSAS and statistical reporting, whilst recognising that some conceptual differences will continue to need to be managed.

⁷³ See <http://www.ifac.org/publications-resources/ipsasb-consultation-paper-2013-2014-work-program>.

⁷⁴ Some of these initiatives could be taken earlier as they do not require changes in standards.

It is nevertheless important to underline that implementation of accruals-based public accounting systems (whether IPSAS-based or not) should involve statistical considerations from the start. For example, the IPSAS/GFS study component on designing charts of account is expected to contribute to this convergence, and could potentially be broadened to efficient external access to, and processing of, information⁷⁵. Furthermore, incorporating statistical classifications into EU public accounting standards would also improve the link between micro and macro data.

It should also be noted that public accounting standard setting in Europe is much more closely associated with statistical guidelines than elsewhere in the world, and any future governance arrangements must take this into account.

⁷⁵ For example by drawing on experience of implementation of XBRL-based reporting in the private sector.

CHAPTER 5

5. IPSAS AND ACCRUALS IMPLEMENTATION PROCESSES

5.1. Introduction

This chapter focuses on the two related issues of implementation processes and timetables.

Firstly it summarises the main issues identified in the guidance for governments and government entities on the transition to accruals accounting provided in Study 14 — Transition to the Accrual Basis of Accounting: Guidance for Governments and Government Entities⁷⁶, a study issued by the IPSAS Board itself. It then describes the related work currently being carried out by the IPSAS Board in the context of its first-time adoption project. An overview is then given of views expressed on implementation processes and timetables in the context of the public consultation carried out by Eurostat for assessing IPSAS.

Short overviews are then provided concerning the recent implementation experiences of four countries: Austria, France, Switzerland and the United Kingdom.

Finally, since the cost of the transition from cash to accruals or from non-harmonised accruals to harmonised accruals would be substantial, Eurostat presents information that it has collected on the actual and estimated costs experienced by some Member States and other countries, as well as international organisations.

5.2. Transition to the Accrual Basis of Accounting: Guidance for Governments and Government Entities — IPSASB Study 14

Study 14 is intended to assist public sector entities in the process of adopting or considering the adoption of accruals basis IPSASs. The study is primarily intended to assist public sector entities make the transition from the cash to the accruals basis but it may also be useful for entities currently reporting on an accruals basis or considering the adoption of IPSAS.

Part I of the study addresses general issues associated with the transition to accruals accounting, including factors influencing the nature and speed of the transition, options in respect of the transition paths, and the management of the transition process. It also considers issues associated with the identification, design, and delivery of training.

The following texts are closely based on the explanations provided in Part I of Study 14.

5.2.1. *Transition paths*

The style and speed of the transition to accruals accounting may vary greatly between entities. A wide range of approaches and combinations of approaches are possible.

⁷⁶ <http://www.ifac.org/publications-resources/study-14-transition-accrual-basis-accounting-guidance-governments-and-governm>.

Before considering alternative transition paths it is necessary to have a clear understanding of the gap between the current system of financial reporting and the desired system of financial reporting.

The factors that may influence the nature and speed of the transition to accruals accounting include:

- The system of government and the political environment. Transition times can be significantly different in a developed, transitional or developing country and also in countries with a presidential or parliamentary system.
- Whether the reforms are focused solely on accounting change or whether they encompass other wider scale reforms.
- Whether the changes are being driven from the top down, or bottom up.
- The current basis of accounting used by the entity, the capability of existing information systems, and the completeness and accuracy of existing information, particularly in relation to assets and liabilities.
- Any change to the basis of accounting for budgeting.
- The level of political commitment to the adoption of accruals accounting or harmonised accruals accounting.
- The capacity and skills of the people and organisations responsible for implementing the changes.

The reforms may be applied to all public sector entities within a government, or they may be restricted to certain types of entities. For example, the implementation of accruals accounting may occur on a sector-by-sector basis. It may begin with autonomous and semi-autonomous government entities which already have some responsibility for managing the resources under their control and which are outside the centralised accounting system. Alternatively, the changes may focus first on budget sector entities because such entities make up the core of government activities.

It is possible to design different transition paths for different types or sizes of entities. For example, large entities may be delegated authority to design and oversee the development of their financial information systems, whereas smaller entities may be required to follow a centrally determined transition path, including the implementation of specific financial information systems. For example, many government business enterprises (GBEs) will already use the accruals basis of accounting. The transition path for such GBEs would therefore focus on ensuring consistency of accounting policies and other consolidation issues⁷⁷.

Where a government decides to implement whole-of-government reporting, there are a number of paths it can take. The first accruals whole-of-government reports can be required at the same time as the first accruals reports from individual entities or they

⁷⁷ Under IPSAS GBEs would adopt IFRS requirements.

may be delayed for a period to allow more time to focus on the transition by individual entities, the boundaries of the reporting entity and other consolidation issues. Consolidated accruals reports for various sub-sectors of the whole-of-government reporting entity could be produced as an interim step, followed by complete whole-government reports. Another option would be to prepare a consolidated cash flow statement as an interim step.

Accruals accounting requires the recognition of all assets and liabilities which meet the definition of assets and liabilities and satisfy the criteria for recognition of assets and liabilities. However, this does not preclude an entity from choosing to move to the full accruals basis by recognising assets and liabilities in stages. For example, it is possible to focus first on the recognition of short-term assets and liabilities such as debtors and creditors. Recognition of property, plant and equipment would often occur next, although recognition of property, plant and equipment may occur in stages with those assets that are readily identified and measured being recognised first. Similarly, the recognition of liabilities can occur in a step-by-step manner. Public debt is often recognised first because an entity usually has reasonably accurate records of existing borrowings. Pension and other long-term obligations may be recognised in stages.

5.2.2. Transition period

Usually, the resources available or the extent of political commitment will determine the period over which reforms occur. The length of this period may differ from jurisdiction to jurisdiction. Reform periods may be short (roughly one to three years), medium (roughly four to six years) or long (over six years).

A short reform period may be appropriate where there is strong political support and a limited number of entities. Medium reform periods provide more time for the preparation of detailed implementation plans, the development of accounting policies, and implementation and testing of new systems. They also provide a reasonably long time for the education of groups such as government employees and politicians regarding the changes. In selecting a time frame for the transition, a government may also establish target dates or stages (milestones) for the achievement of various aspects of the reforms. Entities may be required to meet certain criteria by certain dates in order to progress to the next stage of implementation.

5.2.3. Implementation plan

The transition to accruals accounting is a major project for most governments. Like any large-scale project, it requires careful planning and management. Transition is likely to be smoother and faster when the following features are present:

- A clear mandate from the appropriate level of the government stating what the reforms will encompass, the expected timing and the authority of various government bodies to initiate the changes required. Political commitment from both the governing body and the opposing party: because transition may occur over a period of years there may be a change of government or changes within a government during the transition period.

- The commitment of central entities and key officials.
- Adequate resources (human and financial).
- An effective project management structure.
- Adequate technological capacity and information systems.
- The use of legislation to provide formal authority for the changes and demonstrate the strength of the government's commitment to the changes.

The entity in transition needs to develop an implementation plan to enable it to achieve its goals. The key headings for a generic implementation plan that indicates many of the issues that need to be considered and illustrate the size of the project are:

Project initiation

- Document project and obtain project approval
- Establish the steering committee
- Prepare detailed project plan(s)
- Establish project team
 - Project sponsor
 - Project manager
 - Project team (team leader/director and other staff)
 - Identify required resources
 - Obtain required resources

Detailed scoping and planning

- Document existing processes, procedures, and legislative requirements (including existing accounting policies and systems)
- Identify proposed changes or areas of change (including proposed accounting policies and systems)
- Systems planning
 - Identify structure/ownership of proposed systems
 - Identify system requirements (existing and new systems)
 - Identify control requirements

- Identify interfaces required
- Develop the chart of accounts
- Develop interfaces (if applicable)
- Reporting
 - Develop new reporting requirements
- Audit
 - Liaise with external auditor to assess impact of changes on audit process
 - Identify role of internal audit during the change process
- Develop communications plan
- Prepare training strategies (for example, project team, accruals accounting, and computer literacy)
- Develop change management strategy

Implementation phase

- Initiate project management responsibilities and reporting structures
- Implement new systems/system changes
- Implement interfaces
- Develop detailed accounting policies
- Develop/amend supporting financial management policies and procedures
- Implement roles and responsibilities
- Deliver training
- Obtain approval to switch to new systems
- Implement other phased projects (for example, the recognition of specific categories of assets or liabilities may be phased)

Reporting

- Develop improved external and internal reporting
- Develop financial and non-financial performance measures

- Review controls and procedures that support the integrity of financial and non-financial information

5.2.4. *Chart of accounts*

The development of a new chart of accounts is a key step in the adoption of accruals accounting. A well-planned chart of accounts can assist in the efficient generation of financial information for a variety of purposes.

A chart of accounts is a systematic coding system for the classification and coding of transactions and events within the accounting system. It defines the organisation of ledgers used within the accounting system. The types of classifications provided for by a chart of accounts may include economic, functional, administrative, and regional classifications as well as more detailed classifications for cost centres, programmes, projects, outputs, and outcomes.

The chart of accounts is not used solely in the preparation of external financial statements. It may also be used to support the preparation of internal management reports, the preparation of regulatory information and the tracking of expenditure against budgets and the preparation of fiscal reports for the European System of Accounts (ESA) 1995. In order to eliminate the unnecessary reclassification of financial data or duplicating the entry of data, it is helpful if the chart of accounts can support a range of governmental reporting requirements.

Once established, the chart of accounts becomes a fundamental component of the processing of financial information from simple tasks like paying bills to complex activities such as financial reporting. Because it is embedded in the processing activities of the entity, it becomes costly to change. It is therefore essential that the chart of accounts is carefully designed to allow for change and growth and to meet the various reporting needs of the entity.

In a well-designed system, the chart of accounts should incorporate the budget accounts specified in the budget classification. If a government elects to report on the accruals basis of accounting, but budget on a cash (or modified cash) basis, a combined chart of accounts will be more complicated as it will need to be able to generate both reports on both the accruals basis and cash basis of accounting.

Where a number of individual entities are required to provide information to a central entity for the preparation of consolidated financial statements or for other reporting purposes, it is advised to have a central chart of accounts. Especially in a federal setting, where there is no such reporting requirement, a unified chart of accounts can prove helpful in enabling GFS data to be generated in a cost-efficient manner.

Following the development of a new chart of accounts, it is necessary to assign responsibilities for the day-to-day management of the chart of accounts and prevent unauthorised changes. Supporting guidance and monitoring may also be required to ensure consistent use of codes.

5.2.5. *Staff resources and training*

Besides the chart of account, another key element of successful implementation is the adequacy of staff resource levels:

- All personnel — including management — involved in the transition to accruals accounting or harmonised accruals accounting should understand the reasons for the change, be capable of implementing the changes they have responsibility for, operate the new systems and procedures, and understand the information produced.
- Entities need to assess the impact of the changes on the competencies required in relevant positions, and develop a strategy which includes, but is not confined to, training for upgrading skills.
- Options for addressing gaps in competency include recruitment, engagement of consultants, development of external courses, and training for existing staff.
- Separate outreach activities and information materials are required for educating and creating awareness in groups such as politicians and the media.

5.2.6. *Audit requirements*

The accruals-based accounts will also have an impact on public sector audit. The audit of accruals-based financial statements is more complex and causes more judgments to be made by the auditor than the audit of cash-based financial statements. The auditor (whether a private or public sector auditor) should have the relevant public sector and audit knowledge. The application of generally accepted auditing standards is necessary to assure a uniform audit quality. The International Organisation of Supreme Audit Institutions (INTOSAI) provides professional standards and best practice guidelines for supreme audit institutions and quality control procedures in audit bodies may need to be enhanced with the introduction of accruals-based financial statements, as audit judgments become more significant.

5.3. **First-time adoption project of IPSAS Board**

In 2011-2012 the IPSAS Board began developing a further project related to the first-time adoption of accruals IPSASs. The background to the project was that there is no standard that addresses the range of issues arising from first-time adoption of IPSASs, and it was considered that the development of a standard in this area would help in the implementation of accruals IPSASs. In June 2011, the IPSAS Board approved the project brief on the First-Time Adoption of IPSASs.

The scope of this project is to consider issues related to public sector entities that are moving to accruals IPSASs not only from an accruals basis of accounting, but from a cash basis, modified cash basis or partial accruals basis of accounting.

In particular, several IPSASs contain transitional provisions for when they are applied for the first time. Typically, these transitional provisions allow an entity additional time

to meet the full requirements of a specific accruals-based IPSAS or provide relief from certain requirements when initially applying an IPSAS. The transitional provisions govern the length of time available to make the transition and also indicate whether the IPSAS should be applied prospectively or retrospectively. These transitional provisions are the main focus of the project on first-time adoption.

The aim of the IPSAS Board is to approve an Exposure Draft of the new standard for first-time adoption by March 2013.

5.4. Views expressed on process and timetable in the public consultation

Taking into account the importance of this subject and the potential interest of a wide range of stakeholders, and given the potential resource implications of any recommendations on future IPSAS implementation, Eurostat launched a public consultation from 17 February to 11 May 2012. The consultation asked seven questions. All citizens and organisations were welcome to contribute to this consultation.

From the 68 contributions received, 59 respondents expressed views concerning the process and timetable for a possible future implementation of IPSAS in EU Member States.

Overall, the respondents considered that implementing IPSAS would be a medium-term or long-term project, taking into account the scale and the costs.

The majority of responses — especially from the German regional courts of auditors — expected that more than 10 years would be needed for implementation. Another significant portion of respondents thought that it would take 5 to 10 years, of which 3 to 4 years would be spent on legislation and 5 years on technical implementation. A smaller number of respondents considered that 3 to 5 years could or should be enough.

One issue mentioned by several respondents was the need to establish the starting point of each EU Member State. Based on their preparedness, the timescales may differ from Member State to Member State. As probably no ‘one size fits for all’ model for implementation exists, individual implementation plans with milestones need to be developed which would allow progress to be monitored at both national and EU levels. In this context a ‘phased’ approach was proposed whereby standards could be implemented, for example, either sector by sector or beginning with recognition of financial assets and liabilities and covering non-financial later so as to mitigate the impact of implementation.

Several respondents were of the opinion that a Regulation would be more appropriate than a Directive, in order to ensure the timely and consistent implementation of the accounting principles. However, a few respondents would prefer a Directive with a flexible approach and with scope for derogations.

Some of the contributors also emphasised that IPSAS implementation will require substantial staffing resources, new IT infrastructure and educational changes, which would make up the bulk of the expected expenditure.

5.5. Implementation experiences

5.5.1. Country experience — Accounting reform in Austria

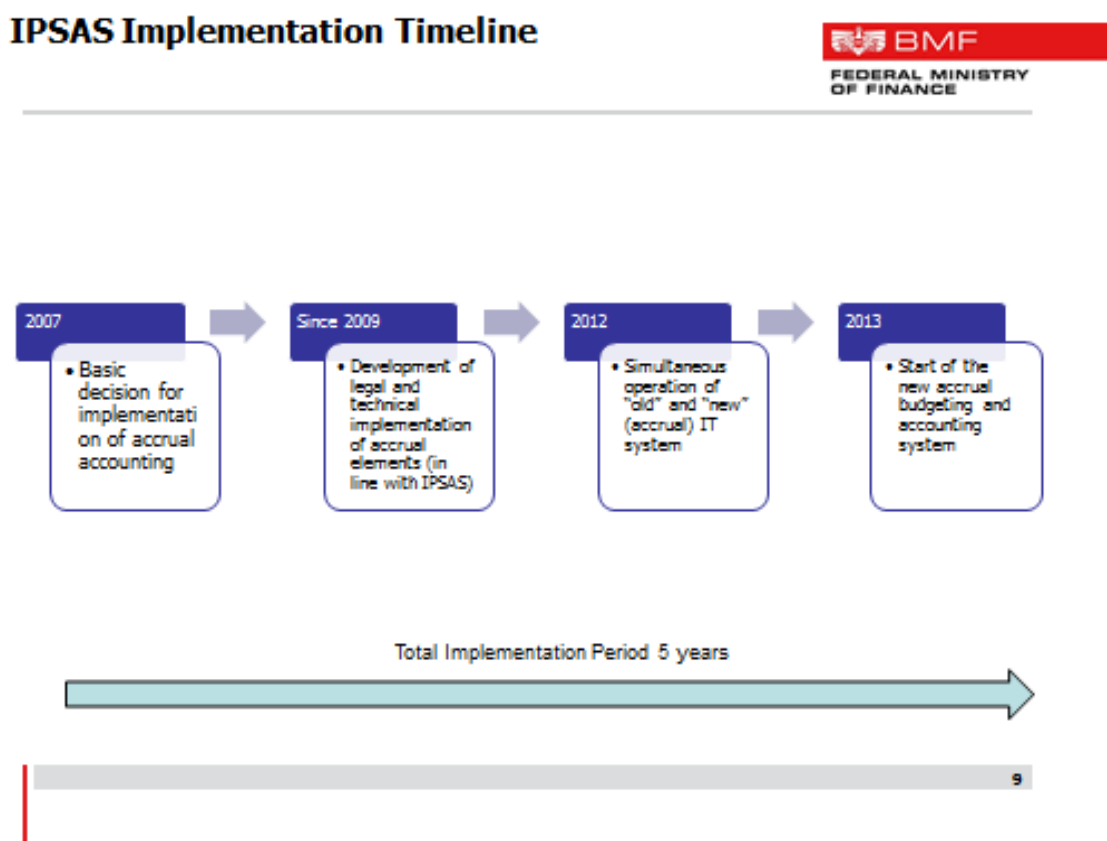
Aim of reform

- Strengthen accountability
- Improve budgetary decision making (more and better information)
- Address weaknesses of current system (input focus, no binding medium term perspective, dominance of annual cash flows)

Austria already had a very developed and comprehensive accounting system. Some accruals elements were already in place (a kind of asset accounting), mainly due to the widespread cost accounting systems of several entities.

The timeline and the process of implementing accruals budgeting and accounting in Austria are illustrated in Figure 5.1.

Figure 5.1: Implementation timeline for Austria



This comprehensive reform is taking place only at federal level, although one state has already decided to implement a very similar reform, and other states are still considering it.

The Austrian budget reform is a very comprehensive approach including a medium-term fiscal framework, new budget structures (lump sum budgets), performance budgeting (with a special focus on gender budgeting), result-oriented management of state bodies and modernisation of the budgeting and accounting system (accruals budgeting and accounting system oriented towards IPSAS).

IPSAS was used as a reference for designing the Austrian federal accounting standards. 87.5% of IPSASs were implemented or would be implemented if applicable (Hyperinflation, Agriculture, Service Concessions, etc.). The area of controlled/owned entities was not implemented in line with IPSAS (no consolidation).

Benefits expected and achieved, costs

Although the first budget compiled and created under the accruals accounting system is currently being discussed in Parliament, several benefits have already become apparent:

- More and better information in the budgeting process (for example depreciation, provisions, etc.) leading to a different discussion in Parliament.
- The view, from start to finish, of the necessary future tasks of certain ministries.
- Accruals accounting supports the identification of future/past spending (back payments and advance payments).

The cost of the overall reform currently amounts to roughly EUR 23 million, because all of the development and implementation tasks, as well as training, were performed by current staff members.

Another aim of the reform was to reduce the efforts needed to transform the data onto an ESA basis. How successfully this aim will be achieved depends on the further development of ESA.

Concerning the implementation of an accruals budgeting and accounting system, two crucial difficulties were encountered: compensating for the lack of accounting know-how in the public sector and ensuring the development of the necessary IT solutions for the reform elements. From the Austrian experience a comprehensive approach uniting all reform forces from all entities under one strategy seems to be the most promising.

5.5.2. *Country experience — Accounting reform in France*

During the first decade of the 21st century, France implemented a comprehensive budgeting and accounting reform. The primary goal for the modernisation of the central government's financial information system was to make government transactions and financial information more transparent, presenting true and fair government accounts to the Parliament and to citizens.

The driver for the French public accounting reform was the Parliament, with the approval of a constitutional by-law known as the LOLF⁷⁸ — the Constitutional By-law of 1 August 2001 on Budget Acts.

With this reform the previous budgetary structure of the central government based on budget chapters was reformed to a structure of missions, programmes and actions⁷⁹ and broken down into public policy objectives and output measures. Greater autonomy and responsibility was given to departments but programme managers, too, became more accountable regarding the use of their appropriations. Continuous accruals-based accounting was introduced. Moreover, the annual set of accruals-based accounts for the central government is audited by the Supreme Court of Auditors.

Concerning the history of public sector accruals accounting development, there are three major milestone periods:

- In the first period, until 1962, modified cash basis accounting with a single entry system was applied by the whole public sector.
- From 1962 to 2005, central government (and, since 1962 with major improvements in the 1990s, for public agencies, local government and social security funds) used modified accruals-based accounting, with double-entry accounting and a chart of accounts (which was different for each of those entities).
- Since 2006, for the central government⁸⁰, accruals-based accounting referring to domestic public accounting standards, with double-entry accounting and a chart of accounts.

In 2001, the LOLF provided for the introduction of accruals-based general government accounts on 1 January 2005, while maintaining the conventional budget presentation in terms of receipts and payments (cash basis which remains the main reference of annual budget acts). The LOLF required the keeping of three independent accounting systems, which should be interconnected: budgetary (cash basis) accounting, financial (accruals basis) accounting and management or costs accounting.

According to Article 27 of the LOLF, the central government must keep accounts of budgetary receipts and expenditures and general purpose accounts for all of its transactions. In addition, it must implement an accounting system designed to analyse the cost of the various actions undertaken as part of its programmes.

Moreover, Article 30 stipulates that these financial statements are based on the accruals accounting principle. Transactions are recognised in the financial year to which they are related, independently of the date of payment or receipt. The same principle is found in the legislation governing business financial statements. Consequently, the constitutional

⁷⁸ Loi organique n° 2001-692 du 1er août 2001 relative aux lois de finances.

⁷⁹ Each mission comprises a set of programmes to which appropriations are allocated and broken down into sub-programmes (actions).

⁸⁰ Local government, social security authorities and public agencies draw up their accounts on an accruals basis using, when it is relevant, rules originating from the standards applicable to the individual financial statements of business undertakings, namely the *plan comptable général*, or general chart of accounts (PCG).

by-law stipulates that the accounting rules for the central government are the same as those for business, except when differences are warranted by the specific nature of the central government's activity⁸¹.

Road map for implementation

For the implementation of the central government⁸² accruals accounting reform, a detailed road map was put in place, with implementation phased over three stages:

- Stage 1 — Building the foundations (Q1 2003)
Structuring the missions, programmes and sub-programmes; Definition of the accounting reference framework — standards and new chart of accounts; Communication plans;
- Stage 2 — Prefiguration (Q3 2003)
Adaptation of the information system; Presentation of appropriations in LOLF format; Definition of performance goals and indicators; Assessment and development of the experiments; Definition of accounting procedures; Planning of training programmes;
- Stage 3 — Implementation (Q3 2004)
Organisational changes and development of internal control; Training; Preparation of the opening balance.

The challenge was overcome in less than five years.

By the end of 2002 the 'Accounting Normalisation Committee' was put in place to organise the continuous building of public accounting standards and a public accounting reference framework. A conceptual public accounting framework and 13 state accounting standards were published in 2004.

The framework and standards are based on private accounting practices — French chart of accounts and accounting rules as primary reference, and IFRS to a lesser extent — but reflect public sector specificities. The framework also refers to IPSAS and entails the development of specific standards and accounting treatments where necessary, for example for taxes and social benefits and recognition, issues that are not addressed by IPSAS.

As a result of the successful implementation plan, the new accounting system was introduced on 1 January 2006 and the accounts for 2006 were provided to the Parliament and certified by the Supreme Court of Audit (*Cour des Comptes*) with some qualifications.

Since 2004 three additional standards have been published and several modifications or additions to the standards (opinions issued by the CNoCP since 2009) have been issued.

⁸¹ Central Government Accounting Standards in France (RNCE — *recueil des normes comptables de l'Etat*) — the conceptual framework for central government accounting.

⁸² Central government accounts do not currently include government-owned public agencies.

Public sector accounting standards

Public sector accounting standards are enacted by the ministry in charge of public accounts (*Ministère de l'économie et des finances*) and other ministries if relevant after receiving an opinion from the Public Sector Accounting Standards Council (*Conseil de normalisation des comptes publics* — CNoCP).

The CNoCP was created in 2008 with the responsibility for expressing an opinion prior to the legal adoption of general accounting rules applicable to central government, local government, social security agencies and private entities financed mainly by public funds and in particular by compulsory levies. The CNOCP is composed of a board, three permanent commissions and an advisory committee for general guidance.

The board is made up of the president of the Council and 18 members (9 ex officio members and 9 technical experts), with representatives from both the public and private sector. The board adopts opinions and recommendations by a majority of members present (providing at least 10 members are present), based on the proposals made by permanent commissions. The three permanent commissions cover: central government and government-controlled organisations; local government and local public agencies, and social security agencies and similar organisations. The permanent commissions are provided with proposals for opinions and recommendations prepared by working groups.

Working groups are set up on each topic to be examined by the board, based on its annual work plan. Each working group is presided over by a technical expert from public or private background and open to all participants. The activity reports and work plan of the CNoCP are available to the public on its internet site⁸³.

5.5.3. Country experience — Accounting reform in Switzerland

The Swiss Confederation is a federal republic consisting of 26 cantons and some 2 500 municipalities in addition to the federal authorities. Switzerland has a strong tradition of decentralised government and autonomy.

In Switzerland, the cantons and local governments have been using a modified accruals accounting model for more than 20 years. The first reforms in the 1970s introduced the Harmonised Accounting Model (HAM), but the first version from 1977 was used by only a few pilot cantons.

The implementation of accruals accounting across all cantons occurred in the 1980s with the Harmonised Accounting Model 1981, following a recommendation by the Cantonal Ministers of Finance. The municipalities followed the cantons, usually with a delay of a few years. The Federal Government considered the Harmonised Accounting Model but, in the 1980s, rejected reforms and stayed on modified cash accounting, with a balance sheet compiled for statistical purposes. HAM 1981 covered both accruals accounting and accruals budgeting. Its key feature was to bring a fully harmonised chart of accounts, but its weakness was that detailed accounting practices were not harmonised. For example, some issues like recognition, measurement and disclosure were not treated.

⁸³ <http://www.economie.gouv.fr/cnocp>.

In the early 2000s, in the light of the growing demands on financial management, the federal level and the cantons of Geneva and Zurich decided to overhaul the Swiss Confederation's accounting system and to introduce the New Accounting Model (NAM) at federal level and HAM2 for the states/cantons. In this new model, the accounting is based on IPSAS and there is an alignment with IPSAS wherever it is considered feasible.

At federal level IPSAS has been directly adopted through references in legislation and the accounting policy and manual are defined by the Federal Finance Administration (FFA). The aim is to eliminate departures from IPSAS over time. The Swiss Federal Finance Administration considers that while some IPSAS standards are more challenging to implement, none is impossible and issues often prove to be non-permanent or organisation-specific. Reasons for departures from IPSAS must be disclosed in financial statements. The new federal accounting model — NAM⁸⁴ was used for the first time for the 2007 budget and the 2008–2010 financial plan.

At cantonal level, projects are most advanced in the cantons of Zurich, Geneva, Basel Stadt, Luzern, Solothurn and Bern. Although these cantons are very much geared to IPSAS they have opted for differing approaches in the development of accounting and statistical systems. At canton and municipality level, HAM2 was drawn up on the instructions of the Conference of the Cantonal Directors of Finance by the Technical Committee for Cantonal Financial Questions (FkF), as a further development of HAM1. Based on IPSAS, and in coordination with the new accounting model of the Confederation, the FkF drew up 20 HAM2 standards, which were approved in January 2008, and the related manual was published with a recommendation to the cantons and municipalities to implement the standards as quickly as possible, i.e. within the next 10 years. Although Swiss cantons and local governments have been using accruals accounting for many years, IPSAS still brings some innovations and is challenging for their accounting systems. The main differences lie in the valuation of assets and liabilities, the consolidation of controlled entities, and disclosures.

The new accounting model is viewed as bringing transparency and comparability, facilitating the job of financial management and helping to generate public confidence. It also brings the accounting standards of public authorities and the private sector closer together, thereby improving comparability. The accounting structure is very close to the model used in the private sector, comprising the Profit and Loss Statement, the Balance Sheet, and the Statement of Investments or Capital Expenditure.

Switzerland's financial statistics system is designed to ensure that government units' data are comparable at national level. One of the main tasks of financial statistics is to disclose the revenue, finance and asset situation of the government units and the structure of their expenditure on a comparable basis. Only by ensuring national comparability is it possible to aggregate the individual federal levels into the general government sector. And only after such aggregation into the general government sector is it possible to view the financial situation of the government units from a macroeconomic perspective. In essence, the statistical system is based on HAM2, and allows analysis of remaining differing accounting practices at the level of individual

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http://www.efv.admin.ch/e/downloads/finanzpolitik_grundlagen/rechnungsmodell/NAM_brochure_e.pdf

government units. The resulting statistics are compiled according to the IMF model and then adapted to the European System of Accounts (ESA 95).

In terms of the basis of consolidation of the federal accounts, the consolidated financial statements include all entities within the group (excluding significant interests⁸⁵) on a full consolidation basis. Assets and liabilities, as well as expenses and revenue are therefore recognised in full.

In the view of the Federal Ministry of Finance, the potential benefit foreseen for Switzerland of implementing a set of harmonised accruals accounting standards in the EU would be to reduce uncertainty, particularly in the financial markets, by means of improved transparency, reliability and comparability of the financial reporting of general government units.

5.5.4. *Country experience — Accounting reform in United Kingdom*⁸⁶

The United Kingdom of Great Britain and Northern Ireland is a unitary state made up of four countries: England, Wales, Scotland and Northern Ireland. The United Kingdom is governed by the UK Parliament and Wales, Scotland and Northern Ireland each have devolved autonomous powers.

Accruals accounting has a long history in some parts of general government in the UK, with the notable exception of central government. Major city councils (e.g. Birmingham, Manchester, Bradford, Cardiff, and Bristol) started to adopt accruals-based accounting from the mid-19th century onwards. Moreover, many of the industries nationalised in the period between 1946 and the early 1950s used accruals and this practice was continued after nationalisation. Accruals became compulsory for all but the smallest local entities under the reorganisation of local government in 1974. In the early 1990s the introduction of an internal market in health led to accruals being adopted by hospitals.

The Public Accounts Committee of the UK Parliament first proposed a system of consolidated accounts for central government in 1990, with the aim of improving accountability and simplifying the government accounts. In 1993 it was announced that resource accounting would be introduced across central government, and a Treasury Green Paper of 1994 on resource accounting proposed moving from cash-based accounts and adopting output and performance indicators. This was followed, in 1995, by a White Paper '*Better Accounting for the Taxpayers' Money*'. The White Paper also proposed the establishment of a Financial Reporting Advisory Board to ensure a high standard of government financial reporting and close compliance with Generally Accepted Accounting Practice (GAAP). Reform was considered necessary in order to achieve comparability across the government sector and with the private sector, and increased transparency and accountability.

The government's 1998 *Economic and Fiscal Strategy Report* also proposed replacing cash-based accounts with accruals for the whole of government. It argued that this

⁸⁵ An extension of the scope for consolidation, including all significant interests, is currently being considered.

⁸⁶ The case of the UK is all the more interesting as it is the only Member State having developed the consolidation of accruals accounts to the level of the whole of government.

would provide better information, consistent across government departments, and would assist macro decision-making and capital planning, as well as providing Parliament with an audited picture of performance and of the financial position.

Legal effect was given to the proposals by the Government Resources and Accounts Act 2000. The introduction of Resource Accounting and Budgeting (RAB) was accomplished in a number of stages, beginning with implementation in all departments in April 1998. Audited resource accounts were published for the financial year 1999/2000, and a public spending review conducted on a resource basis was carried out in 2000. The first full set of resource-based budgets was presented to Parliament for the financial year 2001/02. RAB is an accruals-based accounting framework which aims to convert the Government's policy priorities into departmental strategies and budgets, so that the efficiency and effectiveness of services provided can be reported to Parliament.

A scoping study, *'Whole of Government Accounts'*, was published in 1998 and examined the feasibility of developing a full set of audited accounts covering the whole public sector based on UK GAAP. The study proposed an incremental approach, beginning with a set of consolidated financial statements for central government, and then consolidating other parts of the public sector before deciding whether to move immediately to a consolidation of the whole of the public sector. After several dry run sets of accounts, the first Whole of Government Accounts were published for 2009-2010 in 2011, covering the whole of the UK public sector. WGA consolidate the financial statements of about 1500 entities from central government (including the devolved governments of Wales, Scotland and Northern Ireland), local government, public health services and public corporations.

The National Audit Office, together with the Audit Commission, Audit Scotland, Wales Audit Office, Northern Ireland Audit Office, and private sector firms, have established audit programmes for WGA, covering the consolidation submitted by each entity. The audit opinion on the first 2009/10 WGA was qualified and the auditor's report highlighted several limitations of the published accounts. These included the lateness of publication and the understatement of public assets and liabilities because publicly owned banks, the Bank of England and Network Rail were excluded, and because local government was still on a UK GAAP basis. The Comptroller and Auditor General therefore qualified the audit opinion.

5.6. Cost of adopting accruals accounting as experienced or estimated by countries

One of the main obstacles to the future implementation of IPSASs or other harmonised accruals accounting standards is the high expected cost of implementation. Moreover it can be argued that the ongoing cost of running an accruals-based accounting system would be higher than that of maintaining only a cash-based accounting system.

Costs are strongly influenced by the scale and pace of accruals implementation, the size and complexity of the government sector, and the sophistication of existing systems. Costs will be lower where the extent of the changes required is smaller, and they can be integrated with systems replacement cycles. In practice, the implementation of accruals accounting is often only part of a wider project to modernise government financial and

management information systems, making the separation of costs directly linked only to accruals accounting difficult or impossible.

Eurostat has nevertheless collected information on actual and estimated costs experienced by Member States and some other countries and international organisations, which is annexed to this chapter.

In the Czech Republic, the cost of CZK 2 558.4 million (around EUR 100 million) covers the implementation of the four functional phases of the Integrated Information System. The yearly licence fee for the accountancy IT system is CZK 60 million (around EUR 2.5 million).

In France, the Court of Auditors has estimated the direct and indirect costs of transition to accruals accounting ‘solely’ for the French State (not all French public administrations) to be around EUR 1 500 million over 10 years. This cost covers expenses incurred by the producer of the accounts (in this case the Ministry for the Budget and Public Accounts), information systems (investment and maintenance), training, etc.

In Slovakia, the cost of EUR 21.6 million includes the software, hardware and training of the public employees.

In Denmark, a new ERP system and a reconciliation system were introduced shortly before the decision to move central government accounting to accruals. A few large central government agencies had already moved their accounting to a SAP system. For this reason the move to accruals did not include IT costs. The table below shows both system implementation costs (implementation of the ERP system and the reconciliation system, but not of the SAP implementation) and the costs of introducing accruals accounting. The total cost came to DKK 455 million (around EUR 60 million).

Table 5.1: Breakdown of implementation costs for Danish Central Government (provided by Danish participant of the IPSAS Task Force)⁸⁷

Million DKK	Costs	Total
ERP-system (Navision Stat)		245
Preparation in Ministry of Finance (including software license)	25	
Implementation costs within Ministry of Finance	110	
Implementation costs in Line Ministries	60	
Implementation costs within Ministry of Finance (Upgrade 2004)	10	
Implementation costs in Line Ministries (Upgrade 2004)	40	
Central reconciliation system (SKS)		40
Implementation of Accruals Accounting		170
Preparation and project management within Ministry of Finance	30	

⁸⁷ During 2000-2002 and with a major upgrade in 2004 a new ERP-system was introduced. This was in place before the introduction of accruals accounting. Also in 2004 a new reconciliation system was introduced collecting accounting information from all central government entities. The implementation of accruals accounting was carried out during 2003-2005. The table does not include the costs of implementing a SAP based system in five large central government entities.

Total**455**

The cost of EUR 240 million indicated for Hessen in the annex below only relates to the set-up of the IT system. Other costs, such as training, external consultation fees, the valuation of assets and labour costs are not included.

Box: Overview of the Cost of Government-Wide (state and ministries) Implementation of Accrual Basis Accounting in the Netherlands

Incidental (one-off) costs	Lower Threshold	Upper Threshold
IT systems	€ 30 million	€ 71 million
Personnel	€ 16 million	€ 25 million
Valuation of assets	€ 11 million	€ 22 million
Change process	€ 72 million	€ 143 million
Total implementation	€ 129 million	€ 261 million
Structural costs		
Personnel	€ 6 million	€ 14 million
Maintenance of IT systems	€ 2 million	€ 4 million
Valuation of assets	€ 5 million	€ 11 million
Total structural costs per year	€ 13 million	€ 28 million

In 2010, in the Netherlands following a request made in Parliament, the government produced an analysis which includes an estimation of the cost of introducing accruals accounting across the government.

In Switzerland, for the Federal Government, the cost of implementing the accruals IPSASs was estimated at CHF 65 million (around EUR 38 million) which included the replacement of the Enterprise Resource Planning (ERP) IT system. For larger states/cantons, e.g. Zurich, the cost was approximately CHF 3 million (around EUR 1.75 million) excluding the IT system, which did not need to be replaced. Smaller states/cantons actually made savings as the State of Zurich made its documents available to them.

In conclusion therefore, and as an order of magnitude, and based on the experience of those countries for which data is available, the possible cost for a medium-sized EU country of moving from a cash-based accounting system to an accruals-based accounting system could be up to EUR 50 million, for central government but no other layers of government. This amount would include for example the cost of putting in place new standards and the associated central IT accounting tools, but not costs entailed in a complete reform of the system of financial reporting. For larger Member States, and, for example, for those with autonomous systems of regional government, those with more complex government systems, and those which have made least progress on accruals accounting, the costs could be much higher, especially if the transition to a harmonised accruals system is combined with wider reforms of accounting and financial reporting practices. For example, the cost of the accruals and budgeting reforms in France was very much higher. For a smaller Member State, which already has national systems of accruals accounting in place, the costs might be lower

than EUR 50 million. Taking the estimated costs as a percentage of GDP, all of the cost estimates collected and summarised here fall within the range of 0.02 to 0.1 % of GDP.

ANNEX 5.1: COST OF ACCRUALS IMPLEMENTATION

Body	Year	Costs	Information source	Comments
Czech Republic	2009	CZK 2 558.4 million	http://www.mfcr.cz/cps/rde/xchg/mfcr/xsl/tiskove_zpravy_49192.html?year=2009	CZK 60 million yearly IT licence
Denmark	2003-2005	DKK 455 million	Document provided for IPSAS TF meeting 5/6.07.2012 by the representative from the Danish Agency for Modernisation of Public Administration	
France	2006-2015	EUR 1 500 million	http://www.ccomptes.fr/fr/content/download/1548/15346/version/2/file/P_chorus.pdf	Costs only for the French State budgeting and accruals reform
Slovakia	2005-2008	SKK 651.6 million (EUR 21.6 million)	http://www.nku.gov.sk/documents/10157/22308/456-Sprava+o+vysledku+kontroly+postupov+a+financneho+plnenia+Ministerstva+financii+SR+pri+realizacii+projektu+zavedenia+jednotneho+statneho+uctovnictva+a+vykaznictva+.html.pdf	
Hessen	2000-2004	EUR 240 million	http://www.hessen.de/irj/hessen_Internet?rid=HStK_15/hessen_Internet/nav/dea/dea5072f-a961-6401-e76c-d1505eb31b65.e9d70a4e-3db0-4ef0-b529-618fc951cbc4,,,11111111-2222-3333-4444-100000005004%26_ic_uCon_zentral=e9d70a4e-3db0-4ef0-b529-618fc951cbc4%26overview=true.htm&uid=dea5072f-a961-6401-e76c-d1505eb31b65	Set-up of IT system
Hamburg	2003-2007	EUR 4.6 million	http://www.haushaltssteuerung.de/interview-modernisierung-des-haushalts-und-rechnungswesens-in-hamburg-michael-freytag.html	

Body	Year	Costs	Information source	Comments
Netherlands	Analysis 2010	EUR 129-261 million	http://blog-pfm.imf.org/files/netherlands.pdf	Yearly EUR 13-28 million
Switzerland	2001-2008	EUR 71 million	Visit of Eurostat delegation to Switzerland (9 July 2012)	Only federal government
New Zealand	1987-1992	NZD 170 million	New Zealand Audit Office report, ' <i>Central government management: A new approach</i> ', 1989	All public sector entities, including whole of Government.
Canada	1997-2001	CAD 635 million	http://www.oag-bvg.gc.ca/internet/docs/0101ce.pdf	
Pan American Health Organisation	2006-2010	USD 3.98 million	http://www.paho.org/english/gov/csp/csp27-17-e.pdf	Move from UNSAS to IPSAS
WIPO	2007-2010	SWF 2.02 million	www.wipo.int/edocs/mdocs/govbody/en/a_43/a_43_5.doc	
UNICEF	2008-2013	USD 10.8 million + amount XXX for 2012/2013	http://www.unicef.org/about/execboard/files/IPSAS_for_internet-3Sept.pdf	IPSAS, High Level Project approach
UNFPA	2006-2012	USD 7 million	http://www.unicef.org/about/execboard/files/IPSAS_for_internet-3Sept.pdf	

CHAPTER 6

6. THE NEED FOR HARMONISED STANDARDS AND SUITABILITY OF IPSAS

As explained in Chapter 1, the present staff working document's starting assumption is that the principle of accruals accounting is an indisputable objective for EU public finance accounts. The principle of accruals is already implemented at macro level (ESA 95 is accruals based), and increasingly so at micro level. Chapter 1 extended this objective to harmonised accruals-based public finance standards. This chapter confirms the appropriateness of harmonised accruals-based accounts in the EU and discusses whether IPSASs are suitable to be applied directly as these standards.

6.1. Advantages of harmonised accruals-based public accounting standards

As stated in Chapter 1, what is true for private sector accounting standards, which are harmonised within the EU for listed companies, should be true for government entities. Harmonised accruals-based public sector accounting would provide a firmer basis for understanding the economic position and performance of governments and government entities at all levels. Harmonised standards for public sector accounting would enhance transparency, comparability and cost efficiency and provide the basis for improved governance in the public sector of the EU. It would boost the quality of the macro-accounts. With reference to Article 114 of the Treaty, it would provide the transparency needed for the proper functioning of the internal market in financial services, without which there is a danger that owners of government securities would be entering into transactions without a proper understanding of the level of associated risk.

6.1.1. Policy coordination, advice and surveillance in the EU

The Van Rompuy/Barroso/Juncker/Draghi report *Towards a Genuine Economic and Monetary Union* stresses the need for integrated budgetary and economic policy frameworks and for example states that:

'Sound national budgetary policies are the EMU's cornerstone

The near term priority is to complete and implement the new steps for stronger economic governance. In the past few years, significant improvements to the rules-based framework for fiscal policies in the EMU have been enacted ('Six-Pack') or agreed (Treaty on Stability, Coordination and Governance), with greater focus on prevention of budgetary imbalances, on debt developments, on better enforcement mechanisms, and on national ownership of EU rules. The other elements related to strengthening fiscal governance in the euro area ('Two-Pack'), which are still in the legislative process, should be finalised urgently and be implemented thoroughly. This new governance framework will provide for ample ex ante coordination of annual budgets of euro area Member States and enhance the surveillance of those experiencing financial difficulties. '

Many of the principle objectives advocated in Council Directive 2011/85/EU, such as the greater transparency and accountability of the public sector, as well as more reliable, timely and more comparable fiscal statistics, necessitate a common, harmonised and detailed accounting and reporting tool.

It is moreover fully supportive of the Communication from the Commission *A blueprint for a deep and genuine economic and monetary union — Launching a European Debate*⁸⁸. Using a common accounting tool, the European Parliament and the Council would be in a better position to assess the relationship between the outcome of national budgets and of the budget of the EU.

As seen in Chapter 3, in some Member States, ESA reporting for the government sector depends on basic data taken from cash-based accounts, but, whether the basic data are cash based or accruals based, the accounting standards used are neither harmonised nor comparable across, or within, Member States. For the compilation of macroeconomic statistics on government and with reference to Article 338 of the Treaty, ESA 95 accounts must use sets of estimates and adjustments to approximate accruals, for example for EDP and for the macroeconomic imbalances procedure scoreboard and where entity-level accruals data are not available. The availability of harmonised entity-level audited financial reporting data on an accruals basis would substantially reduce the risk of systematic errors in the data used for the preparation of government finance statistics and therefore in the data used for policymaking. The statistical data needed would be considerably improved if all government entities used harmonised accounting standards. It would allow the use of common bridge tables to compile the entity accounts to produce ESA accounts, which would greatly facilitate the statistical verification processes.

In the longer term, harmonised standards might enable the main EDP indicators to be refined because macro public accounting (deficit/debt) results could be derived from much more direct consolidation of consistent and exhaustive micro accounts. The adoption of an integrated accounting and reporting framework with some adaptations to ESA 95 concepts would make it possible to derive the debt and deficit directly from those systems. They could be based on genuine and harmonised public sector accounting data, which had been subject to control and audit, either directly on the key indicators or indirectly through the financial statements. This could also help reduce the time taken to report the deficit and debt.

At entity level, there would be benefits in terms of transparency and accountability from harmonised accruals accounts, and for the quality of decision-making, which should take into account the full future costs and benefits of decisions on a comparable basis. Moreover, further EU fiscal and budgetary integration highlights the need for harmonised public accounting standards to enable real budgetary decisions applicable at national level to be assessed at EU level. For the purposes of accountability, government entities should report in a complete and comparable manner on their use of public resources and their performance.

There are common benefits

The benefits of having strong and reliable harmonised accruals accounting systems implemented in fellow Member States — for the transparency and functioning of the markets, and for surveillance and policy advice — would therefore be shared by all EU countries. The adoption of harmonised accruals accounting systems in any Member State should be of indirect value to its fellow Member States.

The present financial crisis has demonstrated that the need to assure financial stability is common to all EU countries. Government intervention in response to the crisis places a new importance on assessing long-term effects, including the effects on financial stability, and requires more transparency, improved reporting and stronger accountability.

⁸⁸ COM(2012) 777 final.

Introducing common accounting standards, and high-quality financial reporting and transparency, would contribute to ensuring the financial stability of the Member States by providing assurance that the accounts present a complete and comparable view of the financial position and performance of national governments — improving international acceptance and legitimacy. Harmonised and widely used international accounting standards can reinforce confidence.

The need for harmonisation is supported by many stakeholders.

6.1.2. *Views on harmonised public accounting standards*

International Monetary Fund (IMF)

The IMF is of the opinion that fiscal transparency⁸⁹ is instrumental for the achievement of macroeconomic stability, and it encourages countries to adhere to high standards⁹⁰. The IMF supports developments that may lead to improvements in the accuracy of timely fiscal reports prepared in accordance with internationally accepted standards. Such improvements facilitate work on surveillance and policy advice. Once IPSASs fully become a stable platform for public sector accounting, the implementation of their principles will enhance transparency, comparability, cost efficiency and provide a basis for improved governance in the public sector.

Directorate-General for Economic and Financial Affairs of the European Commission

The Economic and Financial Affairs DG fully shares the views of the IMF that an internationally accepted accruals-based accounting standard would significantly improve the transparency of fiscal policy, whether this was IPSAS or any other ‘emerging’ international standard such as EPSAS.

European Central Bank (ECB)

The ECB fully agrees with the IMF on the importance of implementing internationally accepted public accounting standards with a view to increased fiscal transparency. In this respect the ECB has stated that:

‘The Directive [2011/85/EU] may contribute to simultaneous enhancement of the timeliness and reliability of general government accounts by supporting the implementation of public accounting systems on an accruals basis that are interconnected with ESA 95 based national accounts. The accounting systems should be based on internationally accepted public sector accounting standards to ensure the harmonised recognition and measurement of government transactions.’⁹¹

⁸⁹ IMF Policy Paper — ‘[Fiscal Transparency, Accountability, and Risk](#)’, 7 August 2012. It is argued that fiscal transparency is a critical element of effective fiscal policymaking and the management of fiscal risks. The authors observe that understanding of the underlying fiscal position of a government and the risks to that position remains inadequate. Fiscal transparency is needed to address the shortcomings in standards and practices revealed by the crisis and to guard against a resurgence of fiscal opacity in the face of growing pressures on government finances.

⁹⁰ [Code of Good Practices on Fiscal Transparency \(2007\)](#).

⁹¹ [Opinion of the European Central Bank of 16 February 2011 on economic governance reform in the European Union \(CON/2011/13\)](#).

European Security and Markets Authority (ESMA)⁹²

The financial crisis underlines the importance of timely and reliable financial and fiscal data and evidences the consequences of insufficient financial reporting in the public sector. Some governments were forced over the last years to play an important role in the efforts to restore stability in the financial sector through bailouts, takeovers and guarantees which are likely to result in new liabilities and other obligations. To allow investors in sovereign debt to understand these new liabilities and obligations, they need to be properly reflected in governments' financial reports.

ESMA supports a single set of high-quality and up-to-date public sector accounting standards for EU Member States and the European Institutions. In particular, it believes that accruals-based public accounting would provide a firmer base to understand the economic position and performance of governments at all levels. There is an increasing demand and need for public accountability and transparency on the financial position and performance of governments and ESMA considers that introducing a single set of public sector accounting standards would contribute to a better functioning of the internal market by ensuring a high level of transparency and comparability of government financial reporting which is a necessary condition for building an integrated capital market which operates effectively, smoothly and efficiently. Investors in government securities can currently not rely on a comparable level of transparency as provided by IFRS for listed companies. Introducing a single set of public accounting standards would reinforce the freedom of movement of capital in the internal market and help investors to compare the financial activities of governments and by consequence permit Member States to compete on an equal footing for financial resources available in the Union markets, as well as in the world capital markets.

European Court of Auditors (ECA)⁹³

As a matter of principle, the Court is in favour of the preparation of public accounts (of government and other public entities) according to commonly acceptable and harmonised accrual-based accounting standards throughout the EU, including the EU accounts, as this provides much needed comparability of public accounts within the EU.

IPSAS provide that financial reporting is primarily based on accrual-based accounting¹. In its Annual Report 2005 the Court mentioned that the principal significance of accrual based accounting is that it shifts the focus of the accounts from the recording of cash transactions to the recognition of the 'rights and obligations' as soon as these are acknowledged.

The principal benefit of harmonised accrual-based accounting is that it provides a fuller and more accurate reflection of the financial status and performance of the entity. Cash based accounting systems in the public sector do not give an insight into the current state of assets, finances and revenue (true and fair view). This makes it difficult for the users of the information to assess the financial position.

⁹² [Reply by ESMA to the public consultation on the suitability of IPSAS.](#)

⁹³ It is important to recall that the Court is charged with examining the accounts of all revenue and expenditure of the Union's budget. While the Court has an interest in the accounting standards that will apply to the financial statements of EU Member States and the policy governing the public finances of the EU, the audit of the accounts of Member States is, outside the field of competence of the Court and, as such, it would be inappropriate for the Court to comment with authority on these issues.

The auditing perspective

Article 3 of Council Directive 2011/85/EU states that:

‘As concerns national systems of public accounting, Member States shall have in place public accounting systems comprehensively and consistently covering all sub-sectors of general government and containing the information needed to generate accruals data with a view to preparing data based on the ESA 95 standard. Those public accounting systems shall be subject to internal control and independent audits.’

The use of a harmonised accruals accounting system across all Member States would offer the potential for more efficient and effective auditing. For example, shared audit strategies, procedures and techniques could be developed, and knowledge and experience shared.

The value gained from harmonised accruals-based financial statements is increased when these are subject to independent audit, which adds to transparency and public trust in government. Independent audits help identify instances of poor financial reporting, and thereby contribute to increasing the quality of publicly available information.

From the perspective of government finance statistics and EDP, the knowledge that the accounting systems for all public sector entities in all EU Member States have been subject to external audit, based on common audit strategies, procedures and techniques, would go far to provide the necessary assurance that these data were of the required quality.

6.2. Advantages and disadvantages of IPSASs as the harmonised standards

In order to gather information for this staff working document, Eurostat launched a public consultation in the first half of 2012 to seek the opinion of the widest range of stakeholders, and established a Task Force comprising experts and practitioners from the Member States to share their views and experience.

The following provides a non-exhaustive summary of many of the views provided within the public consultation as regards the appropriateness of harmonised public sector accounting standards such as IPSASs⁹⁴. All of the replies to the public consultation, and a summary report, can be found at: http://epp.eurostat.ec.europa.eu/portal/page/portal/public_consultations/consultations/ipsas.

6.2.1. Advantages of harmonised standards such as IPSAS

- The evolving sovereign debt crisis has demonstrated that there is an urgent need for change in the way public sector financial information is collected and presented in Europe. For the monetary union to function properly it is necessary to have high quality and comparable information about balance sheet items (especially liabilities) and the true annual costs for items that do not currently require cash resources (such as public sector pension obligations) for all Member States. The costs of not acting and thus not having reliable financial information available for internal decision-making and the potentially protracted loss of the markets’ and investors’ trust as a

⁹⁴ The views of those who remain unpersuaded by the case for the principle of accruals accounting in the public sector, whether harmonised or not, have already been covered in Chapter 1, and are not repeated here.

result could be very large. The benefits would still outweigh costs in the medium and long term.

- Implementation of IPSAS in EU Member States would provide a uniform accounting framework and accounting standards for determining deficit and debt levels that would enhance the consistency, transparency and comparability of public sector financial statements. This would help to prevent a situation where negative performance, in breach of the Stability and Growth Pact, was concealed in order to avoid an excessive deficit procedure. Whether full implementation of IPSAS is necessary to achieve this remains unclear.
- An accruals basis such as that of IPSAS would provide a more meaningful picture of a government's financial position and performance, thus reducing uncertainty for ratings agencies and other users of financial statements. The room for misrepresentation of financial positions and performance (i.e. by making payments in subsequent years) becomes narrower. It would enhance stewardship and financial management by identifying entities' assets and liabilities, facilitating a long-term perspective in financial management by identifying current liabilities that will need to be met in future (e.g. borrowings, guarantees, pension liabilities, social contribution, etc.), and better facilitate inter-generational fairness by identifying assets and liabilities. The recognition, measurement and reporting of liabilities, especially those of a long-term and uncertain nature, would be the main advantage of any future implementation of IPSAS in the EU Member States.
- Financial accounting and statistical accounting should be aligned (common chart of accounts, elimination of differences in terms of recognition, valuation, presentation, consolidation, etc.). Data generated by government accruals accounting systems such as IPSAS can be used as a basis for the preparation of GFS, which are crucial to fiscal and spending decisions in most jurisdictions. The European System of Accounts (ESA 95), as a statistical framework using the accruals basis, requires the systematic gathering and processing of accruals-based data. The availability of audited financial reporting data on an accruals basis would substantially reduce the risk of systematic errors in the data used for the preparation of GFS and therefore in data used for policy making.
- The transparency provided by high-quality accruals standards such as IPSASs also provides for better-informed capital markets, in which government financial activity plays a much greater role than is often acknowledged. Better-informed markets are less likely to experience major fluctuations because more reliable information is available.
- Experience with IPSAS would increase know-how and provide the incentive to modernise internal control systems and external audits. Accounting officers will have a source to which they can refer for detailed information on correct accounting treatment. The use of IPSAS would provide a solid foundation and suitable criteria upon which auditors could base their work.
- Although the adoption of IPSAS should not drive the implementation of better financial management, it is a necessary condition for it. This would be an indirect, but important, benefit of the adoption of IPSAS.

- The EU-wide application of IPSAS would foster mobility of accounting expertise and resources across the EU, since, over time, the transfer of personnel and expertise between Member States for both public sector accounting and auditing would be enhanced if common standards were applicable throughout the EU.
- A single set of public accounting standards such as IPSAS would reinforce the free movement of capital in the internal market and help investors to compare the financial activities of governments and consequently permit Member States to compete on an equal footing for financial resources available both in EU markets and in world capital markets.

6.2.2. *Specificities of IPSAS*

While these points show the importance of harmonised accruals-based standards in the EU, the question is then: which harmonised standards?

IPSAS is currently the only internationally recognised set of public sector accounting standards. The standards are founded on the international financial reporting standards (IFRS), which are widely applied by the private sector. The main advantage of the current set of IPSASs, as described in Chapter 2, is that it constitutes a formidable body of existing, harmonised, accruals-based standards for implementation by the public sector.

The 32 existing accruals IPSASs represent more than 15 years' collective work. Each one of them has been drafted and adopted through a well-established process, by a board of well-qualified and independent experts with a wide range of expertise from a variety of institutional and geographical backgrounds. An important advantage is that IPSAS is conceived as a world standard, and not limited to one specific geographic zone.

Indeed, a significant number of responses and exchanges showed support for IPSAS as the candidate for harmonised standards in the EU. However, some difficulties with the current state of IPSAS development and with specific IPSASs emerged during both the public consultation and the meetings of the Eurostat Task Force. Overall, one can conclude that, although there is general support for the use of IPSAS as a reference for EU harmonised public sector accounting standards, there is a need to adapt them if they are to be used on a compulsory basis in the EU.

The following section summarises the issues seen as difficult or problematic with IPSAS. It is based on the Commission interpretation of the contributions of a group of experts and practitioners from the Member States in a dedicated Eurostat Task Force.

The Task Force was set up to share experiences and analyses and discuss perspectives regarding the current state of play of public sector accounting and auditing practices in Member States, and the adoption and implementation of IPSAS or accruals-based public sector accounting standards. The Task Force comprised experts from more than half of the Member States, from national statistical institutes, ministries of finance, national accountancy bodies, and courts of audit, and from several Commission DGs (the Economic and Financial Affairs, Internal Market and Services, and Budget DGs), and observers from the IPSAS Board and IMF.

The main issues which emerged from the discussions in the Task Force are listed below. Participants expressed their views in the Task Force as independent experts, rather than as

representatives of their governments⁹⁵. It should also be noted that an issue may have been included in this list because one or more experts expressed a concern about a particular aspect of the standard, and it does not necessarily mean that other experts agreed. The concerns presented below should therefore not lead one to conclude that there was a general rejection of IPSAS. On the contrary, during the discussions in the Task Force, many experts expressed the view that the current IPSAS set of standards remains an irreplaceable reference for harmonised public sector accounting in the Member States (see box). The key word is therefore ‘adaptation’ and not ‘rejection’. It should also be noted that some concerns are already being addressed by the IPSAS Board and therefore what is the case now may not be so in a few years’ time.

Alternatives to IPSAS?

Since the process of setting IPSAS is anyway designed to adapt IFRS for public sector specific issues, it would not seem appropriate to use IFRS, but not IPSAS, as a source for harmonised public sector accounting standards.

As shown in Chapter 3, many EU countries, when they decided to implement accruals accounting for government, decided to establish their own specific national standards for government accounting. In part this reflects the fact that the IPSASs either did not exist some years ago or were far less complete than they are today. However, there can also be other reasons. For example they built their own public standards based on their own specific private sector accounting standards – national GAAPs. In doing so, they effectively give priority to the consistency of the national public and private standards.

It would not be possible to use the ESA itself as the basis for micro accrual accounts. The ESA may use accrual principles, but it is not sufficiently detailed, so for example the rules for valuation are not sufficiently developed and there is no guidance useful for day-to-day accounting.

Concerns can be classified into: (a) concerns regarding the standard themselves, (b) concerns regarding the governance of the standards.

(a) Concerns regarding the standard themselves, as discussed in the Task Force:

- There is a need for an agreed and complete conceptual framework for IPSAS. Such a conceptual framework, setting out the core principles for the accounting system, is needed to underpin the design of standards reflecting the specific characteristics of the public sector, including the volume and financial significance of non-exchange transactions, the importance of the budget, the nature of plant, property and equipment, and the longevity and regulatory role of governments. The IPSAS Board began a project to develop such a framework in 2008, and the project is due for completion in 2014.
- At the time of writing, it can be argued that the process of translating IFRS principles into IPSASs, and the reference to the IASB framework in the absence of a complete and specific IPSAS conceptual framework, does not take sufficient account of the specific needs and interests of public sector reporting, such as those related to the specific characteristics underlined in the above

⁹⁵ Meetings were held on: 27 February, 26 April, 5-6 July and 7 November 2012.

point. IPSAS is a principles-based set of standards. To apply the standards in practice, more detailed and specific harmonised interpretations are needed, as is the case for IFRSs, for which IFRIC is the system established to provide 'Interpretations' and implementation guidance. Presently, in IPSAS, although 'Application Guidance' is normally included in the standard to show how the core principles of a standard are to be applied in dealing with specific items and transactions, this may not always be sufficiently detailed. There is currently no interpretation function for IPSAS.

- The set of IPSASs could be regarded as incomplete, in that for some standards that have been adopted for private sector accounting (e.g. exploration for and evaluation of mineral resources, accounting and reporting by retirement benefit plans) no counterpart IPSAS has been developed. Furthermore, in the case of financial instruments it may be argued that the IPSAS standard due to enter into force in 2013 is in practice already obsolete, in that the equivalent IFRS rules applicable in the EU have been adapted since the standards were first formulated but the IPSAS standards have not.
- Some existing IPSAS standards, at their current stage of development, are viewed as incomplete, in particular concerning the recognition, measurement and disclosure of specific transactions such as social benefits and taxes and the accounting and measurement of specific items such as public debt (obligations) and heritage assets. For example, under IPSAS the notion of accruals is perceived as insufficiently developed for taxation, which is a key obstacle to the comparable application of IPSAS. For social benefits there is a need for a specific IPSAS standard, for which there would be no IFRS equivalent, and this has not been developed.
- The scope of consolidation and the criteria for control under IPSAS lead to the inclusion of the results of all the controlled entities in reporting entity statements, which would imply the consolidation of public corporations. This would require a potentially large number of government-controlled entities to provide timely and accurate financial data in a suitable format for consolidation, when they may use IFRS as in the case of some government business enterprises (GBEs). GBEs' financial statements prepared under IFRS might use, for example, accounting policies that differ from those applied by the controlling government and that do not include the necessary disclosures.
- IPSAS standards are applicable to all types and sizes of government entities, and this may be excessively burdensome for small and less complex entities. If the costs of applying IPSAS for small government entities are too high in relation to the expected benefits it could lead to unharmonised or lower quality compilation approaches, and at this stage there is no relief for those entities in IPSAS from the application of certain or all the requirements envisaged.
- Some IPSAS standards offer options, which may lead to a lack of comparability. In such cases it would be necessary to remove these options (i.e.

for the valuation of assets, the recognition of interests, and the presentation of income statement⁹⁶).

- In some circumstances, IPSASs allow entities to choose between fair value and historic cost as the measurement basis for non-financial assets, notably for the valuation of property, plant and equipment⁹⁷. As already mentioned, offering options reduces comparability between entities; although preparers of GPFS may voluntarily achieve the necessary harmonisation by consistently choosing the same accounting policy. On the other hand, where the ‘fair value’ measurement basis forms part of the IPSAS standards, this is considered less suitable for public sector financial statements by some experts; particularly regarding the annual impairment of non-financial assets. Moreover, it can be argued that the fair value basis is not applicable for those government assets that are not marketable. The initial recognition at fair value of financial instruments acquired by government requires comparable judgments in practice, to ensure comparability and avoid any scope for accounting misstatements or manipulation.
- The rules on disclosure required under several IPSASs are perceived as too demanding (such as for financial instruments), although the concept of materiality also applies to specific disclosure requirements in an IPSAS⁹⁸.
- Although IPSAS has a specific standard on the presentation of budgetary comparisons, for entities which make public their budget, some experts nevertheless consider that IPSAS is not sufficiently developed concerning the specific presentation requirements of the relationships between budget and financial reporting. This is especially the case where the budget and financial statement are not prepared on a comparable basis and the entity elects to include a comparison of actual and budget amount in its financial statement.
- There is a risk of producing too much information which could make it harder for users to locate relevant information. There should be better linkage between IPSAS and the production of statistical (ESA) data. Requiring governments to prepare both statistical information in accordance with ESA and financial statements in accordance with IPSAS potentially involves duplication. Despite attempts at convergence some differences remain. It is therefore important that any unnecessary differences between IPSAS and ESA be eliminated.

(b) Concerns regarding the governance of the standards

- IPSAS standards are issued by a private sector entity. For the most part, EU government organisations are engaged neither in the standard-setting process nor in the oversight of the IPSAS Board. By making IPSAS mandatory for all EU Member States, standard-setting powers would be delegated from Member

⁹⁶ For example, for the valuation of assets both historical cost and fair value are allowed; for income statement presentation a choice is allowed between two forms of analysis: nature of expense or function of expense; for borrowing costs two methods are also allowed: recognition as expense in the period in which they are incurred, or capitalisation as part of the cost of the asset (if eligible under the standard conditions).

⁹⁷ For statistical reporting, note that the value of an asset is its current market value. See Chapter 4.

⁹⁸ See IPSAS 1.47.

States to the IPSAS Board. It would be essential for public authorities to be involved in the process of drafting and issuing such standards and the governance structure of the IPSAS Board would therefore need to be adapted and/or a specific new structure be created.

- There would need to be a thorough assessment of the quality and applicability of the standards. Such assessment requires experts in the field of public sector accounting. Consequently there would be a need to set up a separate institution whose primary tasks would be to carry out such technical assessment and advice on the possible adoption of particular IPSASs. It would be necessary to provide sufficient financial support for such an institution to carry out its tasks properly.
- It would not be advisable to decide on IPSAS implementation before the process of developing a full set of consistent standards based on the conceptual framework is finalised. The conceptual framework is due for completion in 2014 and there is a high probability that, following its completion, existing standards will need to be modified.
- The IPSAS Board has relatively limited resources which may limit its capacity for dealing with multiple developments simultaneously. This could be a risk to the implementation of IPSAS should gaps in the IPSAS framework be identified which cannot be quickly dealt with.

Many of these concerns about the suitability of IPSAS for implementation in the EU Member States were also echoed within individual contributions provided to the public consultation.

Annex 6.1 summarises the detailed specific issues mentioned by some Member States, IPSAS by IPSAS. Furthermore, Annex 7.1 classifies IPSASs into three categories, taking into account the views of Member State experts: (1) standards that could be adapted with minor or no adaptation; (2) standards that need adaptation or for which a selective approach would be needed; (3) standards seen as needing to be amended for implementation.

6.2.3. *IPSAS governance and resources*

It is clear from the public consultation and the discussions held with the Task Force that the expertise and skills of the IPSAS Board and staff are widely respected. There are, however, concerns that IPSAS governance arrangements are not currently adequate and that the resources available for developing IPSASs are not sufficient. Chapter 2 described IPSAS Board processes, membership, staffing and funding levels, and the EU governance process for adopting IFRS standards are described in the annex to this chapter. As described above some contributors express strong concerns with IPSAS governance.

The IPSAS governance arrangements are under the authority of the International Federation of Accountants (IFAC). IFAC appoints the members of the IPSAS Board. IPSAS is therefore not fully within the institutional control of government authorities; in 2013 half of the board members will be from government authorities and the remainder from other institutions⁹⁹. Moreover in practice the IPSAS Board can be seen as operating without sufficient organised

⁹⁹ Note, however, that from 2014 the nomination process for the IPSAS Board will be more open, so that members may be nominated by a wider range of bodies, for example governments and international organisations.

involvement from EU public authorities. For example, responses to IPSAS Board consultations from EU public authorities are in practice infrequent, with a few exceptions, and most Member States do not contribute. In contrast to the position with respect to private sector accounting standards, there is at present no IPSAS oversight body.

During 2012 the governance framework of IPSAS was placed under review, with a view to ensuring that the independence of the standard-setting process is strengthened, while public-sector-specific needs are effectively addressed. The IFAC Monitoring Group has launched a public consultation on whether the existing Public Interest Oversight Board should act as the supervisory body. However, this, if implemented, is not seen as sufficient in itself to overcome the concerns expressed by Member States.

IPSAS does not have sufficient resources at present to ensure that it can meet with the necessary speed and flexibility the demand for new standards and guidance on issues emerging in response to the evolving fiscal climate, particularly in the wake of the crisis. For example, the staffing level available for developing IPSASs is around 10% of that in place for work on developing and maintaining IFRS standards. The IPSAS Board recognises the resource issue and has been actively seeking additional sources of funding. It also recognises the constraints on its activities, as explained in its recent Consultation Paper on the Board's 2013/14 work programme.

This situation highlights the need for the creation of an EU governance structure, with strong representation of EU public accounting authorities.

6.3. Benefits and costs of implementing IPSAS or other harmonised accruals accounting standards

6.3.1. Benefits of modernising financial information and accounting systems

It should be borne in mind that, despite the fact that accruals accounting is a more elaborated system than pure cash accounting, the multitude of different accounting standards, charts of accounts, booking processes, and IT systems, as well as auditing standards and practices that often co-exist, even within one sub-sector of general government of a single Member State, suggests that harmonisation will achieve a degree of reduction in bureaucracy and costs which in the medium to long term may offset or outweigh the expected investment. Furthermore, the real and important expected financial costs may be balanced against the potential benefits.

In practice, quantifying and valuing the potential benefits from future implementation of IPSAS seems to be impossible. The implementation of harmonised accruals accounting standards by entities at present accounting on a cash basis, or the transition from national accruals standards to harmonised standards, may often require the modernisation of financial information and accounting systems across large parts of government, providing an opportunity to build a more effective administration and reduce ongoing costs.

The occasional paper¹⁰⁰ of the Public Sector Committee of IFAC relating to the New Zealand experience on accruals accounting implementation confirms that:

‘Indeed, one of the advantages of accruals accounting systems is that activities such as commitments or purchase order systems, payroll, fixed assets, creditors and debtors are able to be integrated into one system, thereby reducing double

¹⁰⁰ <http://www.ifac.org/sites/default/files/publications/files/no-1-implementation-accr.pdf>

processing and reconciliation problems associated with disparate systems. The time savings this brings about can be major.

Despite these changes few government department finance functions grew in terms of total staff complements. There was, however, a significant upgrading in financial expertise as compliance officers were replaced with professional staff capable of negotiating budgets and marketing financial information. The Treasury was able to make reductions in staff responsible for routine accounting functions, from six large regional Treasury offices to a complement of just six staff.

An implication of the new environment has been that the central accounting system was modularised into individual accounting systems. This has greatly assisted departmental flexibility as it ensures not only that accounting systems do not fall behind leading technology but that they can continue to meet changing needs as departmental activities change. One department can now take advantage of new system features of particular value to its organisation without reference to the rest of the bureaucracy. Where a new system requires a capital injection by the owner (most in fact are funded from within the departments' own balance sheets) then the owner will seek to ensure that the development aligns with its and the department's objectives, and that the investment is appropriately managed to ensure cost effectiveness in the long run.'

One of the expected benefits might also be felt in financial (value) terms — that of providing the transparency needed for the proper functioning of markets. It might be expected that there would be a lower yield (risk premium) on Member States' government securities if internationally harmonised accruals accounting standards were applied. The savings in interest payable could then be considered against the costs of implementation. In practice, however, it does not seem possible to measure the effect separately from the many other factors which may influence interest rates.

6.3.2. Costs of modernising financial information and accounting systems

Against the potential benefits must be set the expected costs of implementing IPSAS or EPSAS in the EU Member States. As shown in Chapter 5, the costs of implementing accruals-based accounting standards are very significant, based on the information made available by countries which have moved to accruals accounting. Taking the estimated costs as a percentage of GDP, all of the cost estimates collected fall within the range of 0.02%-0.1% of GDP. Ongoing costs of running an IPSAS accounting system could also be significant. Moreover, the implementation of harmonised accruals accounting for the Member States would also have significant resource implications for the European Commission.

6.4. Conclusions concerning the IPSAS standards, governance and resources

6.4.1. The IPSAS standards

IPSAS is currently the only internationally recognised set of public sector accounting standards. IPSAS stems from the idea that modern public sector management, in line with the principles of economy, effectiveness and efficiency, depends on management information systems that provide timely, accurate and reliable information of the financial and economic position and performance of a government, as would be the case with any other type of

economic entity. At present, 15 Member States have some links to IPSAS in their national government accounting standards. Of these, nine have national standards based on or orientated by IPSAS, and five make some reference to IPSAS. However, even when recognising the value of the IPSAS standards, no EU Member State has implemented them in full.

Taking into account the views of Member States' authorities, and others put forward in the IPSAS public consultation and the Eurostat Task Force, the global conclusion is twofold.

On the one hand, it seems that, at its current stage of development, IPSAS could not be simply and directly implemented in all Member States. More specifically, from the perspective of the Member States, there are concerns that currently the IPSAS standards do not describe the accounting practices to be followed with sufficient precision; the suite of standards is not complete — either in terms of coverage or practical applicability to some types of government flows, such as taxes and social benefits — even if ongoing work should lead to significant improvements. Furthermore, some IPSAS standards offer the possibility of choosing between a set of alternative accounting treatments, which would limit harmonisation in practice. Some standards are either considered to be unnecessary or not applicable for EU purposes, and IPSAS is viewed as unstable, in the sense that once ongoing work on the IPSAS conceptual framework is completed it can be expected that some standards will need to be revised.

On the other hand, most stakeholders agree that IPSAS would be suitable as a reference framework for the future development of a set of European public sector accounting standards, referred to in the following discussion as 'EPSAS'.

6.4.2. IPSAS governance and resources

Even if there is an undeniable need for harmonised public accounting standards, IPSAS is, at its present state of development, not governed in an appropriate manner to make it suitable for direct adoption throughout the EU. IPSAS should therefore be a strong support, but not a constraint, for future European public sector accounting standards.

The reference framework for EPSAS should also seek to use the experience and expertise of national public sector accounting governance structures where possible.

ANNEX 6.1: DETAILED COMMENTS ON THE SUBSTANCE OF CERTAIN IPSASs

The main issues which emerged from the discussions in the Eurostat Task Force are listed below. Task Force participants expressed their views as independent experts, rather than as representatives of their governments. Note, too, an issue may be included in this list only because one expert expressed a concern about some aspect of the standard. This does not necessarily mean that other experts agreed with that concern.

IPSAS 1 (Presentation of financial statements) — Issues are associated with the requirement for the comparison of budget and actual amounts the entity makes publicly available its approved budget. A disclosure issue is associated with the inclusion in minimum line items of information on minority and residual interests.

IPSAS 2 (Cash flow statement) — The issue relates to the options offered by this standard: it allows entities to use either a direct or an indirect method of determining cash flow from operating activities, although it encourages use of the direct method; this may result in variations in reporting by entities.

IPSAS 3 (Accounting policies, changes in accounting estimates and errors) — The date of reporting and retrospective correction for fundamental errors could be unsuitable for some countries/entities. IPSAS 3 requires judgment to be used when determining an accounting policy for a transaction to which no specific IPSAS applies. There is as yet no public sector conceptual framework to guide this judgment.

IPSAS 5 (Borrowing costs) — A transitional issue for cash-based systems occurs if the option to capitalise the cost of borrowing as part of the cost of qualifying assets is taken and retrospective application is required in First Time Adoption.

IPSAS 6 (Consolidated and separate financial statements) — The scope of consolidation and the control criteria under IPSAS lead to the inclusion of the results of all controlled entities in reporting entity statements, which would entail the consolidation of public corporations. This would require a potentially large number of government-controlled entities to provide timely and accurate financial data in a suitable format for consolidation, when they may use IFRS (as GBEs do).

IPSAS 8 (Interests in joint ventures) — Some experts considered that it would be appropriate to modify the equity approach to use the book value of equity/net assets rather than applying the fair value model. In addition, an option issue was highlighted for this standard: it allows both proportional and equity consolidation methods, although IPSAS 8 does not recommend using equity accounting for joint ventures.

IPSAS 11 (Construction contracts) — This standard refers to the case of a public sector entity performing construction work under a binding arrangement; for that reason the standard was considered not material for some countries. Under the standard construction contract, work in progress is accounted for using the 'percentage of completion' method. The method is seen as problematic because it involves:

- (a) Estimating the outcome of the contract reliably;
- (b) Determining the revenue and costs attributable to the stage of completion of the contract; and
- (c) Determining the profit attributable to the stage of completion.

These estimates involve a high degree of judgment and in most cases require a cost analysis which may need a dedicated system to track costs.

IPSAS 12 (Inventories) — The application of the standard requiring inventories to be measured at the lower of cost and net realisable value on an item-by-item or group basis, and the recognition of any losses incurred, could be problematic for some items, for example in accounting for strategic stockpiles.

IPSAS 13 (Leases) — Leases are classified as either finance leases or operating leases. Some participants believe that this assessment is difficult to undertake. Transitional issues for cash-based systems arise for financial leases where the lessee is required to recognise a liability (and an asset) in respect of the leased asset. The IASB currently proposes to revise the treatment of leasing in IFRS, with potential consequences for the standard.

IPSAS 16 (Investment property) — The standard is seen as not material for some countries. Separation of investment properties from other long-term assets is perceived as subjective. Transitional issues arise for cash-based systems.

IPSAS 17 (Property, plant and equipment) — The recognition and measurement of assets (notably for military or heritage assets) may require a substantial amount of work, depending on the extent to which an entity already has information available on them. This standard allows two methods: the cost method or the revaluation method; irrespective of the method, the asset should be depreciated. Recognition and accounting of heritage assets is only optional. The recognition and valuation of immovable property would be a long and difficult process. It requires consumption of economic benefit to be estimated against impairment loss. On that basis IPSAS 17 is seen as problematic for the accounting and measurement of public infrastructure. Specific issues arise for accounting of impairment and for use of the component method for measurement.

IPSAS 18 (Segment reporting) — Geographical segment reporting could be problematic for some countries, if the standard is interpreted in this way. Allocating assets and liabilities to various segments is seen as too complicated. Segment reporting is not based on market/non-market activities. The standard does not mention the segmentation of government revenue or central government debt.

IPSAS 19 (Provisions, contingent liabilities and contingent assets) — For provisions which do not become payable for a significant length of time, the effect of the time value of money may be material. In that case, the amount of the provision recorded in the statement of financial position should be the present value of the expenditure expected to be required to settle the obligation. A discount (market) rate will need to be determined, which may be difficult in particular for long-lived provisions such as nuclear decommissioning. The choice of the discount rate can have a significant

impact on the amount of the reported provision. The standard's requirement to also include provisions (net of recoveries) for onerous contracts is seen as problematic.

IPSAS 20 (Related party disclosures) — The required disclosures are perceived as too demanding: for some countries, implementation of this standard would require reporting tools and a time-consuming detailed analysis of the disclosures involved.

IPSAS 21 (Impairment of non-cash-generating assets) — The systematic classification of cash/non-cash generating assets required by the standard is perceived as subjective; in addition, the related assets could be used by public entities for both market and non-market activities, and the standard is therefore difficult to implement. The standard requires impairment to be determined on an annual basis, which is seen as problematic. There is a transitional issue for cash-based systems.

IPSAS 22 (Disclosure of financial information about the general government sector) — The disclosure requirement is perceived as too demanding. The standard applies only if a General Government entity elects to provide information at a consolidated level. The standard provides an exception to IPSAS 6: the requirements of IPSAS 6 are not applied in respect of the relationships of GGS with entities in the public corporation sectors. The standard is currently not applied in any jurisdiction.

IPSAS 23 (Revenue from non-exchange transactions) — Issues relating to accounting for non-exchange revenues include classification, determining recognition points, measurement at initial recognition, and determining the appropriate treatment of conditions attached to grants. This standard is seen as problematic with regard to the definition of the accruals basis for initial points of recognition of revenue related to taxes. In particular, the definition of the accruals criteria as proposed (when the taxable event occurs and the asset recognition criteria are met) is seen as problematic with regard in particular those entities using the time-adjusted cash method for taxes in government finance statistics. Additional difficulties to those highlighted in the discussion above arise for some countries because the criteria for recognition of taxes are defined for the statement of financial position and not the statement of financial performance. Furthermore, the term 'asset' is used instead of 'tax revenues' when discussing the recognition of non-exchange transactions involving taxes. IT implementation issues are perceived as relevant due to the greater complexity of record keeping. The distinction criteria for conditions and restrictions for accounting of grants are also perceived as difficult.

IPSAS 24 (Presentation of budget information in financial statements) — The standard requires comparison with the approved budget and with actual amounts. However, the budget framework is usually different and this may pose implementation difficulties. In particular, some entities adopt the accruals basis of accounting for financial statements but draft the budget under a cash basis.

IPSAS 25 (Employee benefits) — The difficult areas are pensions and, to a lesser extent, other long-term benefits such as long-service leave. Accounting for short-term employee benefits is not generally problematic. This standard is seen as incomplete because it does not cover the accounting and recognition of employee retirement benefit plans. Moreover, the standard does not deal with accounting and recognition of private sector post-employment benefits managed by the general

social security system. The standard requires calculation of the amount of long-term post-employment benefits (unfunded liability for defined contribution plans and the total liability for defined benefit plans). In that case, the entity should use an actuarial assessment to discount the value of the future amount. In particular, actuarial assumptions to determine the cost of providing post-employment benefits include an assumption on the discount rate that is seen as a difficult issue. However, although IPSAS 25 requires the use of (complicated) actuarial techniques (and data collection), it does not require that a qualified actuary be used. It also requires accounting for any constructive obligation that arises from the entity's informal practices of paying employee benefits, and that is seen difficult. The standard is seen as problematic to apply, in view of the current common country practice of accounting for such commitments as off-balance sheet liabilities (at best, disclosed in the notes to the financial statements).

IPSAS 26 (Impairment of cash-generating assets) — The standard is seen as difficult because it requires calculation of impairment on an annual basis. There is a transitional issue for cash-based systems.

IPSAS 27 (Agriculture) — This standard is seen as difficult to implement because of a lack of systems to record this activity. The standard is not seen as material for some countries. It does not deal with the accounting treatment of land or intangible assets related to agricultural activity.

IPSAS 28 to 30 (Financial instruments) — These standards are seen as not sufficiently adapted to public sector characteristics. In particular, the classification of financial assets required by this standard is seen as not suitable for some countries. The standard is seen as problematic for some countries which currently use a nominal value basis, whereas the standard calls for measurement after initial recognition at amortised cost using the effective interest method for loans and receivables and held-to-maturity investments. Accounting for financial instruments on a fair value basis on initial recognition is also considered complex because entities need to apply judgment in determining the market value of similar instruments with the same term, currency and risk profile, on the transaction date. Accounting for financial derivatives is also seen problematic because IPSASs 28 to 30 call for recognition at fair value. Hedge accounting as proposed by the standard is seen as problematic not only in terms of the complexity of accounting treatment, but also in terms of its impact on the statement of financial position and the statement of financial performance. In addition, macro hedging is not recognised by the standard. Transitional issues are highlighted for cash-based systems. Accounting treatment is seen as relying too much on management intention.

ANNEX 6.2: EXPERIENCE OF ADOPTING IFRS IN THE EU

Where governments decide to adopt accruals accounting, a crucial decision has to be made about how the accounting standards should be developed and their application monitored. In addition to Member States' governments, there would be value in giving a significant role to the accounting profession as 'independent experts' on accounting standards.

The Commission already has experience with governance structures linked to the adoption of International Financial Reporting Standards (IFRSs) in the EU. Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards (the 'IAS Regulation') requires publicly traded companies to present their consolidated accounts in conformity with international accounting standards.

The history of IFRS in the EU

Prior to the adoption of the IAS Regulation, the EU examined the possibilities of improving the financial reporting framework for EU companies for several years. In 1995, the Commission adopted a new strategy: in a communication on accounting harmonisation,¹⁰¹ it proposed to associate the EU with the efforts made by the IASC (International Accounting Standards Committee) and IOSCO (International Organisation of Securities Commissions) towards a broader international harmonisation of accounting standards.

Based on that strategy, seven Member States (Austria, Belgium, Germany, France, Finland, Italy, and Luxembourg) allowed listed companies to prepare their consolidated financial statements in accordance with either IAS (International Accounting Standards) or US GAAP (Generally Agreed Accounting Principles). The strategy was updated in 2000: it was necessary to move towards a single set of accounting standards in order to build a unified capital and financial services market by 2005.

Subsequently in 2000, the Commission introduced a legislative proposal requiring all listed EU companies to prepare their consolidated financial statements in accordance with IAS at the latest in 2005. This resulted in the adoption of the IAS Regulation in 2002.

Ten years have passed since then. Considering the time elapsed and the international context of accounting convergence, it is time to assess the functioning of the current system of IFRS in the EU. Therefore, in 2012 a debate was initiated at political level (ECOFIN) in order to identify potential improvements to the current system and the related governance arrangements. An evaluation of the IAS Regulation is to be launched in 2013.

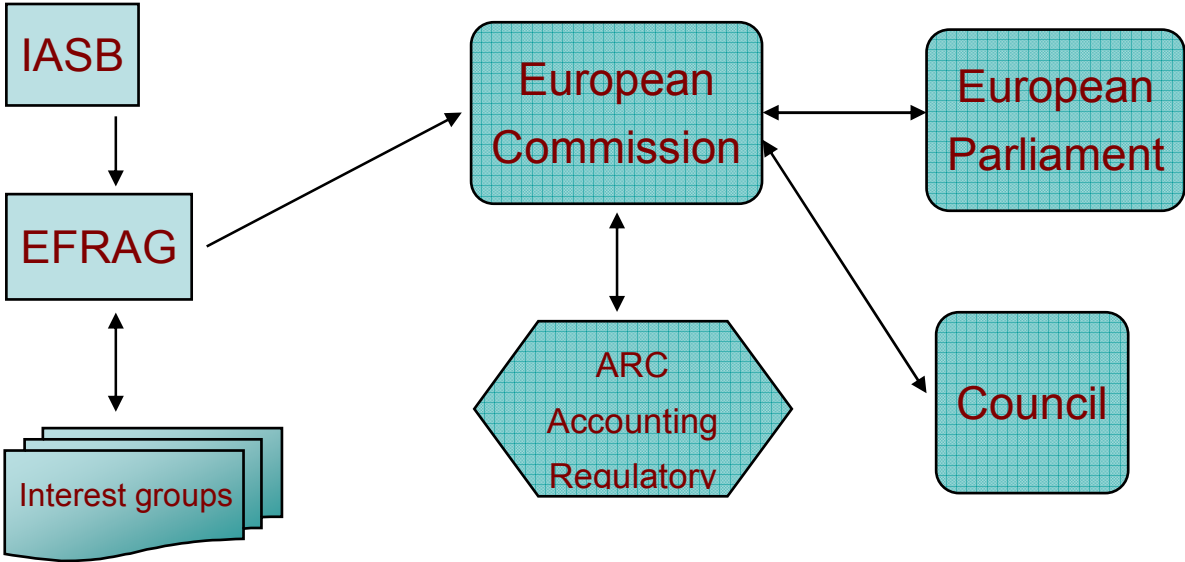
The current governance related to the adoption of IFRSs

The objective is to adopt and use international accounting standards in the EU with a view to harmonising the financial information presented by companies so as to ensure a high degree of transparency and comparability of financial statements and hence ensure that the EU's capital market and the single market work efficiently. This entails greater convergence of the accounting standards currently used internationally, with the ultimate objective of achieving a single set of global accounting standards.

¹⁰¹ [Communication from the Commission, Accounting harmonisation: A new strategy vis-à-vis international harmonisation, COM\(95\) 508 final.](#)

Any IFRS to be adopted in the EU must be consistent with the true and fair view set out in the Accounting Directive, be conducive to the European public good and meet basic criteria as to the quality of information required for financial statements to serve users.

The EU's IFRS endorsement process



In brief, the procedure for adopting EU standards is the following:

- (10) International Accounting Standards Board (IASB) issues a standard
- (11) European Financial Reporting Advisory Group (EFRAG) holds consultations
- (12) EFRAG gives endorsement advice and an effects study
- (13) Commission drafts endorsement regulation
- (14) Accounting Regulatory Committee (ARC) votes and gives an opinion
- (15) European Parliament and Council scrutiny period
- (16) Commission adopts and publishes the standard in the Official Journal

This process typically takes approximately eight months.

The International Financial Reporting Standards (IFRS) are developed by the International Accounting Standards Board (IASB). The IASB is more and more regularly conducting ex-ante field-testing and post-implementation reviews. Interpretations of IFRSs are issued by the IFRS Interpretations Committee (IFRIC), another body under the IFRS Foundation’s umbrella. The Commission participates in the IASB agenda consultation and provides funding (an operating grant) to the International Financial Reporting Standards Foundation (IFRS Foundation) to guarantee stable funding and to increase its actual and perceived independence.

The Commission also supported the establishment of the Monitoring Board to enhance the accountability of the IFRS Foundation and one of the Commissioners is a member of this

Board¹⁰². The Monitoring Board is an independent body, with no legal personality, separate from the IFRS Foundation and governed by its own Charter. Its relationship with the IFRS Foundation is set out in a bilateral Memorandum of Understanding. The Monitoring Board's aim is to ensure that the IFRS Foundation is accountable to public authorities responsible for setting statutory accounting standards. Its principal powers and responsibilities are:

- to participate in the nomination of Trustees and to approve their appointment;
- to review the Trustees' oversight of the IASB's work; and
- to assess the adequacy of the IFRS Foundation's funding arrangements with a view to promoting a non-voluntary, transparent and stable funding platform.

The Monitoring Board may also refer matters of broad public interest to the IASB for consideration on a 'comply or explain' basis.

The Monitoring Board meets two or three times a year.

The European Financial Reporting Advisory Group (EFRAG) is a private sector body. Its core decision-making body on technical matters (the Technical Expert Group, TEG) consists of experts from issuers, accounting professionals, academics and investors. It assists the European Commission with the endorsement of IFRSs and IFRS interpretations by providing endorsement advice and effects studies on technical quality. National standard setting bodies contribute to EFRAG's work and resources. EFRAG attends various IASB Working Group meetings as an observer. EFRAG delivers the input on behalf of the EU to the IASB. The European Commission also supports EFRAG financially and is represented as an observer in EFRAG TEG meetings.

The Accounting Regulatory Committee (ARC) is composed of representatives from each Member State and chaired by the European Commission. The Committee was set up by the Commission as a regulatory comitology committee providing opinions on Commission proposals to adopt an international accounting standard. EFRAG is usually invited as an observer to the Committee's meetings.

There is also a role in this process for the European Securities and Markets Authority (ESMA). ESMA is an independent EU authority that contributes to safeguarding the stability of the European Union's financial system by ensuring the integrity, transparency, efficiency and orderly functioning of securities markets, and enhancing investor protection. In this context ESMA — together with the national supervisory authorities — is responsible for the enforcement of IFRSs.

¹⁰² Currently represented on the Monitoring Board are the Emerging Markets and Technical Committees of the International Organisation of Securities Commissions (IOSCO), the European Commission, the Financial Services Agency of Japan (JFSA), and US Securities and Exchange Commission (SEC). The Basel Committee on Banking Supervision attends Monitoring Board meetings as an observer. The membership is under review with a view to expanding it.

ANNEX 6.3: ADOPTION PROCESS FOR ACCOUNTING RULES APPLICABLE TO EU INSTITUTIONS AND BODIES

The accounting rules applicable to the EU Institutions and bodies are based on IPSAS. The legal basis is Article 143 of EU Financial Regulation stipulating that the accounting officer of the Commission shall adopt rules based on internationally accepted accounting standards for the public sector. The adoption process is as follows:

Elaboration of the draft accounting rules

The draft accounting rules are elaborated by the Commission's accounting officer's services, considering the existing accounting transactions of the Commission, institutions or agencies. The accounting rules applicable to the EU institutions and bodies are drafted based on existing IPSAS and where necessary adjusted to the specific environment of the EU.

In case there are no existing IPSAS standards for specific and important accounting transactions, the Commission may develop its own accounting rules. This is the case for example for the accounting rule for pre-financing without having a counterpart in the IPSAS standards.

Advisory group on accounting rules

Article 152 of the EU Financial Regulation states that the Commission's accounting officer adopts the accounting rules to be applied by all the institutions and EU bodies. The Commission's accounting officer should have a major role in the development of accounting rules. However, other users of the accounts should also play a part in the setting of these requirements.

To this end, an advisory group on accounting rules has been set up. Its role is to:

deliver an independent professional judgement on the accounting standards and rules proposed by the Commission's accounting officer; and

advise the accounting officer on the application of financial reporting principles and standards.

Inter-service consultation of the other EU institutions and bodies

They may give comments on the proposed rules, eventually also highlighting specificities relevant for their accounting environment.

Adoption of the accounting rules applicable for the EU Institutions and bodies,

The adoption of accounting rules applicable for the EU Institutions and bodies is stipulated in Article 152 of the EU Financial Regulation: The accounting officer shall, after consulting the accounting officers of the other institutions and bodies, adopt the accounting rules. When adopting these rules the Commission's accounting officer shall be guided by the internationally accepted accounting standards for the public sector but may diverge from them in order to give a true and fair view of the assets and liabilities, charges, income and cash flow.

The current set of accounting rules applicable for the EU Institutions and bodies with links to IPSAS standards, as at August 2012, is annexed to this chapter. Beside these rules there are two additional accounting rules which do not have an IPSAS counterpart:

accounting rule 3: Expenses and payables

accounting rule 5: Pre-financing

**ANNEX 6.4: LIST OF IPSASs AND RELATED ACCOUNTING RULES APPLICABLE
TO EU INSTITUTIONS AND BODIES**

IPSAS No	Title	EU equivalent rule
1	Presentation of Financial Statements	2
2	Cash Flow Statements	2
3	Accounting Policies, Changes in Accounting Estimates and Errors	14
4	The Effects of Changes in Foreign Exchange Rates	13
5	Borrowing Costs	N/A
6	Consolidated Financial Statements and Accounting for Controlled Entities	1
7	Accounting for Investments in Associates	1
8	Financial Reporting of Interests in Joint Ventures	1
9	Revenue from Exchange Transactions	4
10	Financial Reporting in Hyperinflationary Economies	N/A
11	Construction Contracts	N/A
12	Inventories	9
13	Leases	8
14	Events After the Reporting Date	Not yet developed
16	Investment Property	N/A
17	Property, Plant and Equipment	7
18	Segment Reporting	2
19	Provisions, Contingent Liabilities and Contingent Assets	10
20	Related Party Disclosures	15
21	Impairment of Non-Cash generating Assets	18
22	Disclosure of Financial Information About the General Government Sector	Not yet developed
23	Revenue from Non-Exchange Transactions (Taxes and	17

IPSAS No	Title	EU equivalent rule
	Transfers)	
24	Presentation of Budget Information in Financial Statements	16
25	Employee Benefits	12
26	Impairment of Cash-Generating Assets	18
27	Agriculture	N/A
28	Financial Instruments: Presentation	11
29	Financial Instruments: Recognition and Measurement	11
30	Financial Instruments: Disclosures	11
31	Intangible Assets	6
32	Service concession arrangements: Grantor	N/A

CHAPTER 7

7. HOW TO MOVE TOWARDS IMPLEMENTING EPSAS?

7.1. European Public Sector Accounting Standards — EPSAS

If IPSAS, as it currently stands, is not considered suitable for full and direct adoption throughout the EU, the need to harmonise government accounting standards in the EU calls for the development of a set of European Public Sector Accounting Standards — EPSAS.

EPSAS would give the EU the capacity to develop its own standards to meet its own requirements and with the rapidity required. It would consist of a set of harmonised accruals-based public sector accounting standards adapted to the specific requirements of EU Member States. Standards that could be implemented in practice, and should focus on where they are most needed. The implementation of EU-wide EPSAS would also dramatically reduce the complexity of statistical compilation processes used to transform these data onto a quasi-harmonised basis and minimise risks with regard to the reliability of the data notified by Member States.

As seen with the example of New Zealand's experience described in Chapter 6, the harmonisation of diverse accounting practices which currently co-exist within many of the Member States may even produce cost reductions deriving from the reduced bureaucracy to offset or outweigh the cost of the investment.

7.2. Governance of a future EPSAS

There would need to be strong EU governance for the development and adoption of the EPSAS standards. The system to develop and govern EPSAS would define the agenda for the development of each standard and there would need to be well-defined endorsement procedures. The EPSAS governance structure would need to cover the necessary tasks: legislation, standard setting, and providing technical and accounting advice.

The EPSAS governance structure would not follow the same model used by the Commission for EU governance of IFRS because of the particularities of the public sector and the emphasis on intra-EU comparability. Wherever possible, it should seek to use the experience and expertise of national public sector accounting governance structures in the Member States.

EPSAS would need to establish and maintain close links to the IPSAS Board in order to inform its agenda and decision-making and because EPSAS standards may need to differ in some cases from IPSAS standards.

7.3. A process and a timetable towards EPSAS

The first version of EPSAS could be based on the adoption of a subset of IPSASs consisting of those standards commonly agreed by EU Member States, subject to any necessary adaptations.

However, it should be noted that the definition of a set of EPSASs would not in itself guarantee timely and high quality public accounting data. The benefits require additional conditions to be met, such as:

- Strong political support and joint ownership of the project;
- Public administrations capable of running a more complex accounting system in each individual public entity;
- Integrated IT systems for budget, payment, contract management, double-entry bookkeeping, invoice management, and statistical reporting;
- Timely reporting of all economic events in the integrated accounting system of the public entities (e.g. monthly);
- Availability of human resources and modern IT;
- Effective internal control and external financial audit of public accounting.

For all Member States, but especially for those that currently use only cash accounting, the implementation of EPSAS accruals accounting would be a major reform. Some of the issues that would arise are:

- Conceptual and technical accounting issues;
- Staff and consultant expertise, training skills;
- Communicating with and educating managers and decision-makers;
- Liaison with, and training of, auditors;
- Adjustment or modernisation of IT systems;
- Adapting the existing national regulatory frameworks.

The development, endorsement and implementation of EPSAS would have to be a gradual process, which would take place over a medium-term perspective, by first focusing on the accounting issues which are most important for harmonisation, such as revenue and expenditure — taxes and social benefits — , liabilities and financial assets, and at a later stage considering non-financial assets, etc. For example, as long as cultural heritage assets are not used in production processes, or are not purchased for resale, it may be considered that they do not need to be recognised and valued.

The way forward should take a selective approach, taking into account in particular the perspective of small and medium-sized entities and the issue of materiality. The strategy would need to define priorities, set key deadlines and thus put forward a concrete road map and describe milestones for the EPSAS project, taking into account impact assessment considerations.

The Commission, in cooperation with Member States, would draft an agreed core of basic European Public Sector Accounting Principles and specify the EPSAS governance system and the procedure for developing specific standards.

The first step could be a proposal for a Framework Regulation, requiring the application of the accruals principle in public accounting.

The EPSAS standard setting body could then classify the 32 accruals IPSAS standards into three categories:

- standards that might be implemented with minor or no adaptation;
- standards that need adaptation, or for which a selective approach is needed;
- standards that are seen as needing to be amended for implementation.

This categorisation is further elaborated in the Annex to this Chapter, ‘Possible classification of the IPSAS standards’.

Based on the experience of countries which have implemented accruals-based public sector accounting systems in recent years, the process of implementation should be sequenced. The process should be determined by carefully considering the starting position of each Member State, for example the state of development of their existing national accounting standards and the availability of balance sheet data. In some Member States it might be most appropriate to begin implementation at national level and then follow this at regional and local levels. It should also be envisaged to limit the extent of implementation for smaller entities, or at least prioritise the more important entities, taking into account their materiality.

The process could take place in three distinct stages:

- (17) A preparatory stage to gather further information and to develop a roadmap based on further consultations, and to prepare detailed proposals.
- (18) A stage to develop and put in place the practical arrangements, addressing issues such as finance, governance, possible synergies, and the concerns of smaller government entities. This stage would include the development of the Framework Regulation.
- (19) The implementation stage.

ANNEX 7.1: A POSSIBLE CLASSIFICATION OF THE IPSAS STANDARDS

Taking into account that a number of accounting-related technical issues are seen as problematic in the IPSAS standards, as described in Chapter 6, the IPSAS standards might be grouped as follows:

Standards that might be implemented with minor or no adaptation;

Standards that need adaptation, or for which a selective approach is needed;

Standards that are seen as needing to be amended for implementation.

Eurostat drafted the proposed groups taking into account the views of Member State experts in the Task Force on IPSAS. Note that experts' views on the suitability of some IPSAS standards may differ and therefore this proposal is preliminary and that needs further technical discussion with accounting experts. Note, too, that these proposals refer to the applicability of the standards themselves, and not their consistency with ESA.

Standards that might be implemented with minor or no adaptation	Standards that need adaptation, or for which a selective approach is needed	Standards that are seen as needing to be amended for implementation
IPSAS 1 — Presentation FS ¹⁰³	IPSAS 7 — Investments in associates	IPSAS 6 — Consolidated financial statements
IPSAS 2 — Cash flow	IPSAS 8 — Interests in joint ventures	IPSAS 28 — Financial instruments: Presentation ¹¹¹
IPSAS 3 — Fundamental errors and changes in accounting policies ¹⁰⁴	IPSAS 13 — Leases	IPSAS 29 — Financial instruments: Recognition and measurement ¹¹²
IPSAS 4 — Changes in foreign exchange rates	IPSAS 15 — Financial instruments: Presentation ¹⁰⁸	IPSAS 30 — Financial instruments: Disclosure ¹¹³
IPSAS 5 — Borrowing costs	IPSAS 17 — Property, plant and equipment	
IPSAS 9 — Revenue from exchange transactions	IPSAS 18 — Segment reporting	
IPSAS 10 — Hyperinflationary economies ¹⁰⁵	IPSAS 20 — Related party disclosures	

¹⁰³ Although experts perceive some disclosure issues as relevant.

¹⁰⁴ Experts point to a lack of guidance on determining accounting policy in the absence of a specific IPSAS.

¹⁰⁵ Not relevant in the EU context.

¹⁰⁶ Determining a discount (market) rate to apply in calculating the present value of the provision is perceived as difficult, notably with regard to long-lived provisions (e.g. nuclear decommissioning).

Standards that might be implemented with minor or no adaptation	Standards that need adaptation, or for which a selective approach is needed	Standards that are seen as needing to be amended for implementation
<p>IPSAS 11 — Construction contracts</p> <p>IPSAS 12 — Inventories</p> <p>IPSAS 14 — Events after the reporting date</p> <p>IPSAS 16 — Investment property</p> <p>IPSAS 19 — Provisions, contingent liabilities, contingent assets¹⁰⁶</p> <p>IPSAS 27 — Agriculture¹⁰⁷</p> <p>IPSAS 32 — Service concessions</p>	<p>IPSAS 21 — Impairment of non-cash-generating assets</p> <p>IPSAS 22 — Disclosure general government sector</p> <p>IPSAS 23 — Revenue from non-exchange transactions¹⁰⁹</p> <p>IPSAS 24 — Presentation of budget information</p> <p>IPSAS 25 — Employee benefits¹¹⁰</p> <p>IPSAS 26 — Impairment of cash-generating assets</p> <p>IPSAS 31 — Intangible assets</p>	

¹⁰⁷ Not seen as material for some countries. There is a lack of guidance on the accounting treatment of land or other intangible assets related to the activity.

¹⁰⁸ To be withdrawn — see Chapter 2.

¹⁰⁹ Recognition of revenue related to taxes, accounting for grants according to distinction criteria for conditions and restrictions and IT issues are all perceived as relevant by some countries.

¹¹⁰ The difficult areas are pensions, and to a lesser extent, other long-term benefits such as long-service leave, which represent a large problematic part of the standard.

¹¹¹ However, since IPSAS 28 deals with presentation it may be seen as less problematic than IPSASs 29 and 30.

¹¹² Accounting for financial instruments on a fair value basis on initial recognition is considered to be complex and problematic for some countries which currently use a nominal value basis even for measurement after initial recognition; specific areas considered problematic are hedge accounting, macro hedging and recognition at fair value for financial derivatives.

¹¹³ Disclosure issue is considered relevant by some countries.