

AccountancyAge

Governments told to grasp nettle on accrual accounting

by Richard Crump

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URGENT AND FUNDAMENTAL reforms must be made to inconsistent and unreliable public sector accounting which threatens the sustainability of public finances around the world, according the CEO of the global federation for the accountancy profession.

Speaking to *Accountancy Age*, Faye Choudhury, CEO of IFAC [pictured], says governments have failed to address deficiencies in public sector cash-based accounting that were exposed by the sovereign debt crisis.

Faye believes that governments must ditch the flawed model of public sector cash-based

accounting and adopt accrual accounting and budgeting to better measure and manage fiscal positions.

Private sector companies raising funds from investors on the capital markets are required to provide audited, accruals-based, financial statements, yet too many governments - even ones with bonds on the capital markets - don't follow the same practice. In fact, many do not even use accrual accounting.

The problem, Choudhury explains, is that cash accounting doesn't provide a "comprehensive, comparable or transparent" picture of governments' true financial health.

"It doesn't take into account long-term obligations," Choudhury says. "The sovereign debt crisis revealed the shortcomings of governments' fiscal positions." Choudhury adds that cash-based accounting "contributed" to financial problems in Greece and Portugal, which involved concealing debts and deficits.

It has now been over a year since the G-20 finance ministers and central banks governors' meeting in Moscow declared a "goal of strengthening the public sector balance sheet" and of "looking at transparency and comparability of public sector reporting, and monitoring the impact of financial sector vulnerabilities on public debt".

Indeed, IFAC sent a letter the G-20's finance ministers back in April 2012 that recommended that the world's leading nations "actively encourage" the adoption of accrual accounting. Nevertheless, little action has taken place and political will appears lacking. "Too much transparency is not a good thing...some outcomes are politically uncomfortable," Choudhury says.

Such inaction has led to the "odd situation" where governments require private sector companies to adhere to a strict set of rules, whereas governments' own accounting bodies make up the rules as they wish, Choudhury says.

Choudhury is encouraged, however, by several initiatives that are currently underway; in particular, strengthening the current governance arrangements of the International Public Sector Accounting Standards Board (IPSASB) will improve the credibility of public sector accounting standards and their influence on public sector financial reporting.

"There is much more that needs to be done," Choudhury says, adding that the the G-20 has a "key role" to play in ensuring that governments recognise the benefits of enhancing financial management and reporting.

To promote greater adoption of IPSASs, Choudhury believes that these standards should be added to the Financial Stability Board's list of standards that are designated as deserving of priority implementation.

Furthermore, as part of its key strategic focus IFAC will continue to promote the need for enhanced public sector reporting and financial management through its recently launched Accountability Now! initiative, which aims to promote awareness of the issue, facilitate guidance on implementation of IPSASs, and encourage the development of needed technical capacity.

"We have designed an awareness building campaign working in partnership with civil society organisations, parliamentarians, public accounts committees, development banks and the International Monetary Fund," he says.

European shortcomings

Shortcomings in accounting, reporting and financial reporting within much of the public sector were also recently highlighted in [a joint ICAEW-PwC report](#), which warned the sustainability of public finances in many European countries are being put at risk. Indeed, government accounting standards and arrangements remain extremely diverse in Europe.

Similarly, IFAC's and CIPFA's report, [International Framework: Good Governance in the Public Sector](#), was released last week to address how strong management and processes influenced outcomes within public entities.

According to Eurostat, which is leading a project to develop European Public Sector Accounting Standards (EPSAS), taking into account all tiers and branches of government and the public sector across EU member states, no two countries currently have the same system or apply the same standards.

"The ongoing debate in the EU over which path to take to harmonise public sector accounting standards...needs to focus ultimately on information needed to improve decision-making," says Martin Manuzi, ICAEW's regional director for Europe.

The report suggests that although introducing accruals accounting throughout the public sector in Europe is important, it is not an end in itself. It also calls for an improvement in the financial literacy of citizens, policy-makers, and intermediaries.

"Accruals accounting is just one piece in the jigsaw - albeit a critical one: to reap the full benefits of reform, a comprehensive change management process, involving the broader financial management and governance systems of the public sector, is required," says Patrice Schumesch, PwC's global partner for public finance and accounting.

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