Edging towards better accounting

Most governments are still using cash-based accounting, but more are adopting accruals to improve accountability and decision-making, says PwC partner Patrice Schumesch.

The financial crisis and sovereign debt crisis have created a direct challenge for governments to improve management of resources and report high-quality information to their stakeholders, such as citizens and parliament, investors in government bonds and financial markets.

While sound and transparent public accounting does not in itself lead to high-quality public finance management, it is a necessary component. Better accounting leads to better reporting, which provides the information necessary for better decision-making, which in turn should lead to better use of resources. Public sector entities and their stakeholders need to understand the full and long-term impacts of their decisions on financial performance, financial position and cashflows.

PwC’s global survey of government accounting practices, Towards a new era in government accounting and reporting, shows that only one in four central governments surveyed apply accrual accounting in preparing their financial statements. Most use cash-based accounting practices, which fail to capture information on public sector assets and liabilities, and present a very short-term view of public finances.

However, the landscape is evolving. Of the 100 countries surveyed, 37 intend to adopt accrual accounting over the next five years. The trend is particularly pronounced for developing countries, primarily in Africa, Asia, and Latin America.

International and supranational organisations such as the IMF and World Bank contribute to the adoption of accrual accounting and International Public Sector Accounting Standards (IPSAS) by laying down reporting requirements for their members or funding recipients.

In Europe, there is a clear political consensus on the need to apply harmonised accrual accounting standards to improve the quality of statistical data, which is used in the context of the budget surveillance mechanism and fiscal monitoring and policy decision-making. The European Commission has embarked on a project to implement EPSAS (European Public Sector Accounting Standards), with IPSAS as an indisputable reference and based on a strong EU governance system.

Moving to an internationally recognised accruals-based accounting framework requires a clear vision and strong political commitment to strengthen public institutions, develop high-quality standards and practices, enhance skills and build capacity. The conversion to accrual accounting principles based on IPSAS or similar standards represents a multi-year transformation project that extends well beyond the finance function.

Our survey identifies training and adapting information systems and processes as the biggest challenges. The governments surveyed also indicate a desire to improve their finance function, reporting the following key areas for improvement: fixed asset management, cost accounting, performance management, and long-term planning and forecasting. The full benefits of accrual accounting can be captured as part of a wider finance reform.

By introducing high-quality accrual requirements, governments demonstrate their desire for greater transparency and accountability, and also better information for decision-making. This is essential to the democratic accountability process and to ensure the long-term sustainability of public finances.

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Towards a new era in government accounting and reporting is at http://tinyurl.com/PwCipsas
IPSAS in a nutshell, from principles to practice is at http://tinyurl.com/PwCipsas1