Public Sector

Committee

Research Report

May 2004

Budget Reporting

International Federation of Accountants

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The Research Report

This Research Report was commissioned by the Public Sector Committee (PSC). It was prepared by Dr. Jesse Hughes with input from the Budget Reporting Steering Committee. Dr. Hughes is Professor Emeritus of Accounting at the College of Business and Public Administration, Old Dominion University, Norfolk, Virginia USA.

The objective of the Research Report is to provide input to the PSC's deliberations on such matters as whether developing International Public Sector Accounting Standards (IPSASs) on budget reporting is within the PSC's mandate and whether the PSC should action a project(s) to deal with budget reporting issues.

The Research Report represents the views of the author. At the present time, it does not reflect the views of the PSC nor necessarily of all Steering Committee members.

The PSC will consider the recommendations made by Dr. Hughes at its meeting in July 2004 (and subsequent meetings if necessary) and at that time will determine whether and how it progresses this issue.

Acknowledgement

The Public Sector Committee's Standards Program to develop IPSASs commenced in 1996. The Standards Program has received general budget support from the World Bank, the Asian Development Bank, the International Monetary Fund, the United Nations Development Program and IFAC.

The Public Sector Committee and the author wish to acknowledge that the Budget Reporting project, of which this Research Report is a part, has also received additional project specific funding from the Public Expenditure and Financial Accountability Program (PEFA). PEFA is a partnership program of the World Bank, the European Commission, the UK Department for International Development, the Swiss State Secretariat for Economic Affairs, the French Ministry of Foreign Affairs, the Norwegian Ministry of Foreign Affairs, the International Monetary Fund, and the Strategic Partnership with Africa. The PEFA Secretariat is located in the World Bank offices in Washington, DC.

Preface

International Public Sector Accounting Standards

International Public Sector Accounting Standards (IPSASs) deal with issues related to the presentation of annual general purpose financial statements. General purpose financial statements are those intended to meet the needs of users who are not in a position to demand reports tailored to meet their specific information needs. Users of general purpose financial statements include taxpayers and ratepayers, members of the legislature, creditors, suppliers, the media, and employees. The objectives of general purpose financial statements are to provide information useful for decision-making, and to demonstrate the accountability of the entity for the resources entrusted to it.

The Public Sector Committee (PSC) has issued twenty accrual basis IPSASs and a comprehensive Cash Basis IPSAS. The issuance of these IPSASs establish a core set of financial reporting standards for public sector entities.

Budget Reporting

Most governments prepare and issue as public documents, or otherwise make publicly available, their annual financial budgets. The budget documents are widely distributed and promoted. They reflect the financial characteristics of the government’s plans for the forthcoming period. Monitoring and reporting on budget execution is essential for measuring compliance with Parliamentary (or similar) authorization. Making budget data publicly available is necessary to enable transparent reporting of the government’s financial intentions and of its use of taxes.

Government budgets are generally approved by the legislature. While administrative arrangements can differ from jurisdiction to jurisdiction, in most cases spending units have no authority to commit or spend government funds until the legislation imparting spending authority has been passed by the legislature.

In many respects, and for many external users, the budget documents are the most important financial statements issued by governments. The budget also serves as a key tool for financial management and control, and is the central component of the process that provides for government and parliamentary (or similar) oversight of the financial dimensions of operations. The IPSASs currently on issue do not require the presentation of budget/forecast financial information at the time it is approved by the legislature or other authority, nor do they require the historical general purpose financial statements to report period results against the budget for that period.

Whether or not budget reporting falls within the PSC’s mandate and whether an IPSAS (or IPSASs) on budget preparation, or budget execution or other aspects of budget reporting should be issued is a contentious issue. Accordingly, the PSC determined that before committing resources to the development of an IPSAS it should commission the preparation of a Research Report to provide input to its deliberations. Consequently, the PSC commissioned Dr. Jesse Hughes to undertake research on the following matters, and to provide a report to the PSC on his findings together with any relevant recommendations.

- Current best practices in budget formulation and reporting under differing budget models and government administrative arrangements.
- Whether the development of an IPSAS on budget reporting and/or other budget related matters falls within the PSC’s mandate.
- Notwithstanding the above, whether there is any precedent, and or arguments, for an accounting standards setter to deal with budget reporting issues.
- If an IPSAS on budget reporting (or other budget related) matters is to be prepared, the matters which should appropriately be dealt with by that IPSAS.

The PSC established a Steering Committee to provide input to Dr. Hughes. The Steering Committee is chaired by PSC member Mr. Ron Points and includes non-PSC members with a wide range of experience in budget preparation, execution and reporting from a number of jurisdictions.

Views Expressed

The views expressed in this Research Report are those of Dr. Hughes and are not those of the PSC nor necessarily of all Steering Committee members.

The PSC commends Dr. Hughes for his work and thanks the Steering Committee for their input to this project. The recommendations are significant for the PSC and financial reporting by public sector entities generally. The Report provides valuable input to the PSC’s consideration of how it could progress this critical issue and identifies key issues that will need to be dealt with in any further project development.

The PSC will commence its consideration of this Report at its July 2004 meeting and at that stage consider any further actions that should occur. Readers are reminded that it was not intended that the Report resolve all issues to be addressed in developing IPSASs for budget reporting. Rather, it was developed as an internal document to provide input for the PSC as it considered whether to initiate a project directed at establishing an IPSAS for budget reporting, and the nature of that IPSAS. However, in the interests of transparency of process, and given the wide community interest in this topic, the PSC has decided to make it publicly available to interested parties.

Philippe Adhémar
Chair
Public Sector Committee (PSC)
International Federation of Accountants
May 2004

International Federation of Accountants-Public Sector Committee (IFAC-PSC)
Steering Committee on Budget Reporting

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Members of the Steering Committee are appointed in their personal capacity rather than as representatives of their nominating body. The views expressed in this study are those of the author, and not those of the members of the Steering Committee, their employers or nominating organization. In arriving at these views, the author has considered input from the Steering Committee members but the views remain those of the author.

RESEARCH REPORT ON BUDGET REPORTING

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Executive Summary

Most governments prepare and issue their annual financial budgets as public documents. Whether there should be an IPSAS that deals with general purpose reporting of the budget as a public document is considered in this Research Report. The objective of the IFAC Public Sector Committee (PSC) is to develop programs aimed at improving public sector financial management and accountability, including developing International Public Sector Accounting Standards (IPSASs) and promoting their acceptance. To meet this objective, the PSC has issued a number of IPSASs which identify the general purpose financial statements that are necessary to meet the needs of users who are not in a position to demand reports tailored to meet their information needs, and specify how a wide range of transactions and events are to be accounted for in those financial statements. The IPSASs note that general purpose financial statements can provide users with information indicating whether resources were obtained and used in accordance with the adopted budget. Yet, current IPSASs only **encourage** governments to include in their financial statements a comparison of the actual results of operations with the approved budget for the reporting period.

The PSC identified budget reporting as an important project to be progressed during the second stage of its standards program. It commissioned the preparation of this Research Report to provide input on whether an IPSAS (or IPSASs) should be issued on budget reporting. The Project Brief is included as Appendix A. The objectives of the research are to identify the following:

- Current best practices in budget formulation and reporting under differing budget models and government administrative arrangements;
- Whether the development of an IPSAS on budget reporting and/or other budget related matters falls within the mandate of the PSC;
- Whether there is any precedent for an accounting standard setter to deal with budget reporting issues; and
- The issues which should appropriately be considered in any IPSAS that might be issued.

The major findings and recommendations of the Research Report are outlined below.

Budget Process

There are three main stages in the budgetary process: (1) During the **formulation** stage, initial budgets and forecasts are developed and submitted to the legislative bodies for consideration. Spending authority is granted by legislative bodies based on the political priorities and fiscal policies of government. These ex-ante budget reports reflect the financial characteristics of the government’s plans for the forthcoming period and are used to analyze the potential consequences of those plans on the economy. (2) Implementation of the fiscal policies reflected in these budgets is accomplished through the use of budgetary accounts in the accounting system during the **execution** stage. (3) Public **reporting** of the ex-ante budgets (both legally approved budgets and prospective budgets) permits the government to identify their financial intentions (transparency). Further, ex-post **reporting** of a comparison between the actual results and the approved budget permits the government to identify their adherence to those budgets by comparing performance against the approved budget (accountability) and providing explanations of significant variances.

Budget Practice

This study on budget reporting considers research undertaken and best practices published by many bodies. If the budget is to be effective, it is generally recognized that the budget needs to be comprehensive and encompass all of the expenditures by government for all budget dependent entities. Analysis performed within five African countries indicates that their budgets are prepared on the cash basis and there are varying degrees of transparency in the reporting of budgetary data. Other research has found that some European countries have moved or are in the process of moving toward the accrual basis of accounting but have not expressed significant plans to change from the cash basis of budgeting. Also, a very comprehensive Budget Practices and Procedures survey conducted by the Organization for Economic Cooperation and Development (in collaboration with the IADB, IMF and World Bank) indicates that many countries plan to move toward the accrual basis of accounting. However, some of these countries prepare their budgets on the cash basis and they plan to continue to prepare their budgets on the cash or near cash basis for the foreseeable future although their accounting will be on the accrual basis.

PSC Mandate

The objective of the PSC is identified in the Preface to the IPSASs as follows: “Develop programs aimed at improving public sector financial management and accountability including developing accounting standards and promoting their acceptance.” This Report argues that:

- Inclusion of budgetary information and other budget related matter in the accounting system and reporting budgetary data to constituents is crucial to improving public sector financial management (transparency).
- To assure that government officials are held accountable for their budgetary decisions, it is essential that users be informed on the degree by which their government officials were able to operate within the limits of the approved budget (accountability).
- The best mechanism by which to keep the public informed is through the budget reports (both legally approved budgets and prospective budgets) at the time of their approval as well as the compliance reports issued as a component of the general purpose financial statements.

As such, developing IPSASs to deal with legally approved budgets, prospective budgets, and reporting of actual performance against such budgets fall within the PSC mandate identified in the Preface.

Recommendations

Based on the research conducted in this study, the following is recommended:

1. **The PSC should issue an IPSAS (or IPSASs) on budget reporting since it falls within the mandate identified in the Preface to the PSC. It may be beneficial to issue separate IPSASs on ex-ante and ex-post budget reports.**
2. **An accounting standard should be issued to require that the forecast and other prospective financial information be reported to their constituents in order to keep them informed on future financial implications of government policy.**
3. **The accounting standards should require that the legally approved budget be published with the appropriate supporting budget documentation (e.g. assumptions).**
4. **The accounting standards should be broad enough to support the integration of budgetary and accounting systems through the use of budgetary accounting procedures. It may be beneficial to issue a separate IPSAS on budgetary accounting procedures.**
5. **In relevant studies and guidance, the PSC should acknowledge and encourage the use of commitment accounting procedures intended to assure that budgetary funds are available prior to release of a purchase order or contract.**
6. **Ex-post budget reports reflecting budget to actual comparisons should be part of the general purpose financial statements issued at the end of the fiscal period for each reporting entity at each level of government.**
7. **The Comparative Budget to Actual Statement should include the original budget as approved by the legislative body as well as the final adopted budget.**
8. **Governments should be encouraged to operate their budgeting and accounting systems on the same basis. If the budgetary system is on a different basis than the accounting system, a statement should be developed to reconcile key differences between the two systems.**
9. **Ex-ante and ex-post budget reports should meet the qualitative characteristics (understandability, relevance, reliability, and comparability) of financial reporting specified in IPSAS 1.**
10. **Budget reporting should be incorporated into the conceptual framework for IPSASs.**

Issues Raised by Steering Committee Members

In order to implement the above recommendations, the following key issues need to be resolved:

1. **A clear definition of budget reporting needs to be developed.**
2. **A decision on whether to include ex-ante budget reports (legally approved budgets and prospective budgets) in an IPSAS needs to be made.**
3. **The extent of coverage of budgetary accounting procedures for budgetary execution and control procedures in an IPSAS needs to be defined.**

4. **A decision to include ex-post budget comparative statements as part of general purpose financial statements in an IPSAS needs to be made.**

5. **Where there are differences between the budgetary and accounting bases, the requirement for and format of a reconciling statement needs to be determined.**

6. **When a decision is made to issue an IPSAS on budget reporting, procedures will need to be identified to assure that qualitative characteristics of financial reporting are met.**

7. **Budget reporting procedures will need to be included in the Conceptual Framework for financial reporting of government entities.**

Research Report on Budget Reporting

Objective

The primary objective of this Research Report is to determine if an IPSAS should be issued on budget reporting. In its initial strategy papers prepared in 2000 and 2001, the IFAC Public Sector Committee (PSC) identified budget reporting as a key public sector specific issue to be addressed in the second phase of its standards setting program. With the completion of its core 20 accrual IPSASs and the comprehensive cash basis IPSAS, the PSC actioned[1] this research project to identify and make recommendations as appropriate on the various aspects of budget formulation, execution and reporting.

Scope

This Research Report deals with budgets at all levels of government and for all reporting entities other than Government Business Enterprises (GBEs). Readers should note that the definition of a reporting entity in the IPSASs may differ from the legislative specification of an entity for budget preparation and presentation purposes.

For purposes of this Research Report, budget reporting includes all budget reports issued to the public for transparency and accountability purposes. This would include the budgets approved by the legislative bodies for the government itself and for governmental entities at local, state, and national levels prior to or near the beginning of the fiscal period as well as prospective or forecast budgetary data **(ex-ante)**. In addition, budget reports would include budget to actual comparative statements issued at the end of the accounting period **(ex-post)**.

This study addresses the following:

- Current best practices in budget formulation and reporting under differing budget models and government administrative arrangements;
- Whether the development of an IPSAS on budget reporting and/or other budget related matters falls within the PSC's mandate;
- Notwithstanding the above, whether there is any precedent, and or arguments, for an accounting standard setter to deal with budget reporting issues; and
- If an IPSAS on budget reporting (or other budget related) matters is to be prepared, the issues which should appropriately be dealt with by that IPSAS. The issues to be considered are as follows:
    - The nature and requirements of any IPSAS that might be developed considering budget formulation, execution, and reporting.
    - The application of the recognition and measurement requirements of existing IPSASs in the budget context.

1 See Terms of Reference in Appendix A.

The qualitative characteristics of financial reporting previously identified in IPSAS 1[2] will be considered in this Research Report. These are as follows:

- Understandability
- Relevance
- Reliability
- Comparability
- Constraints on Relevant and Reliable Information

Some governments prepare tax expenditure budgets. These budgets identify the estimated costs to the tax base due to preferential treatment for specific activities (i.e., deductibility of interest payments on home mortgages to encourage the purchase of homes). However, these tax expenditure budgets are not dealt with in this Research Report since income lost due to preferential tax treatment (i.e., costs) is compiled separately from other budget reports.

Management accounting and reporting of financial information in internal or special purpose reports to governments and senior government officials are significant issues that warrant further study. Budget information may be presented in documents other than general purpose financial statements and a cross-reference from general purpose financial statements to such documents may be appropriate, particularly to link budget and actual data to non-financial budget data and actual service achievements. However, management accounting issues are outside the specific objectives and scope of this study. Consequently, they are excluded from this Research Report.

Definitions

Accounting terms included in this Research Report are defined in the “Glossary of Defined Terms in IPSAS 1 to IPSAS 18” as published in the Handbook of International Public Sector Accounting Standards, 2004 Edition. Budgetary terms that are in common use in the budget literature are defined below and are used with these meanings throughout this paper:

Allocation—part of an appropriation that is designated for expenditure by specific organization units and/or for special purposes, activities, or objects.

Allotment—an internal allocation of funds on a periodic basis usually agreed upon by the heads of government departments or similar entities and the chief executive.

Appropriated Budget—the expenditure authority created by the appropriated bills or ordinances that are signed into law and the related estimated revenues. The expenditure authority is generally considered the legal limit within which a governing body must operate.

Appropriation—an authorization granted by a legislative body to set aside funds for purposes specified by the legislature. It is usually limited in amount and time over which it can be expended.

2 Appendix 2, Presentation of Financial Statements, IPSAS 1 (May 2000).

Budgetary Definitions:

1. **Line item (or object class) budget**: The budget is separated into expenses by economic classification such as compensation of employees, use of goods and services, etc., as well as the purchase of capital assets.
2. **Program budget**: a budget made up of programs as groupings of activities intended to contribute to identifiable government objectives (e.g., poverty alleviation, literacy, control of contagious disease.).
3. **Performance budget**: a program budget that also presents measures of performance and service delivery (e.g., students graduating, surgical operations performed, tons of cargo unloaded).
4. **Zero-base budget**: a budget that is justified from zero. Each agency has to justify its whole budget as if it were applying for funding for the first time.
5. **Biennial budget**: a budget that provides funds for two years instead of one. Budget allocations do not lapse until the end of the second year.
6. **Multi-year budget**: a budget that takes into account not just the budget year, but two or more subsequent years. Usually lapse of funds occurs at the end of the budget year. Figures for "out years" are indicative.
7. **Medium-term fiscal framework (MTFF)**: a process for improving government expenditure programs that assists decision-makers to gauge what is affordable in aggregate over the medium-term and to reconcile this with spending policies and their costs over the same period.
8. **Capital budget**: a plan of proposed capital outlays, such as for infrastructure, buildings, equipment, and other long-lived assets, and of the means to finance them.
9. **Recurrent budget**: a plan of proposed funding needed to service the ongoing operations of government. Such a plan would include compensation of employees, use of goods and services, etc.
10. **Supplementary budget**: These are budgets that are enacted during or after the end of the financial year to authorize expenditures not within original budgets. These do not normally represent policy changes, but may be necessary where the original budget did not adequately envisage expenditure requirements (e.g., war, natural disasters, etc.).
11. **Development budget:** Typically the development budget is a collection of projects, whether internally or externally funded. The rest of the budget is then described as a recurrent budget. The development budget frequently includes non-capital items, and the recurrent budget often includes capital items.
12. **Below the line items:** In some countries, this term is used to refer to asset and liability accounts (accounts that are "below the line" of budget accounts), and also in some cases to monies that are effectively held in trust by government for some special purpose.

Budgetary Processes:

1. **Budget formulation**: the practices and concepts that budget professionals use to create and review a budget until enacted into law.

2. **Budget execution**: the management activities that take place from enactment of the budget into law until the end of the fiscal period.
3. **Budget reporting**: considered to be of two types: **ex-ante—**the external reporting of the budget approved by the legislative body at or near the beginning of the fiscal period as well as external reporting of prospective or forecast budgetary data; and **ex-post—**the external reporting of the financial activities relative to the approved budget for the fiscal period until the final audit after the end of the fiscal period. The budget to actual comparative statement is generally issued as a component of the historical financial statements.

Commitment (also known as an encumbrance)—There is not a generally accepted single definition of this term. It is sometimes considered to be synonymous with obligations. A commitment is generally acknowledged as the government's responsibility for a possible future liability based on a contractual agreement. It includes outstanding purchase orders and contracts where goods or services have not yet been received. Some governments consider the term "commitments" to only apply to purchase requests or other such pre-obligation documents. As such, outstanding commitments lapse at the end of the fiscal period. For purposes of this report, commitments, encumbrances, and obligations are considered to be intended actions that could result in a possible future liability, and are subject to the same accounting treatment.

Encumbrance—See definition under "commitment."

Estimated Revenue—an amount anticipated to be collected during the accounting period.

Expenditures—the incurrence of a liability for a capital asset or the disbursement of cash during the fiscal period as used in the cash or modified accrual basis of accounting.

Gross Domestic Product—the value of all final goods and services produced in the country within a given period.

Infrastructure Asset—a long-lived asset that normally is immovable, part of a system or network, specialized in nature, does not have alternative uses, and may be subject to constraints on disposal. Examples include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems.

Prospective budgetary information—financial information based on assumptions about events that may occur in the future and possible actions by an entity. Prospective financial information can be in the form of a forecast, a projection or a combination of both, for example, a one year forecast plus a five year projection.

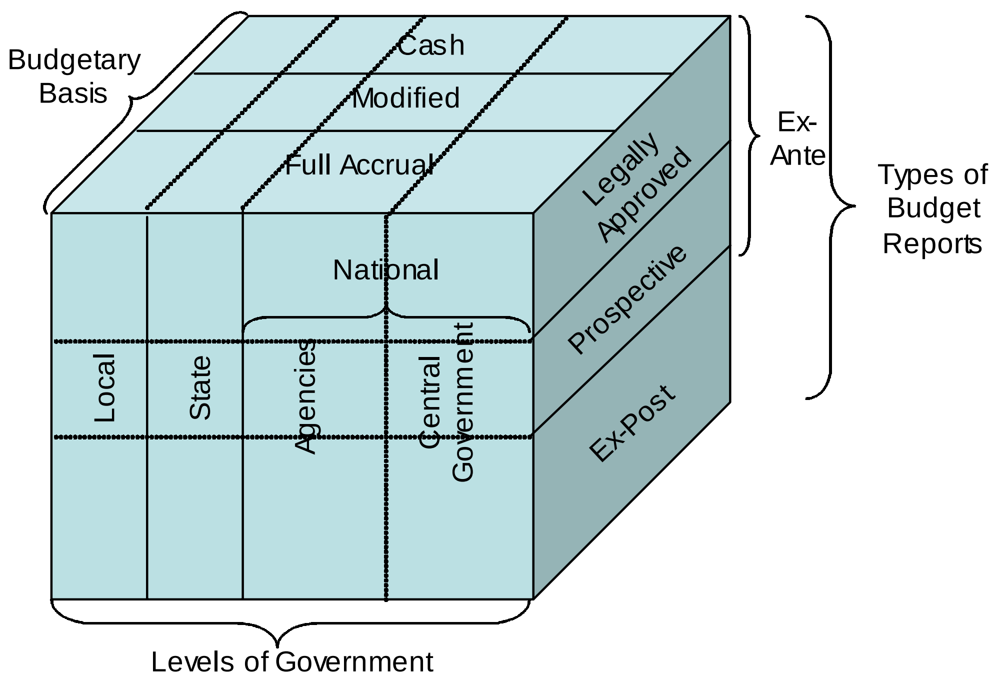
Virements—the transfer of expenditures between budget heads. Normally, these will be constrained by legislation and/or financial rules.

Warranting—the three stages of budgeting are identified as formulation, execution and reporting. In some countries, there is a sub-stage within budget execution of "warranting." The budget as approved does not in itself provide authority for expenditure. Rather, expenditure authority has to be warranted under procedures that will be laid down in the financial procedures. It is often used as a mechanism for cash management.

Budget Overview

Most, but not all, governments prepare and issue their annual financial budgets as public documents, or otherwise make them publicly available. There are three main stages in the budgetary process which may be conducted on a cash or accrual basis at each of the levels of government (local, state, and national): (1) During the **formulation** stage, initial budgets are developed and submitted to the legislative bodies for consideration. Spending authority is granted by legislative bodies based on the political priorities and fiscal policies of government. These budgets reflect the financial characteristics of the government's plans for the forthcoming period and are used to analyze the potential consequences of those plans on the economy. (2) Adherence to these fiscal policies is accomplished during the **execution** stage. (3) Ex-ante public **reporting** of the initial budgets and forecast budgetary data (important for transparency) permits the government to identify its financial intentions. In the ex-post **reporting** stage, a comparison of the actual results with the final budget permits the government to identify its actual performance against the approved budget (accountability) and provide explanations of significant variances. The following budget reporting model is used throughout this Research Report to identify this relationship:

Exhibit 1. Budget Reporting Model



Note: The modified budgetary basis encompasses both the modified cash and modified accrual bases. It could also apply to the commitments/obligations basis that is referred to by some governments.

The Budget

Budget documents are usually published and frequently widely commented upon in the mass media. Given the lateness of issue and complexity of historical public accounts in some countries, **the budget reports (both ex-ante and ex-post) are often the most important source**

of publicly available information on public finance. They reflect the financial characteristics of the government's plans for the forthcoming period and are used to analyze the consequences of those plans on the economy. Making budget data publicly available at the time of approval is necessary to enable transparent reporting of the government's financial intentions. Reporting period results against the budget for the same period is a necessary component of any accountability regime. The matters to be considered in the three stages of budget formulation, execution, and reporting are identified in Exhibit 2 below:

Exhibit 2: Matters to be Considered in the Budgetary Process

Stage	Possible areas for consideration and guidance
1. Formulation	Budget formulation is a policy process and there are important aspects of the matters in the budget documents that could be addressed by an IPSAS, e.g., • Basis on which budget revenues and expenditures are estimated and time periods to which budgeted amounts are allocated (linked to accounting base for financial reporting) • Information to be included to achieve transparency, including need to facilitate analysis by external stakeholders • Classification of items –as defined in the chart of accounts • Presentation and aggregation of data - linked to concepts of transparency • Incorporation of non-financial performance targets • Where accrual is the basis for budgeting, inclusion of cash flow data to be able to assess fiscal impact of budget decisions
2. Execution	This tends to be an "internal" government process and not subject to external reporting as indicated below. However, there is a need to consider how "virements" and supplementary budgets will be reported to external stakeholders
3. Reporting	Ex-ante and ex-post budget reporting should be an important part of financial statements. There are many issues to be considered, e.g., • Consistency of definitions between accounting and budget figures • What figures are used as comparators when budgets are adjusted through virements and supplementaries • Incorporation of non-financial information • Achieving transparency and accountability

Fiscal Transparency

Fiscal transparency is a major contributor to the cause of good governance. It should lead to better informed public debate about the design and results of fiscal policy, make governments more accountable for the implementation of fiscal policy, and thereby strengthen credibility and public understanding of macroeconomic policies and choices. Some countries (i.e., Germany) have special mechanisms for reviewing the realism of underlying economic forecasts, as well as related revenue estimates, to assure that the public is fully informed regarding these projections. Fiscal transparency requires disclosure of more than just budget (and actual) figures. It also requires disclosure of information on the assumptions behind budget figures (i.e., economic and other risk factors) that may be subject to audit or review by the external auditors. In a globalized environment, fiscal transparency is of considerable importance in demonstrating macroeconomic stability and high-quality growth. However, it is only one aspect of good fiscal management. Attention has to be given also to increasing the efficiency of government activity and establishing sound public finances.

To encourage countries to publicize their budgetary practices, the International Monetary Fund (IMF) issued a Code of Good Practices on Fiscal Transparency (See Appendix B). The Code recommends the following four key objectives:

- The roles and responsibilities in government should be clear;
- The public should be provided with full information on the past, current, and projected fiscal activity of government in a timely manner;
- Budget preparation, execution, and reporting should be undertaken in an open manner; and
- Fiscal information should attain widely accepted standards of data quality and be subject to independent assurances of integrity.

Financial Management

Many governments provide various guidance documents on the procedures to be followed as part of the budget process. These include the areas to be considered when developing proposals and new initiatives, capital budgeting and working capital management, setting user charges, and output costing. An example of the range of information that a government might provide is available on the New Zealand Treasury’s “Managing the Public Sector” section of their website: http://www.treasury.govt.nz/publicsector/.

Some professional organizations publish best practices in public budgeting in order to encourage their members to improve their budgeting procedures. One such set of practices, by the National Advisory Council on State and Local Budgeting in the United States, is summarized in Appendix C. The following four principles are recommended:

1. Establish broad goals to guide government decision making;
2. Develop approaches to achieve goals;
3. Develop a budget consistent with approaches to achieve goals; and
4. Evaluate performance and make adjustments.

The budget also serves as a key tool for financial management and control, and is the central component of the process that provides for government and parliamentary (or similar) oversight of the financial dimensions of operations. For budgetary control by internal management, many governments prepare budget to actual comparative schedules periodically within the budgetary period as well as at the end of the fiscal year. The format of these comparative schedules is generally similar to the following:

Organization	Original Budget	Adjustments	Modified Budget	Actual	Variance
XXXXX	$XXX,XXX	$XXX	$XXX,XXX	$XXX,XXX	$XXX

Note: Some countries compute the variance from the original budget and explain the reason (including in-year updates) for subsequent adjustments. Other countries compute the variance from the modified budget and explain significant differences. (See Appendix J.)

Budget Authorization

Government budgets are approved by the legislature and compliance is a legal matter. At each level of government, these budgets serve as plans for economic governance and controlled use of resources for the governmental entity. While administrative arrangements can differ from jurisdiction to jurisdiction, in most cases, spending units have no authority to commit or spend government funds until the legislation imparting spending authority (the budget) has been passed by the legislature. In some cases, spending authority is granted at the same level as the prior year under a continuing resolution if the budget is not passed prior to the beginning of the fiscal year. In addition, some governments permit purchase orders that have not been filled prior to the end of the fiscal period to be carried forward and funded in the next fiscal year.

Budget Reports

Each level (local, state, or national) of government will issue budget reports to inform users of their fiscal plans. These budget reports include those that are issued at or near the beginning of a fiscal period to reflect the legally approved budget as well as those reports that identify prospective or forecast data (ex-ante). In addition, budget reports are issued at the end of the fiscal period to reflect the actual use of resources compared to those resources that had been approved by the legislative body (ex-post). The relationship between the types of budget reports and the levels of government are identified below:

Types of Budget Reports		**Local**	**State**	**National**	
				Agencies	**Central Govt.**
Ex-Ante	**Legal Limits Approved by Legislature**				
	Prospective				
	Ex-Post				

Budget reports by type may be prepared on the cash, modified cash or modified accrual (including obligation/commitment), or the accrual basis as reflected in the table below:

<table>
<tr><th colspan="2">Types of Budget Reports</th><th>Cash</th><th>Modified</th><th>Accrual</th></tr>
<tr><td rowspan="2">Ex-Ante</td><td>Legal Limits Approved by Legislature</td><td></td><td></td><td></td></tr>
<tr><td>Prospective</td><td></td><td></td><td></td></tr>
<tr><td></td><td>Ex-Post</td><td></td><td></td><td></td></tr>
</table>

Consistency in Reporting Between Accounting and Budget Systems

Most governments will prepare their budget reports on the cash basis because the cash information is more readily available. In addition, some argue information about only cash is more readily understandable than information about all assets and liabilities. Further, cash systems are simpler to implement and costs are low due to the lower level of accounting skills required. As some governments transition to the accrual basis of accounting, a few prepare their budget reports on the modified accrual basis (which includes current assets and liabilities) in order to plan for the use of financial resources. If the full accrual basis of accounting (which includes total assets and liabilities) is used, some governments may move to the accrual basis of budgeting so that they can plan for the use of total resources. This relationship is reflected in the table below:

<table>
<tr><th colspan="2" rowspan="2"></th><th colspan="3">Budgeting Basis</th></tr>
<tr><th>Cash</th><th>Modified</th><th>Accrual</th></tr>
<tr><td rowspan="3">Accounting Basis</td><td>Cash</td><td></td><td></td><td></td></tr>
<tr><td>Modified</td><td></td><td></td><td></td></tr>
<tr><td>Accrual</td><td></td><td></td><td></td></tr>
</table>

Note: The shaded areas identify those governmental entities where the budgeting system and the accounting system use the same basis.

As countries transition to the accrual basis of accounting, some may prefer to retain the cash basis for budgetary reporting purposes. Consequently, the accounting system would retain the cash or near cash basis for budgetary control and use the accrual basis for preparation of the general purpose financial statements. A few countries are in the process of moving the budgetary system from the cash basis to the accrual basis in order for the budgetary system to be consistent with the accounts recorded on the accrual accounting basis. However, this transition period can be lengthy in order to assure that control is retained in the budgetary system. When there is a difference between the budgetary basis and the accounting basis, readers of the financial statements may get confused between the differences reported as surplus/deficit from operating activities in the accrual accounting reports and net cash flows from operating activities in the cash or modified cash/accrual basis budget report.

Current Budget and Accounting Practices

Comprehensive Budgets

To be effective, it is generally recognized that the budget needs to be comprehensive and governmental activities should encompass all of the expenditures by government for all budget dependent entities. Since one objective of this Research Report is to identify guidance on best practices in budget formulation, execution, and reporting, it is necessary to develop some criteria for such best practices. The World Bank Public Expenditure Management Handbook[3] suggests three levels of goals for expenditure management. These are linked to criteria in a matrix provided by Michael Parry (International Management Consultants), as indicated in Exhibit 3 below:

Exhibit 3: Financial Management Goals and Criteria

GOALS	CRITERIA		
Level 1 - fiscal management ➢ Flows - revenues, debt, transfers, capital and recurrent expenditures ➢ Balances - internal and external debt, assets ➢ Risk - contingent liabilities	**Proper use of public resources** In accordance with constitutional, legal and regulatory requirements Avoidance of corrupt practices	**Transparency** Information for stakeholders in a format that facilitates understanding and analysis	**Accountability** Those accountable for the use of public resources made accountable for their actions and stewardship
Level 2 - resource allocation ➢ Optimal resource allocation ➢ In accordance with government policy priorities			
Level 3 - value for money ➢ Management of public resources in order to achieve efficiency, economy and effectiveness in expenditure			

In some jurisdictions, budget formulation and execution is a centralized function. In others, it is decentralized. For example, in Europe, some budgets are prepared and reported for the aggregate of three levels of government: national, state or provincial, and local governments. Where it is decentralized, the national government does not control the state or local government.

Extra budgetary funds weaken the budget both as a resource allocation tool, and as a tool of fiscal management. Many systems, especially in developing countries, have the potential for large extra budgetary expenditures. Some examples include the following:

(i) Funds are received by line agencies that are then available for expenditure, without passing through the consolidated fund. There may be merit on occasions for linking expenditures to revenues raised, but these need to be planned and controlled through a central budget process. In most countries, direct use by agencies of monies they collect is against the Constitution (which requires all monies to be paid into the consolidated fund) but it still

[3] Chapter 2, Public Expenditure Management Handbook, 1998 (The World Bank).

happens. From a managerial perspective, such linkage may be beneficial since it links expenditure to collection efficiency.

(ii) Quasi-fiscal activities of state financial institutions exist to subsidize state enterprises. This includes loans at low interest rates without the expectation of repayment.

(iii) Some government entities permit direct access by projects to donor funds. From a project management perspective, it may be desirable to by-pass the bureaucracy and have direct access to donor funds. In some cases, donors encourage such a system. However, this reduces the effectiveness of the budget process to control expenditures.

(iv) Some government entities have multiple funds outside the consolidated fund that are not included in the central budget process. This includes special funds for ongoing expenditures (e.g. road construction, health care projects, etc.), special funds managed by the central budget authority, budgets of autonomous/decentralized agencies, emergency/contingency funds, etc. In such cases, it is difficult to achieve effective control over these funds.

OECD/World Bank Survey of Current Budgetary Practices

The Organization for Economic Cooperation and Development or OECD (in collaboration with the World Bank, the Inter-American Development Bank, and IMF) developed a very comprehensive survey on Budget Practices and Procedures. They are in the process of surveying 30 OECD Member countries and 30 non-OECD countries on their Budget Practices and Procedures. The goal of this survey is to create a database of quantitative measures that will provide a unique and comprehensive resource for various groups to assist them in making well-informed analyses and enable them to compare and contrast national practices. The OECD/World Bank recently published the results of their Budget Practices and Procedures Survey on their website (see http://ocde.dyndns.org). Forty-four of the 60 polled countries responded by December 31, 2003 although not all the questions were answered in full by each of the countries. Responses are in the process of being verified. The countries responding to the survey were as follows:

Algeria	Argentina	Australia	Austria
Belgium	Bolivia	Cambodia	Canada
Chile	Colombia	Czech Republic	Denmark
Egypt	Finland	France	Germany
Greece	Hungary	Iceland	Indonesia
Ireland	Israel	Italy	Japan
Jordan	Kenya	Korea	Mexico
Morocco	Netherlands	New Zealand	Norway
Peru	Portugal	Slovak Republic	Slovenia
South Africa	Spain	Suriname	Sweden
Turkey	United Kingdom	United States	Uruguay

The results of the survey are grouped under these separate and distinct parts:

1. General Information
2. Formulation
3. Budget Execution
4. Accounting, Control and Monitoring Systems
5. Budget Documentation and Performance Management
6. Fiscal Relations Among Levels of Government
7. Special Relationships/Issues

Selected sections of the survey results that were felt to be especially pertinent to this study are reflected below:

Budgeting, Accounting, and Financial Reporting

Section 4.2 of the survey discusses the Budgeting, Accounting and Financial Reporting practices of the countries. The major findings were as follows:

Number with a unified accounting and budget classification system	35
Authority for determining the technical standards for the budget:	
Internally by Ministry of Finance (MOF) or Central Budget Authority	26
Formal Advisory Board	9
Authority for determining the technical standards for the financial statements:	
Internally by MOF or Central Budget Authority	17
Formal Advisory Board	9
Cash or obligations/commitments basis of accounting for the budget	
Full accrual basis budgeting to be introduced	5
Additional accrual basis information to be presented	11
Planning to change from cash to obligations/commitment basis	2
Not planning any change from the cash or obligations/commitments basis	16
Number indicating public debt interest as highest chance of being on accrual basis	10
Number providing a partial or full statement of their accounting basis in the budget	28
Consolidated, government-wide annual financial statements:	
Number reporting on a cash, or cash with a few exceptions, basis	20
Number reporting on a full accrual, or full accrual with a few exceptions, basis	7
Number not reporting such a statement	4
Government organization annual financial statements:	
Number reporting on a cash, or cash with a few exceptions, basis	18
Number reporting on a full accrual, or full accrual with a few exceptions, basis	8
Number reporting on full accrual basis that capitalize and depreciate all assets	10

Assets not capitalized and depreciated:	
Military assets	11
Historical buildings	9
Highways	7
Basis for valuation of capital assets with readily identified market values:	
Historical cost	13
Current market value or replacement cost	10
Audited final accounts published and available publicly:	
Within three months of the end of the fiscal year	4
Within three to six months of the end of the fiscal year	13
Generally more than six months of the end of the fiscal year	17
Not published and available	2

Types of Data Reported in Budget Documents[4]

In Section 5.2, the countries were questioned on the Types of Data Reported in Budget Documents. The major findings were as follows:

Time period of budget forecasts:	
Forecast of fiscal aggregates for the budget year plus two years	23
Formal rolling medium-term (3-5 years) estimates of expenditures	20
Formal rolling medium-term (3-5 years) estimates of revenues	17
Audited final accounts submitted to the legislature:	
Within six months	20
Within six to 12 months	13
After more than 12 months or not at all	7
Budget to actual comparative statement prepared:	
Yes, for past year	27
Yes, for past two years or more	6
No	2
Other	5
Budget to actual comparative statement legally required:	
Yes	13
No	27

4 There was no indication that the budget forecasts were subject to external review. Budget information was included in ex-post comparative financial statements. Although it is not specified in the survey instrument, it is assumed that budgetary information is included in the audited final accounts when submitted to the legislature.

Budget Classification

Section 5.3 of the survey addresses Budget Classification. The major findings were as follows:

Classification schemes:	
By function	33
By economic class	35
By line-item or object class	21
Capital/current expenditure breakdown	33
By organization or administrative unit	29
By program	22
UN/GFS functional classification used	14

Budgeting and Reporting

Section 6.5, Budgeting and Reporting, asks questions about the fiscal relationships between the various levels of government. The major findings were as follows:

Common standard for budgeting by national and sub-national governments:	
Yes, same budget classification and accounting rules set by national government	18
No, common standards are not used but national government sets standards for both	11
No, common standards are not used and each authority decides own classification	9
Actual general government figures transmitted to legislature:	
Yes, transmitted and discussed at the end of the financial year	8
Yes, transmitted for knowledge purposes at the end of the financial year	17
No, figures are not transmitted at the end of the financial year	10

Summary of Five African Countries

In 2002, civil society budget analysis organizations from Ghana, Kenya, Nigeria, South Africa and Zambia published the results of a research project on Budget Transparency and Participation in the Budget Process.[5] The purpose of the study was to evaluate the extent to which these countries provided sufficient budgetary information and access to citizens and civil society organizations so that they can participate effectively in the budget process. The study was intended to create a civil society agenda to demand changes in the budget process.

Research Method

The research results were derived from semi-structured interviews with respondents in the executive and legislature branches of government, independent organs of state, civil society and the media. The qualitative data derived from these interviews was supplemented by a survey of budget documentation, audit reports, policy papers and legislation. In addition, a peer review

5 Details of the project may be found at http://www.internationalbudget.org/resources/africalaunch.htm.

group was established in each country to check the congruency and accuracy of the results. The study framework examined three issues. The first dimension examines the four stages of the budget process – the drafting, legislative, implementation and auditing stages. The second dimension examines each of these stages by looking at the availability of information, the clarity of roles and responsibilities between institutions in the budget process, and the systems and capacity to generate budget information. The third dimension focuses on the legal framework supporting transparency and participation in the budget process.

Results

Although aspects of budget transparency and participation in the budget process were found to be wanting in each country, there were important distinctions between the countries studied. The results suggest that the countries could be classified into three layers. South Africa scored the highest, Ghana and Kenya occupy a second layer, and Nigeria and Zambia a third layer. South Africa scored “good” on the legal framework and “moderate” on transparency and participation in the budget process. This reflects the comprehensive overhaul of the budget process undertaken since 1994 and the substantial improvements in public availability of information. There is a clearer framework for accountability for public resources and delivery and more transparent management of the wider public sector. The primary concern now is the creation of better access for parliament and citizens, and the development of capacity in these institutions to make good use of the information.

The next layer of countries is Kenya and Ghana. Both countries scored “moderate” on the legal framework and “weak,” but improving, on participation. The Kenyan legal framework was found to be comprehensive, but outdated and in conflict with government policy. Although substantial public information is generated, it is often late, inaccurate and in formats that are hard to use. The budget process in Kenya does not easily accommodate external participation, but both parliament and civil society are increasingly exploiting opportunities to hold the executive accountable. In Ghana, a moderately good legal framework should ensure greater information and participation. However, this potential is compromised by gaps and the official secrets legislation, and is often outdated. Although public information is more available in Ghana than in Zambia and Nigeria, the information that is produced is frequently late, inaccurate and not particularly useful – in many cases the result of poor capacity to produce information. On the positive side, the introduction of the Medium Term Expenditure Framework (MTEF) and increasing participation by civil society is helping to push the country in the right direction.

In the third layer of countries, Zambia and Nigeria were found to have both “weak” legal frameworks and “weak” transparency and participation. The legal framework in Zambia allows for virtually limitless expenditure with approval after the fact and requires very little information to be published. While transparency is hampered by lack of compliance and cash budgeting, civil society and parliament are starting to forge a space for participation with positive effects. In Nigeria, a contradictory and ambiguous legal framework is a large part of the problem, particularly as it impacts on the comprehensiveness of the budget and the audit process. While civil society participation also remains weak, the increasingly active engagement of the legislature is a positive sign.

Summary of Nine European Countries and the European Commission (EC)

"Reforming Governmental Accounting and Budgeting in Europe" was published in late 2003.[6] To facilitate convergence in the accrual-based reforms, this book describes (at national and sub-national levels) the current and prospective forms of financial reporting and budget preparation for nine countries in Europe: Finland, France, Germany, Italy, Netherlands, Spain, Sweden, Switzerland, and the United Kingdom. In addition, a chapter was added on the reform of the EC's accounting system. The goal of the publication was to spark discussion, highlight areas for action, and present practical solutions. The reform of governmental budgeting and accounting practices was identified as an important and necessary long-term objective.

Research Method

Research was conducted in each of the countries by one or more nationals of the relevant country in a cooperative effort between academe and practice. The intent of the research was to identify current governmental accounting practices, as well as current budgetary accounting principles and procedures. Workshops were conducted throughout the research period to establish a uniform structure for the country studies, to discuss relevant findings, and to assist in developing cross-country conclusions.

Results

All of the countries covered by the study have embarked on reforms of the accounting reporting systems towards full accrual accounting for their core national or local governments. Whereas all local government systems have been or are being reformed, the reform process has not yet started in the national governments of Germany, Italy, and the Netherlands. Six of the national governments (Finland, France, Spain, Sweden, Switzerland, and United Kingdom) have begun the reform process, as has the EC. Three of them (Finland, Spain, and Sweden) have essentially completed the reform by creating the necessary legal requirements and the new system is in regular operation. This also applies to the United Kingdom except that whole-of-government financial statements are not yet in place. The accounting method used impacts on the budgetary reporting practices, especially relative to comparative budget to actual statements if the budget is on a different basis than the accounting system.

The clear pattern was for the local governments in each country to precede the national governments; in none of the countries was national governmental accounting reformed first. "The norm for budgeting is that the accrual accounting either has no influence on budgeting (which retains its basis of cash or cash plus changes in financial assets and liabilities) or the influence is implicit (the accrual accounting is used to report on realization of the budget but the budget itself does not significantly refer to accruals)."[7]

PSC Mandate on Budget Reporting and/or Other Budget Related Matters

This Report focuses on IPSASs that are standards for general purpose financial statements. Recommendations made about the PSC role in developing standards (rather than identifying and

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6 Reforming Governmental Accounting and Budgeting in Europe; Klaus Luder and Rowan Jones, editors (Fachverlag Moderne Wirtschaft, Frankfurt, Germany), 2003.

7 Ibid, p. 55.

encouraging best practices) refer to standards that will be complied with in preparation of general purpose financial statements. These statements will be audited to ensure compliance with the IPSASs. Thus, use of these standards is different from benchmarks (or industry standards) identified by international oversight bodies for best budget practice and often relate to matters of process, technique and skill.

Discussion

The objective of the PSC is identified in the Preface to the IPSASs as follows: "Develop programs aimed at improving public sector financial management and accountability including developing accounting standards and promoting their acceptance."[8] Further, the Preface notes that: "financial statements issued for users that are unable to demand financial information to meet their specific information needs are general purpose financial statements. Examples of such users are citizens, voters, their representatives and other members of the public. The term 'financial statements' used in this Preface and in the Standards covers all statements and explanatory material which are identified as being part of the financial statements."[9]

Inclusion of budgetary information and other budget related matter in the accounting system and reporting budgetary data to constituents is crucial to improving public sector financial management (transparency). To assure that government officials are held accountable for their budgetary decisions, it is essential that users be informed on the degree by which their government officials were able to operate within the limits of the approved budget.

International Public Sector Accounting Standards[10]

IPSASs deal with issues related to the presentation of annual general purpose financial statements at each level of government (local, state, and national) and for public sector entities other than GBEs. General purpose financial statements include those that are presented separately or within another public document such as an annual report. The objectives of general purpose financial statements are to provide information useful for decision-making, and to demonstrate the accountability of the entity for the resources entrusted to it. IPSAS 1 notes that users include taxpayers and rate payers, members of the Legislature, creditors, suppliers, the media, and employees. Elected representatives act on behalf of their constituents and use the financial statements to hold the government and the civil service to account for the resources that they were allocated to provide the agreed level of goods and services. Where the financial information needs of members of government for these purposes differ from the needs of other users, and where governments are dependent on general purpose financial statements for such information, their information needs should dominate.

In addition, general purpose financial statements can have a predictive or prospective role since they can provide information useful to predict the level of resources required for continued operations. Further, these statements provide users with information indicating whether resources were obtained and used in accordance with the legally adopted budget. Currently, the IPSASs

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8 "Preface to International Public Sector Accounting Standards", Handbook of International Public Sector Accounting Standards (2003 Edition), International Federation of Accountants, p. 18.

9 Ibid, p. 19.

10 Sections from the existing IPSASs pertaining to budgets or budget reporting are identified in Appendix D.

encourage governments to include in the financial statements a comparison of the actual results of operations with the approved budget for the reporting period.[11]

The current IPSASs prescribe standards for the presentation of annual general purpose financial statements on the cash or the accrual basis of accounting. The accrual basis is preferred[12] for the following reasons: improved resource allocation, strengthened accountability over all resources, enhanced transparency on total resource costs of government activities, and more comprehensive view of government's impact on the economy. A Cash Basis IPSAS has been issued to prescribe financial reporting requirements where the countries do not prepare financial statements of public sector entities on the accrual basis. The Cash Basis IPSAS requires an annual Statement of Cash Receipts and Payments. If their financial statements are prepared on the cash basis, the government entities are **encouraged** to transition to the accrual basis as soon as proper procedures and systems can be established.[13]

Recommendation #1: The PSC should issue an IPSAS (or IPSASs) on budget reporting since it falls within the mandate identified in the Preface to the PSC.[14] It may be beneficial to issue separate IPSASs on ex-ante and ex-post budget reports. An IPSAS (or IPSASs) on Budget Reporting will provide guidance on information that should be disclosed in general purpose financial reports about budgetary actions (both legally approved budgets and prospective budgets) at the time of their approval as well as the comparative reports issued as a component of the general purpose financial statements at the end of the fiscal period. The IPSASs should also provide guidance on the format of disclosure.

Budget Formulation and Ex-Ante Reporting

Budget formulation is the practices and concepts that budget professionals use to create and review a budget until enacted into law. Ex-ante budget reporting includes the external reporting of the budget approved by the legislative body at or near the beginning of the fiscal period as well as prospective or forecast budgetary data. The approved budget and forecast budgetary data are generally issued as separate reports at or near the beginning of the fiscal period.

Prospective Financial Information and Medium Term Fiscal Framework (MTFF)—also known as Medium Term Budget Framework (MTBF)

Fiscal targets are now widely accepted as a useful guide to sound public financial management and are increasingly required under such mechanisms as fiscal responsibility/transparency laws. These targets may cover a range of variables (budget balance, net public debt, net worth, etc.) and they are invariably medium term covering more than one year. Given that governments have medium term targets (under a MTFF or other documents), governments are encouraged to report on future projections beyond the current year in their budget reports.

11 Paragraph 22, IPSAS 1, Presentation of Financial Statements (May 2000).

12 Government Finance Statistics Manual, International Monetary Fund (2001).

13 For further guidance, see Study 14—Transition to the Accrual Basis of Accounting: Guidance for Governments and Government Entities, IFAC Public Sector Committee (December 2003).

14 It is interesting to note, at meetings in July 2003 and November 2003, the PSC expressed the view that compliance reporting was in its scope. However, PSC members had different views about an IPSAS on Budgetary Reporting. PSC members agreed not to prejudge the outcome of the research on this subject.

A MTFF includes both revenue and expenditure forecasts. If the forecasts only deal with expenditures, it is referred to as a Medium Term Expenditure Framework (MTEF). To ensure consistency in taxing and spending policies from one fiscal period to another, it is beneficial to have a planning horizon of at least three years. This planning horizon can be assisted by the work of macroeconomists to assure comparability in reporting from country to country. **Accurate accounting systems** are critical to providing good information for computing a country's gross domestic product and other key statistics used by macroeconomists.

Each country hopes to improve their standard of living over time. Dividing GDP by the population is a good guide to measure average living standards. The degree of improvement in the standard of living from year to year is measured by the percentage change in the per capita GDP. Decision makers use this information to develop their taxing and spending policies (i.e., fiscal policy) for future years. Some countries incorporate this information into a MTFF to assist in preparing future budgets. The objectives of a MTFF (as identified by the World Bank[15]) are as follows:

- Improve macroeconomic balance by developing a consistent and realistic resource framework;
- Improve the allocation of resources to strategic priorities between and within sectors;
- Increase commitment to predictability of both policy and funding so that ministries can plan ahead and programs can be sustained; and
- Provide line agencies with a hard budget constraint and increased autonomy, thereby increasing incentives for efficient and effective use of funds.

A MTFF is generally prepared for at least a three-year period. The stages for the preparation and implementation of a MTFF have been identified as follows by the World Bank:[16]

1. Link economic projections to fiscal targets on what is fiscally affordable and construct a macroeconomic model.
2. Perform sector review of ministry objectives, outputs, and activities with agreement on programs and their costs over a three year period.
3. Conduct series of hearings between the Ministry of Finance and sector ministries to go over the outputs of the sector reviews.
4. Develop strategic expenditure framework to provide the basis for the sector expenditure ceilings for the upcoming budget year as well as the two outer years.
5. Ceilings approved by the main decision-making body in government (i.e., Cabinet) in order to make medium term sectoral resource allocations on the basis of affordability and inter-sectoral priorities.
6. Ministries adjust their budget estimates to make them fit within the approved ceilings.

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15 Page 46, Public Expenditure Management Handbook, Poverty Reduction and Economic Management, The World Bank, 1998.

16 Ibid, Pp. 47-52.

7. Revised ministerial budget estimates are reviewed again by the Ministry of Finance and presented to the Cabinet and the Parliament for final approval.

At least one country (New Zealand) requires that prospective financial information be prepared and presented to its constituents.[17] Its objectives are to assist users:

(a) In assessing the entity's prospective financial performance, prospective financial position and prospective cash flows;

(b) By informing them of the entity's actual or future likely compliance with legislation, regulations, common law and contractual arrangements, as these relate to the assessment of the entity's prospective financial performance, prospective financial position and prospective cash flows; and

(c) In making decisions about providing resources to, or doing business with, the entity.

Recommendation #2: An accounting standard should be issued to require that the forecast and other prospective financial information be reported to their constituents in order to keep them informed on future financial implications of government policy. Preparation of a MTFF or other prospective financial information so that the "predictive or prospective role" provided by the general purpose financial statements can be met and one of the purposes of financial statements specified in IPSAS 1[18] can be achieved. The elements of historical financial information used in the preparation of a MTFF and other prospective financial reports primarily include revenue and expense data. In some cases, the value of fixed assets and their age is also included in order to compute the anticipated cost for replacement of those assets and to plan for new construction. In addition, the repayment (both principal and interest) of debt is an essential component of the MTFF and other prospective financial reports. This information is very beneficial to the users in the ongoing debate of government policy. If this recommendation is adopted, issues associated with the recognition and measurement of the data will need to be identified and the extent of external validation by auditors will need to be determined.

Annual or Biennial Budget Formulation

Funds are appropriated on an annual or biennial basis to permit control of funds within a fiscal period. The United Nations Development Program has identified some of the key factors that contribute to making the budget preparation process effective in practice. These are as follows: transparency, management, decentralization, co-ordination and co-operation, integration, flexibility, discipline, link to medium term framework, accountability and credibility, and comprehensive. Specifically, it recommends that the budget contain information on the previous and current years' expenditures. (See Appendix E.)

To permit comparisons between countries, the IMF encourages the use of prescribed codes that assist in computing analytic measures for fiscal policy decisions. The reporting system prescribed by the IMF is a statistical system to measure fiscal performance but it is not an accounting system. The functional classification of expenses is the same as that used by the

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17 Financial Reporting Standard No. 29, Prospective Financial Information, Institute of Chartered Accountants of New Zealand (October 2001).

18 Paragraph 14, IPSAS 1.

United Nations in their System of National Accounts. The breakout of the revenue and expense codes is summarized below:[19]

- Classification of Revenue
  - Taxes
  - Social Contributions
  - Grants
  - Other Revenue
- Economic Classification of Expenses
  - Compensation of Employees
  - Use of Goods and Services
  - Consumption of Fixed Capital
  - Interest
  - Subsidies
  - Grants
  - Social Benefits
  - Other Expenses
- Functional Classification of Expenses
  - General Public Services
  - Defense
  - Public Order and Safety
  - Economic Affairs
  - Environmental Protection
  - Housing and Community Amenities
  - Health
  - Recreation, Culture, and Religion
  - Education
  - Social Protection

Note: Countries and regions (i.e., the European System of Accounts) may provide alternative economic and functional classifications. Although the classifications may differ slightly from those specified above, they can generally be converted to the classifications desired by the IMF and the UN.

In those countries in which a MTFF or other prospective financial information is prepared, the initial efforts to formulate the annual budget and set the spending limits is taken from the

[19] Summarized from pages 178-179, 182-183 of the Government Finance Statistics (GFS) Manual 2001, International Monetary Fund. See http://www.imf.org/external/pubs/ft/gfs/manual/ for detailed breakout.

forecast information for the upcoming budget year. This planning budget is revised, based on input from responsible decision makers (i.e., ministers, etc.), to reflect any major changes in priorities due to changes in economic or political situations. In those countries in which a MTFF or other prospective information is not prepared, a budget call is sent to responsible decision makers in order that they might identify their needs for the upcoming fiscal period.

Historical accounting records are used to identify the revenues received and expenses incurred for each fiscal period. This historical data is critical to assure that proposed budgets are consistent with prior periods and that the proposed budgets might be sustainable in future periods. These records are maintained at a sufficiently low level of detail to establish spending limits by functional and economic expense classifications.

As soon as the decision makers have identified their needs to the Minister of Finance, a series of meetings and hearings are held to give all concerned parties an opportunity to assist in establishing spending priorities for the upcoming budget year. Depending on the amount of revenue anticipated, spending limits are established and the budget is sent to the legislative body for deliberation (with revisions, as necessary) and approval. Once approved, a law is passed that legally authorizes the expenditure of funds for the upcoming fiscal period. If the financial management system is automated, this approved budget is then loaded into the accounting system in order to assure that budget users operate within their authorized budgetary authority and to provide commitment control over expenses.

As a result of the African study mentioned earlier, numerous reforms were proposed. Across all countries included in the study, growing civil society and legislative demand for transparency, access and better results were shown. Given the shift in the political climate towards democratization, the study argues that now is a fortuitous time for budget reforms, provided that they pay attention to the principles of transparency and participation. Although greater civil society and legislative monitoring of budgets is a relatively recent development, their intervention can contribute to modest first steps on the road to more open systems and can help kick-start a virtuous cycle of transparency, participation and better spending results. In addition to recommendations for each country, the study concludes with the following cross-country recommendations for budget reform:

- The improvement of budget documentation is a critical first step. Budget documentation should include fiscal policy statements, explain the policy base of allocation decisions and be framed in the previous years' actual spending and non-financial information.
- Repeal official secrets legislation and replace it with legislation that guarantees appropriate citizen access to state-held information.
- Entrench the provision of comprehensive and timely information on estimated and actual expenditure and revenues in a budget law that also sets out a clear budget process and clarifies roles and responsibilities.
- External reporting during the spending year should be obligatory, including a cash budgeting system. This should include departmental reporting on achievements. If late audit information makes early annual reports at central government and spending agency level unfeasible, interim mechanisms should be created.

- Extra-budgetary spending should be brought onto budget. If this is difficult, comprehensive and accurate information on these activities should be included with the budget.
- The enhancement of external transparency should coincide with efforts to build internal transparency. Often political decision-makers and their administrative advisors make decisions on very imperfect information.
- The capacity of auditors general should be enhanced. Parliamentary capacity to scrutinize budget proposals and oversee implementation should be institutionalized.

Recommendation #3: The accounting standards should require that the legally approved budget be published with the appropriate supporting budget documentation (e.g., assumptions). The following documentation and procedures are suggested**:**

- Clearly identify the assumptions used and their rationale, risks associated with those assumptions, sensitivities, etc.
- Use of asset, liability, net assets, revenue, and expense codes in accordance with IPSASs and statistical classification bases to the maximum extent possible. Although attempts have been made to harmonize the statistical bases with the IPSAS, some differences may exist particularly in respect of the reporting entity. In those instances, the procedures prescribed by the IPSAS should prevail. Further, budgets may be prepared on the basis of programs relevant for financial management and service delivery in some jurisdictions and the need to complete statistical returns should not undermine that role of the budget.
- Preparation of an annual budget in sufficient time to establish spending limits prior to the beginning of the fiscal period. It is expected that the annual budget would use the prior year financial statements in the preparation stage of the budget. As stated in paragraph 74, IPSAS 1, “An entity should be in a position to issue its financial statements within six months of the reporting date.”
- The scope of the budget should be comprehensive including all aid, government business enterprises, revolving funds, income of dedicated funds, etc.

Budget Execution and Control

Budget execution is the management activities that take place from enactment of the budget into law until the end of the fiscal period. Budget control is assuring that the budget is executed within the legal limits established by the legislative body.

Inter-Relationship between Accounting and Budgeting Systems

The World Bank has developed a diagnostic tool (called a Country Financial Accountability Assessment or CFAA) to enhance the Bank’s knowledge of public financial management (PFM) arrangements in client countries.[20] The CFAA supports both

- The Bank’s fiduciary responsibilities by identifying the strengths and weakness of PFM arrangements so that the likelihood that all public funds, including those provided by the Bank and development partners managed through the country’s PFM system, are appropriately managed, and

[20] Guidelines to Staff, Country Financial Accountability Assessment, Financial Management Sector Board, World Bank (March, 2003).

- The Bank's development objectives, by facilitating a common understanding by the borrower, the Bank, and development partners that leads to the design and implementation of capacity-building programs to improve the country's PFM system.

The key issues to be examined in the CFAA in the areas of external fiscal reporting and transparency (including the standards to be used in their preparation—GFS, IPSAS or modifications of either) are identified in Appendix F. Integration between the financial reporting and budgeting systems are essential for budgetary control as explained below.

There is a close relationship between accounting systems and budgetary systems in order to identify whether funds are expended in the manner desired by the legislature. This close relationship has been identified in an OECD document on Best Practices for Budget Transparency. The Best Practices are in three parts: Part I lists the principal budget reports that governments should produce and their general content. Budget reports identified were as follows: the budget, pre-budget report, monthly reports, mid-year report, year-end report, pre-election report, and long-term report; Part II describes specific disclosures to be contained in the reports; and Part III highlights practices for ensuring the integrity of the reports. The budget is identified as the government's key policy document and should include a medium-term perspective illustrating how revenue and expenditure will develop during, at least, the two years beyond the next fisca year. The year-end report is identified as the key accountability document showing compliance with the level of revenue and expenditures authorized by parliament in the budget. The OECD Report recommends that the year-end report be audited by the Supreme Audit Institution and released within six months of the end of the fiscal year. The document further states that "All fiscal reports referred to in these Best Practices should be made publicly available."[21]

The OECD Report also argues it is essential that these systems be integrated to the maximum extent possible. These integrated systems are sometimes referred to as Government Financial Management (GFM) systems. The objectives of a well-performing budget resource allocation and management system are to:

- Control aggregate spending and the deficit;
- Facilitate strategic prioritization of expenditures across policies, programs, and projects for allocative efficiency and equity; and
- Encourage better use of budgeted resources to achieve outcomes and produce outputs at the lowest possible cost.

As explained in a World Bank document,[22] "management of these three objectives is integrated through a perspective that goes beyond the annual budget cycle. This is achieved by linking policy, planning and budgeting in a medium term expenditure framework at both the overall government and sectoral levels. GFM systems provide decision-makers and public sector managers with a set of tools to support these objectives. The architecture of the information systems network is determined by the basic functional processes that public sector managers

21 Par. 3.4, OECD Best Practices for Budget Transparency, 19 September 2000, http://www.oecd.org.

22 Page 9, Information Systems for Government Fiscal Management by Ali Hashim and Bill Allan, The World Bank, 1999.

employ to achieve these objectives and the overall regulatory framework that underpins these processes." (See Appendix G for the basic functional processes including budget preparation, execution, accounting, and fiscal reporting.)

The overall regulatory framework for operating the various component modules of the GFM system consists of the following elements:

- Control Structure—Generally derived from a legislative framework with basic principles laid down in financial provisions in the constitution and laws related to the management of public finances.
- Accounts Classification—The code structure for classification of accounts is a methodology for consistently recording each financial transaction for purposes of financial control and costing as well as economic and statistical analysis. This structure is needed to provide a consistent basis for the following:
    - Consolidating government-wide financial information;
    - Integrating planning, budgeting and accounting;
    - Capturing data at the point of entry throughout the government; and
    - Compiling budget allocations as well as program and project costs within and across various government agencies.
    - Reporting Requirements—Generally specified in two areas: (1) external reporting to provide information to the legislature, the public, and other interested parties, and (2) internal management reporting for government policy makers and managers.

Members of the World Bank and the IMF explain the importance of the relationship between accounting and budgetary information as follows:[23]

> The Treasury System is used to produce periodic fiscal reports that give a consolidated picture of all receipts and expenditures and progress against budget targets. For these reports to be comprehensive, all items of receipts and expenditure need to be captured. The Government Chart of Accounts is the basis of the fiscal reporting process. These include the Fund, organizational, functional and economic classifications structure of the budget and the classification of account groups, assets and liabilities. . . . On the basis of this data, the MOF can prepare overall fiscal reports that compare actual expenses and receipts with the budget estimates. These reports provide a status report and recommendations and action plans for corrective action during the course of the year.

Recommendation #4: The accounting standards should be broad enough to support the integration of budgetary and accounting systems through the use of budgetary accounting procedures. It may be beneficial to issue a separate IPSAS on budgetary accounting procedures. Budgetary accounting procedures may include separate accounts for estimated revenues, appropriations, allotments, allocations, and commitments. The elements of financial information (especially revenue and expenses) used in the accounting system should be the same

[23] Page 176, Treasury Reference Model by Ali Hashim (World Bank) and Bill Allan (IMF), http://www1.worldbank.org/public sector/pe/trmodel.htm (3/14/2001).

as that used in the budgeting system in order to compare the results of operations with the approved budget. For maximum benefit, these comparative results should be reported in the general purpose financial statements although such comparative information is not currently required by the IPSASs. This does not mean that the budgetary system and the accounting system need to be on the same basis. It does mean that the accounting system needs to support the preparation of a comparative statement on the same basis as the budgetary system. For example, if a cash budget is approved by the legislative body and the accounting system is on an accrual basis, the revenue and expenses in the accounting system would need to be reported in the comparative statement on the cash basis in order to be comparable to the budgetary data.

Budgetary Control

To assure that spending limits are not exceeded, the approved budget is entered into the accounting system at the beginning of the fiscal period at the level of control desired (i.e., by economic and functional expense classifications) in a fully integrated financial management system. Then, as transactions occur, the actual revenue and expenses can be compared to the budgeted revenues and expenses in order to provide assurance that the spending limits have not been exceeded. For those budgetary systems that are not well integrated with the accounting module, a separate budget or funds control module is often maintained. In addition, a separate cash management module is used to assure that cash is available to compensate employees or pay invoices when payment is due. Consequently, proper cash planning is critical to the overall management process.

Compensation of employees (an economic expense classification in GFSM 2001) is generally the largest recurring expense item in any government. Funds are set aside in the approved budget to assure that sufficient funds (by functional expense classification) are available for periodic payment of employees. As actual payrolls are processed, the financial managers within each function can monitor this economic expense and be assured that the expense will not exceed the approved levels during the fiscal period.

Repayment (both principal and interest) of debt is often another large outlay of funds. Funds are set aside in the approved budget for this purpose. Fiscal discipline by the financial managers in their respective areas of responsibility is critical in order to assure that sufficient funds are available for payment of debt when due. In this manner, the country is able to maintain a good credit rating that will generally contribute to lower interest payments on future debt.

The use of goods and services, as well as expenditures for capital projects, is also budgeted at the beginning of each fiscal period. To assure that these spending limits are not exceeded, some countries use “commitment” accounting procedures. This technique permits a financial manager to compare budgetary fund availability to the anticipated expenses for the goods or services or the approved budget for capital projects **prior to** the release of a purchase order or a contract. Once approved and released, the financial manager can be assured that budgetary funds will be available for the payment of the goods or services at the time they are received or the payment on capital projects when due. There is some inconsistency throughout the world in the use of “commitment” accounting procedures. To clarify these procedures and lessen the confusion over the terminology, see Appendix H for a more complete discussion of this technique as explained by IFAC in a previous study.[24]

Recommendation #5: In relevant studies and guidance, the PSC should acknowledge and encourage the use of commitment accounting procedures intended to assure that budgetary funds are available prior to release of a purchase order or contract. Although budgetary accounting procedures are not presently included in an accounting standard, effective use of commitment accounting procedures will lessen the explanatory notes at the end of the fiscal period when actual expenditures exceed the approved limits. Further, these procedures can be beneficial in a budgetary system for the acquisition of infrastructure and military special assets, as well as the control of government grants.

Ex-Post Budget Reports

Ex-post budget reporting would include external reporting of the financial activities relative to the enacted budget for the fiscal period until the final audit after the end of the fiscal period. The budget to actual comparative statement is generally issued as a component of the historical financial statements.

Part of General Purpose Financial Statements

In a prior IFAC study, the following user needs[25] were noted:

> "49. Although the users described above have a range of information needs, and some groups may place a higher or lower priority on certain types of information than other groups, the user groups also have similar information needs. The PSC considers that, taken as a collective group, users expect that governmental financial reports will help them to:
>
> - Assess the sources and types of revenues;
> - Assess the allocation of and use of resources;
> - Assess the extent to which revenues were sufficient to cover costs of operations;
> - Predict the timing and volume of cash flows and future cash and borrowing requirements;
> - Assess the government's long term ability to meet financial obligations, both short and long term;
> - Assess the government's or entity's overall financial condition;
> - Provide the public with information concerning those assets held on behalf of taxpayers, specifically information on ownership and control, composition, condition and maintenance;

24 Study 11, Government Financial Reporting, May 2000. IFAC Public Sector Committee.
25 Ibid. Pp. 11-12.

- Assess the financial performance of the government or entity in its use of resources;
- Assess the economic impact of the government on the economy;
- Evaluate government spending options and priorities;
- **assess whether resources were used in accordance with legally mandated budgets and other legislative and related authorities such as legal and contractual conditions and constraints;** and
- assess the government's or entity's stewardship over the custody and maintenance of resources."

[emphasis added]

The present IPSASs **encourage** comparisons with budget but do not specify any financial reports that would satisfy user needs in assessing "whether resources were used in accordance with legally mandated budgets and other legislative and related authorities such as legal and contractual conditions and constraints." To fill this void and provide a higher degree of transparency, almost all countries prepare and publish "Budget to Actual Comparative Statements." Differences between the actual expenses and the final (or original) budget are reflected in the comparative statements in order to assist the user in determining how close the government came to meeting the budget expectations. The budgetary comparisons are generally made at the major levels of control as approved by the legislature. Since approved budgets are considered law in many countries, explanations are generally required in those instances where expenses exceed budgetary authority. Guidance in the present IPSAS[26] is as follows:

> General purpose financial statements can also have a predictive or prospective role, providing information useful in predicting the level of resources required for continued operations, the resources that may be generated by continued operations, and the associated risks and uncertainties. Financial reporting **may** also provide users with information (emphasis added):
>
> (a) indicating whether resources were obtained and used in accordance with the legally adopted budget, and
>
> (b) indicating whether resources were obtained and used in accordance with legal and contractual requirements, including financial limits established by appropriate legislative authorities.

The scope of general purpose financial statements is usually clearly designed and defined in the statements (with a list of entities covered by the statements, and the description of the method used to built that list). It is not always the case for budgetary reports, which are not necessarily based on the "control" approach described in IPSAS 6. The budget scope can be broader or narrower than the scope of the financial statements based on the "control" approach, to the extent that the budget reflects the financial relationships between the government and a range of national or international entities. Moreover, budgetary reports don't deal with consolidation aspects. Sometimes national accounting systems are also built on a different basis, concerning the links between governments and other entities. In the event of conflict between the budgetary

[26] Paragraph 14, IPSAS 1, Presentation of Financial Statements.

reporting system and the IPSAS, the IPSAS definition of a reporting entity would be expected to prevail. However, the budget to actual comparative statement would need to be prepared on the basis of the approved budget.

Recommendation #6: Ex-post budget reports reflecting budget to actual comparisons should be part of the general purpose financial statements issued at the end of the fiscal period for each reporting entity at each level of government. Inclusion of the budgetary information in the general purpose financial statements will "meet the needs of users who are not in a position to demand reports tailored to meet their specific information needs."[27] While it is appropriate to advocate inclusion in general purpose financial statements of comparisons between budget and actual data, it is acknowledged that further guidance is needed in the following areas:

- How budget data should be summarized to avoid information overload. To ensure that reports are not too voluminous, any future IPSAS should specify that only major classes be included in the comparative reports that would include the primary and secondary levels of control identified by the legislature. This would apply to the whole-of-government statements as well as the statements covering general and sub-national governments.
- How an IPSAS should deal with comparisons if the scope of the budget entity and the IPSAS reporting entity differ. The reporting entity needs to be clearly defined so that the budget to actual comparisons relate to the same entity.
- How extra-budgetary funds that may be excluded in government financial statements should be handled. It is essential that comprehensive budgets be presented in order to reflect the actual results of operations as compared to the budgetary authority.
- How an IPSAS should deal with comparisons if different measurement bases were adopted for such items as inventory, investments, and provisions in budget document and financial reports.

Format of Comparative Statement

Since budgets are prepared in advance of the current fiscal year, natural disasters, political, or economic conditions may dictate a need for revisions to the initially approved budget during the fiscal year. Consequently, most countries identify those procedures necessary for budgetary revisions. In some countries, this authority is delegated to the Minister of Finance (within specified limits); in other countries, the revisions must be approved by the legislature. In some of those countries where comparative statements are encouraged (see Appendix J for an illustration from the United States), the initial budget as approved by legislation is expected to be included in the comparative statement along with the final, revised approved budget.

Guidance in the present IPSAS[28] is as follows:

> Public sector entities are typically subject to budgetary limits in the form of appropriations or budget authorizations (or equivalent), which may be given effect through authorizing legislation. General purpose financial reporting by public sector entities may provide information on whether resources

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[27] Paragraph 2, IPSAS 1.

[28] Paragraph 22, IPSAS 1, Presentation of Financial Statements.

were obtained and used in accordance with the legally adopted budget**. Where the financial statements and the budget are on the same basis of accounting, this Standard encourages the inclusion in the financial statements of a comparison with the budgeted amounts for the reporting period.** *(Emphasis added)*. Reporting against budgets may be presented in various different ways, including:

(a) the use of a columnar format for the financial statements, with separate columns for budgeted amounts and actual amounts. A column showing any variances from the budget or appropriation may also be presented, for completeness; and

(b) a statement by the individual(s) responsible for the preparation of the financial statements that the budgeted amounts have not been exceeded. If any budgeted amounts or appropriations have been exceeded, or expenses incurred without appropriation or other form of authority, then details may be disclosed by way of footnote to the relevant item in the financial statements.

Recommendation #7: The Comparative Budget to Actual Statement should include the original budget as approved by the legislative body as well as the final adopted budget. Significant variances should be appropriately identified and justified. This would include comparison of actual expenditure and income with the budgeted amounts agreed by parliament, variances for each line between these two items considering budget assumptions, and explanations for all variances (positive and negative) above a certain significant level (e.g. 5%). Clarification is needed in the following areas:

- Whether comparisons of actual should be made with original and/or revised budgets (and which revision if the budget was revised periodically during the reporting period to reflect changing policies, economic environment and experience);
- What impact a change in policy settings might have if comparisons were to be made against original budgets and how such changes should be dealt with if comparisons were to be made with revised budgets;

Reconciling Budgetary Basis with Accounting Basis

Some countries that have adopted the accrual basis of accounting as their generally accepted accounting principle (GAAP) continue to prepare their budgets on the cash basis. If the accounting basis (i.e., accrual) is different from the budgetary basis (i.e., cash), the comparative statement is generally prepared on the budgetary basis. A reconciliation is made so that the reader is informed about the differences between the budgetary and accounting balances in the general purpose financial statements. Some of the more common differences are identified in Appendix I. An example from the US of a comparative statement is shown in Appendix J. In addition, the UK includes the requirement for a “reconciliation of resources to net cash requirement” in their Summary of Resource Outturn Report.[29] The present IPSASs do not specify the action to be taken in those instances where the budget and accounting are on different bases. However, a similar reconciling statement is encouraged in IPSAS 2 when the Cash Flow Statement is prepared using the direct method. An illustrative note (reproduced below) is

[29] Paragraph 12.1.12, Schedule 1 – Summary of Resource Outturn, UK Accounting Manual. Schedule 1 is the parliamentary control schedule comparing outturn with Estimate for both resource expenditure and the overall cash requirement. (See http://www.accounting-manual.gov.uk)

included in the Appendix to IPSAS 2 and reflects a reconciliation of the surplus/deficit from ordinary activities with the net cash flow from operating activities.[30]

Notes to the Direct Method Cash Flow Statement in the Appendix

(c) Reconciliation of Net Cash Flows from Operating Activities to Net Surplus/(Deficit) from Ordinary Activities (in thousands of currency units)

	20X2	***20X1***
Surplus/(deficit) from ordinary activities	*X*	*X*
Non-cash movements	*X*	*X*
Depreciation	*X*	*X*
Amortization	*X*	*X*
Increase in provision for doubtful debts	*X*	*X*
Increase in payables	*X*	*X*
Increase in borrowings	*X*	*X*
Increase in provisions relating to employee costs	*X*	*X*
(Gains)/losses on sale of property, plant, and equipment	*(X)*	*(X)*
(Gains)/losses on sale of investments	*(X)*	*(X)*
Increase in other current assets	*(X)*	*(X)*
Increase in investments due to revaluation	*(X)*	*(X)*
Increase in receivables	*(X)*	*(X)*
Extraordinary item (that falls within the definition of operating activities)	*(X)*	
Net cash flows from operating activities	*X*	*X*

Recommendation #8: Governments should be encouraged to operate their budgeting and accounting systems on the same basis. If the budgetary system is on a different basis than the accounting system, a statement should be developed to reconcile key differences between the two systems. Since the accrual financial reports include cash flow statements, a reconciliation may be achieved by ensuring these cash flow statements articulate with the cash budget. In those instances where the budgetary system is transitioning to accrual budgeting, a separate reconciliation procedure with the accrual financial reports will be necessary. Further guidance is needed on how an IPSAS should deal with comparisons if differences in the basis of accounting were adopted in budget and historical financial reports.

Qualitative Characteristics of Financial Reporting

Budget reports would be expected to meet the qualitative characteristics of financial reporting specified in IPSAS 1.[31] These are discussed below:

Understandability

Budget reports should be clearly and concisely presented in sufficient detail in order for users to comprehend its meaning. Taxing and spending policies of the government should be adequately

[30] Paragraph 29, IPSAS 2 and Note (c), Appendix, p. 112, Cash Flow Statements.
[31] Appendix 2, IPSAS 1 – Presentation of Financial Statements.

explained in the budget reports so that the average user, after due study, can apprehend the economic impact of the entity's activities and the environment in which it operates. Complex economic concepts should not be excluded from the financial statements merely on the grounds that it may be too difficult for certain users to understand.

Relevance

Information included in the budget reports should be provided in a timely manner and relevant to the decision-making needs of users by helping them evaluate past, present, or future events. To prevent information overload, only the information that is material to the user's needs should be included in the budget reports. Materiality implies that omission or misstatement of information could influence the decisions of users or assessments made on the basis of the budget reports. For example, information about financial position and past performance is frequently used as the basis for predicting future financial actions in which users are directly interested. The ability to make predictions on budget reports is enhanced, by the manner in which information on past transactions and events is displayed.

Reliability

To be reliable, budget reports must be free from material error and bias so that they can be depended on by users to represent faithfully that which they purport to represent. This implies that information in budget reports be complete and presented in accordance with their substance and economic reality; not merely their legal form. Further, the budget reports should be free from bias and presented in such a manner that a user would not be unduly influenced in making a decision or judgment in order to achieve a predetermined result or outcome. In addition, preparers of budget reports do have to contend with the uncertainties that inevitably surround many events and circumstances in which budget forecasts are made. Consequently, prudent judgment needs to be exercised in making the estimates required under conditions of uncertainty.

Comparability

Users must be able to compare the budget reports of a governmental entity through time in order to identify trends in their financial position and performance. In addition, users must be able to compare the budget reports of different governmental entities in order to evaluate their relative financial position, performance, and changes in net assets. An important implication of comparability is that users be informed of the accounting policies employed in the preparation of the budget reports, any changes in those policies and the effects of such changes.

Constraints on Relevant and Reliable Information

To be useful, budget reports must be presented in a timely manner. All information needed to prepare complete and accurate budget reports may not be available in time for preparation of the budget or legislative action may delay the approval of the budget. Conversely, if reporting is delayed until all aspects are known, the information may be highly reliable but of little use to users who have had to make decisions in the interim. In achieving a balance between relevance and reliability, the overriding consideration is how best to satisfy the decision-making needs of users. In addition, a balance must be maintained between benefit and cost to assure that the benefits derived from the budget reports do not exceed the cost of providing it. Further, professional judgment must be applied to achieve a balance between the qualitative characteristics in order to meet the objectives of the budget reports.

Recommendation #9: Budget reports should meet the qualitative characteristics (understandability, relevance, reliability, and comparability) of financial reporting specified in IPSAS 1. In order to assure that these qualitative characteristics are achieved, external validation (after considering the constraints on relevant and reliable information) of the budgetary data by the external auditor will be necessary.

Developing a Conceptual Framework

As this research progressed, it became obvious that a conceptual framework was needed on which to build an IPSAS or IPSASs on Budget Reporting. Such a framework could identify how a new IPSAS (or IPSASs) would be used and by whom, as well as specify what the new IPSAS would do and what specific guidance it would provide. An attempt in made in this section to discuss some of the issues for such a framework.

The International Accounting Standards Board has not established accounting standards for budgetary reporting by private sector entities. Budgetary reporting in the public sector is different from and more significant than budgets of commercial entities for many of the following reasons:

- Because many governments deal with non-exchange transactions, financial measures must be combined with non-financial performance measures to provide a comprehensive model. Budget standards must recognize the importance of such non-financial measures and address how they are to be incorporated within budget reporting. In the public sector, planned income and expenditure in future years together with information on unfunded current and future priorities is as (if not more) important as historical actual to budget reports. The attainment of projected service delivery, measured against predetermined objectives, is also central to performance evaluation. Productivity in delivering outputs in support of desired outcomes should be and can be measured by setting measurable objectives in advance.
- Investment in and lending to commercial entities is voluntary with the major financial consequences of the actions of those entities impacting on investors, lenders, employees, customers, and suppliers. While governments may borrow, most funding comes from taxes, fines and fees and is not usually provided voluntarily. Therefore, stakeholders in government encompass a much broader range of constituents and the decisions made impact on current and future generations. Consequently, information needs, on a planned future, are as important as information needs on historical actual to budget performance.
- Options for the volume, nature and form of delivery of services in the public sector are also wider and different than the private sector—for example, additional funds may be collected to provide addition services. Alternatively, current collections and services may be reduced. Possible service providers include the public and private sectors as well as Public/Private Partnerships. The spending level, in itself, does not guarantee service delivery and thus the provision of performance indicators on preset measurable objectives are needed in much the same way as private sector shareholders may look to an Earnings

> Per Share indicator. Budget reporting is not only about finance. It is also about meeting measurable performance promises and about offering choice, in the prioritization of the use of available funding, with the medium term fiscal framework.

There is then a sound basis for acknowledging that budget reporting (both ex-ante and ex-post) fits within the public sector financial reporting conceptual framework, and should be developed as that framework is developed. Budget reporting on historical and future budget allocations enables stakeholder involvement in exercising choice in the setting of equitable share slices to ministries. The reporting of budget needs, marginal priorities, and unfunded priorities support the revenue collection decision. These and other characteristics could form the basis for identifying issues that need to be addressed in budget reporting standards. The matrix in Appendix K is the beginning of such an exercise.

At the present time, IPSAS 1 only encourages countries to prepare budget to actual comparative schedules. Many countries routinely prepare such schedules for budgetary control purposes. If the comparative schedules were required as part of the general purpose financial statements, they would require external validation. This would provide users of the financial statements with the assurance that the budgetary information is fairly presented and that budgetary authority had not been exceeded unless otherwise annotated.

PSC Study 14 provides guidance on migration from a cash to an accrual basis of financial reporting. A similar publication could provide guidance on the “reform path” to assist countries further develop their budget formulation and execution processes and to adopt “best practices” as recommended and updated, from time to time. Such a guide would give leadership, alignment and direction, as well as promote the achievement of the objectives and qualitative characteristics set out earlier in this Research Report.

The allocation of funding between governmental units is mostly a subjective decision driven by policy and political priority on disparate needs, productivity improvements, and functionality growth. Disclosure of information about future financial commitments and financial prioritization decisions could usefully be reported upon by the presentation of a management report. A report of progress against the “Code of Good Practices on Fiscal Transparency” as presented in Appendix B and the “Best Practices in Public Budgeting” as presented in Appendix C of this Research Report could also usefully be included in such a management report.

Recommendation #10: Budget reporting should be incorporated into the conceptual framework for IPSASs. The recommendation in this Research Study to require the reporting of financial actual to budget performance is but one aspect of concern to stakeholders on budget matters. Reporting on the planned future is as important as reporting on the past. A case study on South Africa has been published by the International Consortium of Governmental Financial Managers[32] to demonstrate the actions taken in one country to strengthen budget reporting.

[32] See http://www.icgfm.org/digest.htm, Vol. IV, No. 1, 2004 for article by Alan Mackenzie titled “Case Study on South Africa.”

Issues Raised by Steering Committee Members

Definition of Budget Reporting.

There was a difference of views among Steering Committee members as to what was meant by budget reporting. Some members felt that budget reporting included the budgets submitted to and approved by the legislative body during the budget formulation stage. Some members believed that budget reporting included the budget to actual comparisons made during the fiscal period in the budget execution stage. Other members felt that budget reporting only related to the final approved budget as compared to the actual revenues and expenses for the entire budgetary period (the budget reporting stage). While conducting due process through Invitations to Comment or Exposure Drafts for an IPSAS (or IPSASs) on Budgetary Reporting, these positions need to be clarified.

Inclusion of Ex-ante Budget Reports in an IPSAS.

The position taken in this Research Report is that budget reporting referred to the external reporting of the budget approved by the legislative body at or near the beginning of the fiscal period as well as the external reporting of the financial activities relative to the enacted budget for the fiscal period until the final audit after the end of the fiscal period. The approved budget is generally issued as a separate report at or near the beginning of the fiscal period while the budget to actual comparative statement is generally issued as a component of the historical financial statements.

Coverage of Budgetary Execution and Control Procedures.

Current best practices in budget formulation, execution and reporting among international financial institutions and developed countries indicate a high degree of consistency in those practices. However, the Steering Committee members generally felt that the budget formulation and execution practices reflect significantly different administrative arrangements as well as political, institutional and cultural systems and processes. Consequently, accounting standards for budget formulation and execution would probably not be beneficial except to ensure that data collected through the use of budgetary accounting procedures will support the preparation of the budget with the financial information desired for comparison to actual performance. Further, the use of commitment accounting procedures for budgetary control purposes should be clarified.

Inclusion of Ex-post Budget Reports in an IPSAS and Format of Comparative Statements.

There was a high degree of consensus among Steering Committee members for an accounting standard on ex-post budget reporting. Further, it was believed that such a standard falls within PSC’s mandate for general purpose financial statements and that it meets the qualitative characteristics of financial reporting (i.e., understandability, relevance, reliability, comparability, and constraints on relevant and reliable information). However, the format of such a statement needs to be clarified.

Country specific laws[33] and accounting standard setters (i.e., Croatia, France, Ghana, Honduras, Nigeria, Sweden, Tanzania, Uganda, United Kingdom, United States and many others) encourage the preparation of comparative "budget to actual" financial statements. In addition, such a standard would permit comparability of budget reports over time and between governments. For such comparisons to be beneficial, disclosures in the general purpose financial statements would need to identify the basis of accounting used for the budgetary reports and whether they were in compliance with the cash or accrual IPSASs. Additional information would be needed to identify the government business enterprises included in the budget, as well as the functions (identified in the GFS Manual) included within general government.

Reconciling Budgetary Basis and Accounting Basis Where Differences Exist.

In those instances where the budget is prepared on a basis (i.e., cash) different than the accounting basis (i.e., accrual), the Steering Committee members believed the proposed accounting standard should identify the need for a reconciliation between the cash increase/(decrease) projected in the budgetary report and the net surplus/(deficit) reflected in the Statement of Financial Performance. Such a reconciliation would disclose the cause for the differences between the cash and accrual basis of accounting. However, there was no consensus that the budgetary reports should address the recognition and measurement requirements of the existing IPSASs in the budget context.

Assuring That Qualitative Characteristics of Financial Reporting Are Met.

The Steering Committee members felt that the standards would need to be explicit enough to provide guidance to preparers of budget reports that will meet the qualitative characteristics identified in IPSAS 1. These budget reports could be subject to external audit by the auditor if specified as general purpose financial statements.

Developing a Conceptual Framework.

Substantial input was provided by Steering Committee members to assure that budget reporting was incorporated into a conceptual framework for IPSASs. Such a framework would then provide the guidance needed in the development of future standards pertaining to the extremely critical area of budget reporting.

[33] See Appendix L for highlights of the Budgetary Law in Sweden, Appendix M for Budget Preparation Procedures in Denmark, and Appendix N for Budget Procedures in France.

Research Report
Budget Reporting
Appendices

APPENDIX A

TERMS OF REFERENCE

INTERNATIONAL FEDERATION OF ACCOUNTANTS PUBLIC SECTOR COMMITTEE STEERING COMMITTEE PROJECT BRIEF

Budget Reporting – Stage 1

Background

The Budget

Most, but not all, governments prepare and issue as public documents, or otherwise make publicly available, their annual financial budgets. For many/most jurisdictions these budgets are prepared on a cash or near cash basis.

The budget documents are widely distributed and promoted. They reflect the financial characteristics of the government's plans for the forthcoming period and are used for analysis of the consequences of those plans for the economy. Making budget data publicly available is necessary to enable transparent reporting of the government's financial intentions. Reporting period results against the budget for the same period is a necessary component of any accountability regime. It enables the Government to communicate to its constituents the extent to which performance and plan coincide and to explain any differences therein.

In many respects, and for many external users, the budget documents are the most important financial statements issued by governments.

The budget also serves as a key tool for financial management and control, and is the central component of the process that provides for government and parliamentary (or similar) oversight of the financial dimensions of operations.

Government budgets are approved by the legislature and compliance is a legal matter. While administrative arrangements can differ from jurisdiction to jurisdiction, in most cases, spending units have no authority to commit or spend government funds until the legislation imparting spending authority (the budget) has been passed by the legislature.

International Public Sector Accounting Standards

International Public Sector Accounting Standards (IPSASs) deal with issues related to the presentation of annual general purpose financial statements. General purpose financial statements are those intended to meet the needs of users who are not in a position to demand reports tailored to meet their specific information needs. Users of general purpose financial statements include taxpayers and ratepayers, members of the legislature, creditors, suppliers, the media, and employees. General purpose financial statements include those that are presented separately or within another public document such as an annual report. The objectives of general purpose financial statements are to provide information useful for decision-making, and to demonstrate the accountability of the entity for the resources entrusted to it by:

The Issues

(a) Whether Budget Reporting is an issue that the PSC should deal with

The IPSASs currently on issue do not address the presentation of budgetary/forecast financial information, nor require the disclosure of information that enables users to determine whether actual financial results are broadly consistent with previously issued budgets or forecasts.

Given the widespread practice in the public sector of publicly reporting and commenting on budgetary information, a strong case can be made that government budgets are general purpose financial statements (see above) and there is a need for an IPSAS to be developed on the financial reporting of budget information.

While there may be strong support for such an IPSAS, there are different views on:

- Whether the preparation of such an IPSAS is within the mandate of the PSC; and
- If within the PSC's mandate, the matters that should be dealt with by such an IPSAS and the nature and extent of its "requirements."

(b) The nature of any IPSAS that might be developed

As noted below, there are also differing views and arguments on the matters that should be dealt with by such an IPSAS, and the nature and extent of the requirements of any IPSAS.

Budget Formulation

Some may be of the view that in the interests of better financial management the PSC should issue an IPSAS, or at least a best practice guide, on matters including:

- Budget formulation, definition and classification; and
- Budget reporting and use as a management tool.

However, others note that such an exercise is unlikely to be practicable given that budget formulation requirements and practices are developed within a legislative framework and reflect different administrative arrangements and political, institutional and cultural systems and processes.

General Purpose Financial Reporting–Presentation

Some are of the view that an IPSAS should not deal with issues of budget formulation or classification for internal financial management purpose. Rather it would deal only with:

- How budget data should be presented in budget reports that posses the characteristics of general purpose financial statements as noted above; and
- The relationship between budget reports and historical financial statements and how budget execution should be reported in historical financial statements.

An IPSAS developed on this basis could include requirements directed at such matters as:

- Ensuring that the principles underlying the preparation of the budget were clearly communicated to readers, including;
  - clear explanations of the scope of the budget including whether, for example, the budget encompassed all government operations or only those traditionally designated as "general government" in GFS or similar statistical classifications;
  - whether the budget was prepared on a cash, accrual or other basis; and
  - whether the principles adopted for recognition, classification and disclosure in the budget papers reflected those in the cash or accrual IPSASs;
- Enhancing the comparability of budget reports over time and between governments (or in enabling users to identify the major sources and effects of differences);
- Enhancing the comparability of the budget with historical financial reports encompassing the budget period.

General Purpose Financial Reporting **– Recognition and Measurement Rules**

Some are of the view that an IPSAS on presentation of budget reporting should go further and deal with the application of the recognition and measurement requirements of the existing IPSASs in the budget context. The budget reporting IPSAS would then:

- Deal only with general purpose budget reports;
- In respect of budgets prepared on the accruals basis, include requirements on the application of the definition and recognition criteria for assets, liabilities, revenues and expenses in "forward" budgets, the presentation of such information and related disclosures; and
- In respect of budgets prepared on the cash basis, include requirements on the basis on which projected cash receipts and payments should be included in the budget report, the presentation of that report and the additional disclosures that are required and encouraged.

Project Objectives

The Project is to be developed in two stages as follows.

Stage 1

The preparation of a research report to identify:

- Current best practices in budget formulation and reporting under differing budget models and government administrative arrangements;
- Whether the development of an IPSAS on budget reporting and/or other budget related matters falls within the PSC's mandate;
- Notwithstanding the above, whether there is any precedent, and or arguments, for an accounting standards setter to deal with budget reporting issues; and
- If an IPSAS on budget reporting (or other budget related) matters is to be prepared, the matters which should appropriately be dealt with by that IPSAS.

Stage 2

Based on the results of Stage 1 above, and with the agreement of the PSC, prepare an Exposure Draft of an IPSAS.

The specific matters to be addressed in Stage 2 will not be developed until the results of Stage 1 emerge.

Steering Committee

A Steering Committee will be established to assist in the progress of this matter.

The stages in the development of the IPSAS, the process to be adopted by the Steering Committee, the responsibilities of the Steering Committee and its relationship to the PSC are outlined in *PSC Steering Committees: Terms of Reference and Operating Procedures*.

The issues identified are intended to serve as a broad guide to the Steering Committee to assist it in scoping its task. These matters may be varied by the Steering Committee with the agreement of the PSC. The PSC acknowledges that as the Steering Committee researches the issue in depth and develops its guidance it may determine that certain matters identified should not be further progressed at this time and may identify other matters that will need to be dealt with.

It is anticipated that the Steering Committee will not formally meet during stage 1 of the project but will conduct its business electronically.

Project Timetable

The Project is to be developed in two stages as follows.

Stage 1

2003 Complete Research Report.

Stage 2

2004 Subject to recommendations of the Research Report, commence development of Exposure Draft. Issue and review responses to Exposure Draft and develop IPSAS.

2005 Issue IPSAS, as appropriate.

Matters to be addressed

Stage 1

The examination of the relationship of budget reporting to the PSC’s mandate will include an analysis of PSC terms of reference and a review of what other standards setters do in this area: GASB, FASAB, AASB, NZ-FRSB, IASB, UK Treasury etc. This would include any initiatives/plans in respect of reporting projected/prospective financial information.

In the first instance, the survey countries will be focused based on advice from appropriate sources of instances of “best practice.” The first round survey will include the following countries (a selection of countries from the PSC members: USA, UK, France, Norway, Hong Kong, Germany or Netherlands, and Australia or New Zealand. Advice from USAID, OECD etc.) Then one developing country influenced by those models.

APPENDIX B

IMF CODE OF GOOD PRACTICES ON FISCAL TRANSPARENCY

Extracted from IMF website— http://www.imf.org/external/np/fad/trans/index.htm.

Countries are encouraged to implement the following Code of Good Practices on Fiscal Transparency. The Code is based around the following key objectives: roles and responsibilities in government should be clear; information on government activities should be provided to the public; budget preparation, execution, and reporting should be undertaken in an open manner; and fiscal information should attain widely accepted standards of data quality and be subject to independent assurances of integrity.

The Code sets out what governments should do to meet these objectives in terms of principles and practices. These principles and practices are distilled from the IMF's knowledge of fiscal management practices in member countries. The Code will facilitate surveillance of economic policies by country authorities, financial markets, and international institutions. Guidelines to the implementation of the Code are provided in a supporting manual, which has been revised in line with the changes in the Code, and updated in a number of areas.

The Code acknowledges diversity across countries in fiscal management systems and in cultural, constitutional, and legal environments, as well as differences across countries in the technical and administrative capacity to improve transparency. Most countries have scope for improvement in some aspects of fiscal transparency covered in the Code. Diversity and differences across countries, however, inevitably imply that many countries may not be able to move quickly to implement the Code. Moreover, it is recognized that there may be a need for technical assistance if existing fiscal management practices are to be changed. The IMF, together with other international organizations, will give some priority to providing technical assistance to those countries that need help and are strongly committed to improving fiscal transparency.

Revised Code of Good Practices on Fiscal Transparency

I. Clarity of Roles and Responsibilities

1.1 **The government sector should be distinguished from the rest of the public sector and from the rest of the economy, and policy and management roles within the public sector should be clear and publicly disclosed.**

1.1.1 The structure and functions of government should be clearly specified.

1.1.2 The responsibilities of different levels of government, and of the executive branch, the legislative branch, and the judiciary, should be well defined.

1.1.3 Clear mechanisms for the coordination and management of budgetary and extrabudgetary activities should be established.

1.1.4 Relations between the government and nongovernment public sector agencies (i.e., the central bank, public financial institutions, and nonfinancial public enterprises) should be based on clear arrangements.

1.1.5 Government involvement in the private sector (e.g., through regulation and equity ownership) should be conducted in an open and public manner, and on the basis of clear rules and procedures that are applied in a nondiscriminatory way.

1.2 **There should be a clear legal and administrative framework for fiscal management.**

1.2.1 Any commitment or expenditure of public funds should be governed by comprehensive budget laws and openly available administrative rules.

1.2.2 Taxes, duties, fees, and charges should have an explicit legal basis. Tax laws and regulations should be easily accessible and understandable, and clear criteria should guide any administrative discretion in their application.

1.2.3 Ethical standards of behavior for public servants should be clear and well publicized.

II. Public Availability of Information

2.1 **The public should be provided with full information on the past, current, and projected fiscal activity of government.**

2.1.1 The budget documentation, final accounts, and other fiscal reports for the public should cover all budgetary and extra-budgetary activities of the central government, and the consolidated fiscal position of the central government should be published.

2.1.2 Information comparable to that in the annual budget should be provided for the outturns of the two preceding fiscal years, together with forecasts of the main budget aggregates for two years following the budget.

2.1.3 Statements describing the nature and fiscal significance of central government contingent liabilities and tax expenditures, and of quasi-fiscal activities, should be part of the budget documentation.

2.1.4 The central government should publish full information on the level and composition of its debt and financial assets.

2.1.5 Where sub-national levels of government are significant, their combined fiscal position and the consolidated fiscal position of the general government should be published.

2.2 **A commitment should be made to the timely publication of fiscal information.**

2.2.1 The publication of fiscal information should be a legal obligation of government.

2.2.2 Advance release date calendars for fiscal information should be announced.

III. Open Budget Preparation, Execution, and Reporting

3.1 **The budget documentation should specify fiscal policy objectives, the macroeconomic framework, the policy basis for the budget, and identifiable major fiscal risks.**

3.1.1 A statement of fiscal policy objectives and an assessment of fiscal sustainability should provide the framework for the annual budget.

3.1.2 Any fiscal rules that have been adopted (e.g., a balanced budget requirement or borrowing limits for sub-national levels of government) should be clearly specified.

3.1.3 The annual budget should be prepared and presented within a comprehensive and consistent quantitative macroeconomic framework, and the main assumptions underlying the budget should be provided.

3.1.4 New policies being introduced in the annual budget should be clearly described.

3.1.5 Major fiscal risks should be identified and quantified where possible, including variations in economic assumptions and the uncertain costs of specific expenditure commitments (e.g., financial restructuring).

3.2 **Budget information should be presented in a way that facilitates policy analysis and promotes accountability.**

3.2.1 Budget data should be reported on a gross basis, distinguishing revenue, expenditure, and financing, with expenditure classified by economic, functional, and administrative category. Data on extra-budgetary activities should be reported on the same basis.

3.2.2 A statement of objectives to be achieved by major budget programs (e.g., improvement in relevant social indicators) should be provided.

3.2.3 The overall balance of the general government should be a standard summary indicator of the government's fiscal position. It should be supplemented where appropriate by other fiscal indicators for the general government (e.g., the operational balance, the structural balance, or the primary balance).

3.2.4 The public sector balance should be reported when non-government public sector agencies undertake significant quasi-fiscal activities.

3.3 **Procedures for the execution and monitoring of approved expenditure and for collecting revenue should be clearly specified.**

3.3.1 There should be a comprehensive, integrated accounting system which provides a reliable basis for assessing payment arrears.

3.3.2 Procurement and employment regulations should be standardized and accessible to all interested parties.

3.3.3 Budget execution should be internally audited, and audit procedures should be open to review.

3.3.4 The national tax administration should be legally protected from political direction and should report regularly to the public on its activities.

3.4 **There should be regular fiscal reporting to the legislature and the public.**

3.4.1 A mid-year report on budget developments should be presented to the legislature. More frequent (at least quarterly) reports should also be published.

3.4.2 Final accounts should be presented to the legislature within a year of the end of the fiscal year.

3.4.3 Results achieved relative to the objectives of major budget programs should be presented to the legislature annually.

IV. Assurances of Integrity

4.1 **Fiscal data should meet accepted data quality standards.**

4.1.1 Budget data should reflect recent revenue and expenditure trends, underlying macroeconomic developments, and well-defined policy commitments.

4.1.2 The annual budget and final accounts should indicate the accounting basis (e.g., cash or accrual) and standards used in the compilation and presentation of budget data.

4.1.3 Specific assurances should be provided as to the quality of fiscal data. In particular, it should be indicated whether data in fiscal reports are internally consistent and have been reconciled with relevant data from other sources.

4.2 **Fiscal information should be subjected to independent scrutiny.**

4.2.1 A national audit body or equivalent organization, which is independent of the executive, should provide timely reports for the legislature and public on the financial integrity of government accounts.

4.2.2 Independent experts should be invited to assess fiscal forecasts, the macroeconomic forecasts on which they are based, and all underlying assumptions.

4.2.3 A national statistics agency should be provided with the institutional independence to verify the quality of fiscal data.

APPENDIX C

BEST PRACTICES IN PUBLIC BUDGETING

Extracted from Government Finance Officers' Association website http://www.gfoa.org/services/nacslb/.

Principle I—Establish Broad Goals to Guide Government Decision Making

- Element 1—Assess Community Needs, Priorities, Challenges and Opportunities
  - Practice 1.1—Identify Stakeholder Concerns, Needs, and Priorities
  - Practice 1.2—Evaluate Community Condition, External Factors, Opportunities, and Challenges
- Element 2—Identify Opportunities and Challenges for Government Services, Capital Assets, and Management
  - Practice 2.1—Assess Services and Programs, and Identify Issues, Opportunities, and Challenges
  - Practice 2.2—Assess Capital Assets, and Identify Issues, Opportunities, and Challenges
  - Practice 2.3—Assess Governmental Management Systems, and Identify Issues, Opportunities, and Challenges
- Element 3—Develop and Disseminate Broad Goals
  - Practice 3.1—Identify Broad Goals
  - Practice 3.2—Disseminate Goals and Review with Stakeholders

Principle II—Develop Approaches to Achieve Goals

- Element 4—Adopt Financial Policies
  - Practice 4.1—Develop Policy on Stabilization Funds
  - Practice 4.2—Develop Policy on Fees and Charges
  - Practice 4.3—Develop Policy on Debt Issuance and Management
  - Practice 4.3a—Develop Policy on Debt Level and Capacity
  - Practice 4.4—Develop Policy on Use of One-Time Revenues
  - Practice 4.4a—Evaluate the Use of Unpredictable Revenues
  - Practice 4.5—Develop Policy on Balancing the Operating Budget
  - Practice 4.6—Develop Policy on Revenue Diversification
  - Practice 4.7—Develop Policy on Contingency Planning
- Element 5—Develop Programmatic, Operating and Capital Policies and Plans

- Practice 5.1—Prepare Policies and Plans to Guide the Design of Programs and Services
- Practice 5.2—Prepare Policies and Plans for Capital Asset Acquisition, Maintenance, Replacement, & Retirement

- Element 6—Develop Programs and Services That are Consistent with Policies and Plans
    - Practice 6.1—Develop Programs and Evaluate Delivery Mechanisms
    - Practice 6.2—Develop Options for Meeting Capital Needs & Evaluate Acquisition Alternatives
    - Practice 6.3—Identify Functions, Programs, and/or Activities of Organizational Units
    - Practice 6.4—Develop Performance Measures
    - Practice 6.4a—Develop Performance Benchmarks
- Element 7—Develop Management Strategies
    - Practice 7.1—Develop Strategies to Facilitate Attainment of Program and Financial Goals
    - Practice 7.2—Develop Mechanisms for Budgetary Compliance
    - Practice 7.3—Develop the Type, Presentation, and Time Period of the Budget

Principle III—Develop a Budget Consistent with Approaches to Achieve Goals

- Element 8—Develop a Process for Preparing and Adopting a Budget
    - Practice 8.1—Develop a Budget Calendar
    - Practice 8.2—Develop Budget Guidelines and Instructions
    - Practice 8.3—Develop Mechanisms for Coordinating Budget Preparation and Review
    - Practice 8.4—Develop Procedures to Facilitate Budget Review, Discussion, Modification, and Adoption
    - Practice 8.5—Identify Opportunities for Stakeholder Input
- Element 9—Develop and Evaluate Financial Options
    - Practice 9.1—Conduct Long-Range Financial Planning
    - Practice 9.2—Prepare Revenue Projections
    - Practice 9.2a—Analyze Major Revenues
    - Practice 9.2b—Evaluate the Effect of Changes to Revenue Source Rates and Bases
    - Practice 9.2c—Analyze Tax and Fee Exemptions
    - Practice 9.2d—Achieve Consensus on a Revenue Forecast
    - Practice 9.3—Document Revenue Sources in a Revenue Manual

  - Practice 9.4—Prepare Expenditure Projections
  - Practice 9.5—Evaluate Revenue and Expenditure Options
  - Practice 9.6—Develop a Capital Improvement Plan
- Element 10—Make Choices Necessary to Adopt a Budget
  - Practice 10.1—Prepare and Present a Recommended Budget
  - Practice 10.1a—Describe Key Policies, Plans and Goals
  - Practice 10.1b—Identify Key Issues
  - Practice 10.1c—Provide a Financial Overview
  - Practice 10.1d—Provide a Guide to Operations
  - Practice 10.1e—Explain the Budgetary Basis of Accounting
  - Practice 10.1f—Prepare a Budget Summary
  - Practice 10.1g—Present the Budget in a Clear, Easy-to-Use Format
  - Practice 10.2—Adopt the Budget

Principle IV—Evaluate Performance and Make Adjustments

- Element 11—Monitor, Measure, and Evaluate Performance
  - Practice 11.1—Monitor, Measure, and Evaluate Program Performance
  - Practice 11.1a—Monitor, Measure, and Evaluate Stakeholder Satisfaction
  - Practice 11.2—Monitor, Measure, and Evaluate Budgetary Performance
  - Practice 11.3—Monitor, Measure, and Evaluate Financial Condition
  - Practice 11.4—Monitor, Measure, and Evaluate External Factors
  - Practice 11.5—Monitor, Measure, and Evaluate Capital Program Implementation
- Element 12—Make Adjustments as Needed
  - Practice 12.1—Adjust the Budget
  - Practice 12.2—Adjust Policies, Plans, Programs and Management Strategies
  - Practice 12.3—Adjust Broad Goals, If Appropriate

APPENDIX D

SECTIONS FROM EXISTING IPSASs PERTAINING TO BUDGETS OR BUDGET REPORTING

IPSAS 1, Presentation of Financial Statements (May 2000), prescribes the following:

2. General purpose financial statements are those intended to meet the needs of users who are not in a position to demand reports tailored to meet their specific information needs. Users of general purpose financial statements include taxpayers and ratepayers, members of the legislature, creditors, suppliers, the media, and employees. General purpose financial statements include those that are presented separately or within another public document such as an annual report. This Standard does not apply to condensed interim financial information.

13. The objectives of general purpose financial statements are to provide information about the financial position, performance and cash flows of an entity that is useful to a wide range of users in making and evaluating decisions about the allocation of resources. Specifically, the objectives of general purpose financial reporting in the public sector should be to provide information useful for decision-making, and to demonstrate the accountability of the entity for the resources entrusted to it by:

(a) Providing information about the sources, allocation and uses of financial resources;

(b) Providing information about how the entity financed its activities and met its cash requirements;

(c) Providing information that is useful in evaluating the entity's ability to finance its activities and to meet its liabilities and commitments;

(d) Providing information about the financial condition of the entity and changes in it; and

(e) Providing aggregate information useful in evaluating the entity's performance in terms of service costs, efficiency and accomplishments.

14. General purpose financial statements can also have a predictive or prospective role, providing information useful in predicting the level of resources required for continued operations, the resources that may be generated by continued operations, and the associated risks and uncertainties. Financial reporting may also provide users with information:

(a) indicating whether resources were obtained and used in accordance with the legally adopted budget; and

(b) indicating whether resources were obtained and used in accordance with legal and contractual requirements, including financial limits established by appropriate legislative authorities.

22. Public sector entities are typically subject to budgetary limits in the form of appropriations or budget authorizations (or equivalent), which may be given effect through authorizing legislation. General purpose financial reporting by public sector entities may provide information on whether

resources were obtained and used in accordance with the legally adopted budget**. Where the financial statements and the budget are on the same basis of accounting, this Standard encourages the inclusion in the financial statements of a comparison with the budgeted amounts for the reporting period.** *(Emphasis added)*. Reporting against budgets may be presented in various different ways, including:

(a) The use of a columnar format for the financial statements, with separate columns for budgeted amounts and actual amounts. A column showing any variances from the budget or appropriation may also be presented, for completeness; and

(b) A statement by the individual(s) responsible for the preparation of the financial statements that the budgeted amounts have not been exceeded. If any budgeted amounts or appropriations have been exceeded, or expenses incurred without appropriation or other form of authority, then details may be disclosed by way of footnote to the relevant item in the financial statements.

IPSAS 2, Cash Flow Statements (May 2000), prescribes the following:

29. 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. This reconciliation may be provided as part of the cash flow statement or in the notes to the financial statement.

64. Where appropriations or budget authorizations are prepared on a cash basis, the cash flow statement may assist users in understanding the relationship between the entity's activities or programs and the government's budgetary information. ***Refer to IPSAS 1 for a brief discussion of the comparison of actual and budgeted figures.*** *(Emphasis added.)*

CASH BASIS IPSAS, Financial Reporting Under the Cash Basis of Accounting (January 2003), prescribes the following:

1.3.11. Entities preparing general purpose financial statements in accordance with this Standard may disclose such information in the notes to the financial statements where that information is likely to be useful to users. Where such disclosures are made they should be clearly described and readily understandable. If not disclosed in the financial statements themselves, comparisons with budget may also be included in the notes. Part 2 of this Standard encourages inclusion of information about non-cash assets and liabilities and a comparison with budget in general purpose financial statements.

2.1.33. An entity is encouraged to disclose in the notes to the financial statements:

(a) Information about the assets and liabilities of the entity; and

(b) A comparison with budgets.

2.1.36. Public sector entities are typically subject to budgetary limits in the form of appropriations or other budgetary authority which may be given effect through authorizing legislation. One of the objectives of financial reporting by public sector entities is to report on whether cash was obtained and used in accordance with the legally adopted budget. In some jurisdictions, this requirement is reflected in legislature. This Standard encourages the disclosure of a comparison of actual with the budgeted amounts for the reporting period. Reporting against budgets may be presented in different ways, including:

(a) The preparation of a note with separate columns for budgeted amounts and actual amounts. A column showing any variances from the budget or appropriation may also be presented for completeness; and

(b) A statement by the individual(s) responsible for the preparation of the financial statements that the budgeted amounts have not been exceeded. If any budgeted amounts or appropriations have been exceeded, or payments made without appropriation or other form of authority, then details may be disclosed by way of note to the relevant item in the financial statements.

Appendix 2, p. 78, Comparison with budgets (paragraph 2.1.33(b)), Cash Basis IPSAS

(in thousands of currency units	Actual	Budgeted	Variance
RECEIPTS			
Taxation			
Income tax	X	X	X
Value-added tax	X	X	X
Property tax	X	X	X
Other tax	X	X	X
	X	X	X
Aid Agreements			
International agencies	X	X	X
Other Grants and Aid	X	X	X
	X	X	X
Borrowings			
Proceeds from borrowings	X	X	X
Capital Receipts			
Proceeds from disposal of plant and equipment	X	X	X
Trading Activities			
Receipts from trading activities	X	X	X
Other receipts	X	X	X
Total receipts	X	X	X
PAYMENTS			
Operations			
Wages, salaries and employee benefits	(X)	(X)	(X)
Supplies and consumables	(X)	(X)	(X)
	(X)	(X)	(X)
Transfers			
Grants	(X)	(X)	(X)
Other transfers	(X)	(X)	(X)
	(X)	(X)	(X)
Capital Expenditures			
Purchase/construction of plant and equipment	(X)	(X)	(X)
Purchase of financial instruments	(X)	(X)	(X)
	(X)	(X)	(X)
Loan and Interest Repayments			
Repayment of borrowings	(X)	(X)	(X)
Interest payments	(X)	(X)	(X)
Other payments	(X)	(X)	(X)
Total payments	(X)	(X)	(X)
NET RECEIPTS/(PAYMENTS)	(X)	(X)	(X)

APPENDIX E

BUDGET PREPARATION PROCESS - KEY FACTORS

Based on The United Nations Development Program, Appendix 3, The Draft Country Assessment in Accountability & Transparency Report, at http://magnet.undp.org/Docs/efa/CONTAC~1.htm, February 1997.

Some of the key factors, which contribute to making the budget process effective in practice, are outlined in this Appendix.

Transparency	The budget documents should provide a clear link between objectives and expenditures; All participants in the budget process should be clear about their roles and responsibilities; Simple well documented procedures; Well defined basis of budgeting e.g., incremental, zero based etc. Departmental targets and resources allocated, clearly indicated and explained.
Management	Effective budgeting involves more than simply preparing annual budgets; the management and monitoring of the budget is equally important.
Decentralisation	It is potentially inefficient and may undermine the budget system for all decisions to be made at the center.
Co-ordination and Co-operation	Between all those involved in the budget process is required to ensure links between recurrent and development budgets and the remainder of the processes of the financial management system.
Integration	Of recurrent and development budgets: the recurrent costs arising from development projects need to be built into recurrent expenditure planning and the trade-offs between recurrent and development expenditure considered.
Flexibility	The system should allow responses to changing circumstances: these responses should be built into the system, so that implications of any changes are sufficiently analysed and still fit within government's overall objectives and priorities.
Discipline	Although the system should provide flexibility, there should also be effective control over expenditures; Any changes to the budget should be carefully analysed and justified; Only limited use of Supplementary Estimates; Penalties for breach of rules and regulations.

Link to Medium-term Framework (National Development Plan)	Link between the resource framework of the National Development Plan and the annual budget; Link between the policies and priorities of the National Development Plan and budget allocations.
Accountability and Credibility	Political involvement: good links between politicians and civil servants; Involvement and accountability of senior managers in all stages of the process; If ministries do not believe that they will be held to their ceilings, or if they can easily bypass normal procedures, the whole process of budgeting can be undermined; Budgets should be reliably close to the actual out-turn.
Comprehensive	The budget process and documents need to include all revenues and expenditures, including all aid funds; The budget should also contain information on previous year's and current year's expenditures; Measuring the impact of the budget through output performance indicators for recurrent and development expenditures.

APPENDIX F

WORLD BANK COUNTRY FINANCIAL ACCOUNTABILITY ASSESSMENT (CFAA)

Explained on World Bank website— http://www1.worldbank.org/publicsector/cfaa.htm

Annex B. Key Issues to Examine

(i) External Fiscal Reporting and Transparency

Do the central budget office and spending ministries receive timely and accurate information to enable them to monitor budget implementation? Do they act on this information?

Is this information provided according to the same classification as the budget construction?

Is there regular external reporting on budget implementation?

What is the quality and timeliness of the government's annual external fiscal statements? Do they reflect budgets results, extra-budgetary operations, information on assets and liabilities? Do they exclude or not identify any significant parts of government activity?

What standards are used in their preparation – GFS, IPSAS or modifications of either? Are they applied consistently?

Are the statements used for any accountability or decision-making purposes?

How reliable is the published information? Are the statements audited? Are any suspense accounts reconciled/closed before end of the year? Is there a reconciliation between fiscal and monetary data?

APPENDIX G

GOVERNMENT FISCAL MANAGEMENT PROCESSES AND INFORMATION SYSTEMS

Pages 6-7, Information Systems for Government Fiscal Management by Ali Hashim and Bill Allan, The World Bank, 1999

Government Fiscal Management Processes

Macro Economic Forecasting

This process assists expenditure and resource planning by developing a macroeconomic framework linking the growth of national income, savings, investment and balance of payments to public expenditures and revenues. The process helps in the development of: aggregates of the government budget. notably revenues, expenditures, and the overall fiscal deficit and its financing; the balance between the capital and recurrent components of the budget: composition of expenditures by the main sector spending agencies; revenue forecasts consistent with macro-economic assumptions; forecasts of non-tax revenues based on macroeconomic projections; estimates of resources available from domestic and external borrowings; projections of current expenditure.

Information Systems Support

Information Systems to Support Macro Economic Forecasting

This group of systems assists the MOF with macro fiscal forecasting and development of the macroeconomic framework. This is in turn used by the MOF to advise cabinet on aggregate budget parameters and guidelines for budget agencies to submit budget estimates. These systems require data from external economic databases, and the assumptions regarding GNP, inflation rates, and the central government deficit. In addition they require information on programs and projects the government intends to implement over the period of the MTEF, data on estimates of tax and non-tax revenues, data on domestic and external borrowings, for example, manpower component, the maintenance and other operating expenses maintained by other components of the GFM systems network.

Government Fiscal Management Processes

Budget Preparation

The process of budget preparation starts with the development of a budget circular indicating economic prospects, broad policy objectives, how the budget is expected to attain them, and sectoral allocations/ceilings consistent with the macroeconomic framework. The next step is the preparation and analysis of line agency expenditure proposals and revenue forecasts and their consolidation into an annual budget document after a series of discussions at cabinet level, between line ministries, the MOF, the budgetary committees of parliament and approval by the legislature. These discussions focus on how the budget proposals would meet the policy objectives outlined in the budget circular, on inter-se priorities of the various proposals, the validity of the resource requirements contained in these proposals and how they can best be accommodated in the overall budgetary envelope.

Information Systems Support

Information Systems to Assist in Budget Preparation and Approval

The Budget preparation systems receive details of ongoing and planned programs and projects from the various line agencies, consolidate them, and produce from them the documents that form the basis of the negotiations between the line agencies and central agencies (MOF). After finalization of the budget by cabinet, the systems produce the approved budget estimates. The systems record and maintain the budgetary proposals and income estimates of all government agencies and record any changes during the budget preparation, approval and amendment processes. To assist in the evaluation of the budget proposals the system should be able to access and generate the baseline data on the manpower component, the maintenance, and other operating expenses from the relevant past-year databases. Examination of the capital expenditures requires data on the status (physical and financial) of government-approved projects, (both locally and foreign-funded). The budget preparation systems need to be supplemented with tools (such as those for cost-benefit analysis, evaluation, and performance measurement) that assist the sector and core agencies in deciding between alternative program proposals.

Government Fiscal Management Processes

Budget Execution, Accounting, and Fiscal Reporting

This set of processes covers the functions associated with implementing the budget, including the procurement of goods and services in accordance with budget estimates, the recording and accounting of all government transactions, and development of periodic reports to monitor the overall flow of spending or use of appropriations over the course of the year, highlighting major deviations from the planned budget and suggesting corrective measures.

Information Systems Support

Information Systems for Budget Execution, Accounting and Fiscal Reporting

These systems are the centerpiece of the GFM systems network, the primary repository of financial data, and serve as the basis of the governments Financial Management Information System (FMIS). These systems are used to perform the processes associated with budget execution, monitoring and control to obtain the status of actual expenditures on ongoing projects. These systems also monitor and evaluate the overall budget implementation processes and produce the necessary fiscal reports. In addition, these systems would provide useful financial information to the line ministries, and spending units (in their respective areas) to enable them to better manage their work programs.

Systems support is focused on four main systems (1) budget and warrant control; (2) accounts payable; (3) accounts receivable; and (4) the treasury general ledger system (TLS). Together they constitute the government’s Core Accounting System. The first of these is concerned with maintaining data on spending authority. These systems maintain data on approved budgeted appropriations (both capital and recurrent), sources of financing for programs and projects, budget transfers, and supplementary allocations, fund releases (warrants) against budgetary allocations over the course of the year. The second and third group of systems is used to process transactions electronically as they occur, and record data on commitments and actual expenditures against budgeted allocations. The TLS is used for compilation of summary records for control and analysis.

Government Fiscal Management Processes

Cash Management

This includes the processes of developing agency and central cash flow forecasts, the release of funds to spending agencies, the monitoring of cash flows and expected cash requirements, the issue and redemption of government securities for financing government programs.

Debt Management

This process defines the tasks associated with maintenance of records on all contracted public debt on an individual loan basis and classified according to source and type of loan. This process also assists economic and policy analysis by determining, for example, the debt implications of different fiscal and deficit financing policies by preparing projections of debt service commitments under existing and anticipated contracts.

Information Systems Support

Cash Management System

The cash management system assists Government to maintain an up-to-date picture of the government's liquidity position and cash requirements. It obtains information on actual agency expenditures and cash balances in government (including agency) accounts from the general ledger. Revenue inflows, borrowing, loan disbursements, treasury bills, government bonds, and cash deposit maturities are obtained either from the general ledger or from the specific systems for these areas, for example, the debt management system. Using this information, the government can decide on (a) budget ceilings and fund releases to line agencies; and (b) the timing of the issues and redemptions of government securities to provide short-term financing for shortfalls.

Debt Management System

These systems maintain information on public domestic and external borrowings. This includes information contained in loan documents and transactions and issues of government securities. In addition to accounting information, these systems also provide important information required in the formulation of fiscal policy such as forecasts of drawdown and debt-servicing liabilities, and debt implications of various fiscal and deficit financing policies. Payments related to government borrowings are carried out by the central system based on the data in the debt management system. Loan receipts recorded in government accounts are processed by the central accounting system and then used to update the debt database maintained by the debt management system.

Government Fiscal Management Processes

Revenue Administration

The process deals with formulation and administration of tax policies and covers the actual levy and collection of revenues including taxes and duties as laid down in these policies, and the valuation and collection of non tax revenues, such as stamp duties, user fees, charges for services etc.

Personnel Administration

This covers the activities associated with the development and maintenance of government's human resource policies including manpower planning, complement control, civil service pay and pension policies, the fiscal impact of these policies and their administration.

Information Systems Support

Systems for Revenue Administration

This group of systems assists the government in the processes associated with formulating tax and tariff policies and the subsequent collection of tax and non tax revenue. A number of separate systems are involved in this group: for example, those supporting the administration and collection of income taxes, customs duties or VAT, and those supporting the collection of various types of non-tax revenues, such as stamp duties. The revenue administration systems provide summary information on revenue collections to the Core Accounting Systems as shown in the diagram. Revenues collected by the tax and customs administration departments would be recorded at an aggregate level in the TLS, and would be reconciled with deposits made in the banking system.

Systems to Assist in Fiscal Aspects of Personnel Management

The aspects of personnel management which are relevant from the point of view of GFM are the processes associated with post management and complement control and with payroll and pension payments. The corresponding systems modules therefore form important elements in the GFM network of information systems as shown in the diagram. The payroll, pensions and employee advances systems periodically post summaries to the central system.

Government Fiscal Management Processes

Auditing

The process deals with the analysis and scrutiny of public, financial, and other transactions to ensure the compliance with government policies and procedures and to ensure cost-effective use of public funds in accordance with overall government priorities.

Information Systems Support

Systems to Support Auditing

Auditing takes place at two levels: internal audit at line ministries during the course of the FY and external audit by the auditor general through random checks and on the final accounts for the FY. These systems assist the internal and external audit agencies in their functions

APPENDIX H

COMMITMENT ACCOUNTING PROCEDURES

Page 123, Government Financial Reporting, Study 11, May 2000, IFAC Public Sector Committee

490. A commitment is generally acknowledged as the government's responsibility for a future liability based on an existing contractual agreement. Although there may be a contractual agreement, the contract does not yet give rise to a present obligation. This is because no exchange has yet taken place or, in the case of a non-reciprocal transaction, the payment is not yet due. The obligation, and therefore the liability, normally arises on delivery of the goods and services. For example, when an entity enters into a commitment to purchase or construct a capital asset in the future, an obligation normally arises only when the asset is delivered or the entity enters into an irrevocable agreement to acquire the asset. The difference between commitments and liabilities is usually clear for contractual obligations. Classification may be more difficult when obligations are embodied in legislation and some judgment may be required.

491. Commitments differ from contingent liabilities in that there is generally certainty that the liability will occur, but the present obligation will not occur until a future reporting period. The obligation is not dependent upon the outcome of an uncertain future event. At the point at which the present obligation does occur, the item ceases to be a commitment and is recognized as a liability.

492. Commitments may be disclosed in the notes or in a separate schedule. They are not accrued as liabilities in the financial statements. Various international accounting standards require the disclosure of commitments. IAS 1, Presentation of Financial Statements requires business enterprises to disclose amounts committed for future capital expenditure. IAS 17, Leases is an example of a standard that expands on the general disclosure requirement in IAS 1. It requires the disclosure of commitments for minimum lease payments under finance leases and under non-cancelable operating leases with a term of more than one year in summary form, showing the amounts and periods in which the payments will become due.

493. Governments can readily report the types of commitments that businesses report such as those related to purchase of goods and services to be provided as set out in existing contracts, agreements or legislation.

494. An argument can be made that a government's entire budget, once approved, can be considered an expenditure commitment by the government. But disclosure of that "commitment" would be of little use in the government's financial statements. The amounts allowed for in a government's annual budget would be recognized as expenses by the end of the annual reporting period.

495. Generally obligations arising from ongoing social programs would not be disclosed as commitments as there is no legal obligation to make the payments in the future (although this may vary between jurisdictions). Information on the government's future obligations under

ongoing social programs is needed to assess future borrowing requirements and taxation levels and the resulting impact on the economy; the long-term viability of social programs; and policy options available to control or reduce spending or deficit levels. This information may be disclosed in budget documents and/or financial statements.

496. Another alternative is to disclose information about only those commitments that are abnormal in relation to the government’s financial position or normal course of “business,” or that will have a significant effect on the need for revenue in the future.

497. Information about employment agreements is not disclosed as a commitment because such agreements are in the normal course of business. Similarly, it could be argued that ongoing social programs are in the normal course of the government’s business and need not be highlighted unless there is a new program commitment or a significant change to expand existing programs.

498. Some governments (e.g., the U.S. federal government) are required by law to project future expenditure levels on the basis of existing policy and disclose this information.

APPENDIX I

COMMON DIFFERENCES BETWEEN GAAP AND BUDGETARY BASIS OF ACCOUNTING

Extracted from "Relationship Between Budgetary and Financial Statement Information (1999)" published by the Government Finance Officers Association of America on their website, http://www.gfoa.org

The timing of revenue and expenditures may be different under the GAAP basis of accounting than under the budgetary basis of accounting. For example, in GAAP accounting revenues are recognized in governmental funds as soon as they are both "measurable" and "available" whereas revenue recognition under the budgetary basis of accounting may be deferred until amounts are actually received in cash.

Encumbered amounts are commonly treated as expenditures under the budgetary basis of accounting while encumbrances are never classified as expenditures under the GAAP basis of accounting.

Budgetary revenues and expenditures may include items classified as "other financing sources" and "other financing uses" under the GAAP basis of accounting.

Under the GAAP basis of accounting, changes in the fair value of investments generally are treated as adjustments to revenue, which commonly is not the case under the budgetary basis of accounting.

Under the GAAP basis of accounting, expenditure is recognized for the net present value of minimum lease payments at the time a government enters into a capital lease involving a governmental fund. No such expenditure typically is recognized under the budgetary basis of accounting.

There may be differences between the fiscal year used for financial reporting and the budget period (e.g., the use of lapse periods in connection with encumbrances, project-length budgets, grant budgets tied to the *grantor's* fiscal year).

The fund balance used in GAAP financial statements may differ from the fund structure used for budgetary purposes (e.g., debt service payments may be accounted for in the general fund for budgetary purpose, but reported in a debt service fund in the GAAP financial statements).

The government's budget document may not include all of the component units and funds incorporated into the GAAP financial statements (e.g., a school district included in the GAAP financial statements may not be incorporated into the budget).

Under the GAAP basis of accounting used in proprietary funds, the receipt of long-term debt proceeds, capital outlays and debt service principal payments are not reported in operations, but allocations for depreciation and amortization expense are recorded. Often the opposite is true under the budgetary basis of accounting.

APPENDIX J

ILLUSTRATIVE BUDGETARY COMPARISON STATEMENTS FOR THE UNITED STATES

Extracted from p. 267-273, GASB 34 Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments, June 1999

Budgetary comparison schedules should be presented as required supplementary information (RSI) for the general fund and for each major special revenue fund that has a legally adopted annual budget. The budgetary comparison schedule should present both (a) the original and (b) the final appropriated budgets for the reporting period as well as (c) actual inflows, outflows, and balances, stated on the government's budgetary basis. A separate column to report the variance between the final budget and actual amounts is encouraged, but not required. Governments also may report the variance between original and final budget amounts. Governments may elect to report the budgetary comparison information in a budgetary comparison *statement* as part of the basic financial statements, rather than RSI.

Sample City
Budgetary Comparison Schedule for the General Fund
For the Year Ended December 31, 2002

	Budgeted Amounts Original	Budgeted Amounts Final	Actual Amounts Budgetary Basis	Variance with Final Budget Positive (Negative)
Budgetary Fund Balance, January 1				
Resources (inflows)				
Charges to appropriations (outflows)				
Budgetary Fund Balance, December 31				

Sample City
Statement of Revenues, Expenditures, and
Changes in Fund Balances—Budget and Actual for the General Fund
For the Year Ended December 31, 2002

	Budgeted Amounts Original	Budgeted Amounts Final	Actual Amounts Budgetary Basis	Budget to GAAP Over(Under)	Actual Amts GAAP Basis
Revenues					
Expenditures					
Other Financing Sources (Uses)					
Special Item					
Beginning Fund Balances					
Ending Fund Balances					

APPENDIX K

GOVERNMENT BUDGET CHARACTERISTICS

Prepared by Michael Parry (International Management Consultants) in an initial effort to develop a conceptual framework.

Characteristic	Consequent features	Relevance for budget standards
1 Constitutional and legal status	1.1 Generally, there is a constitutional/legal requirement for an annual budget, and frequently the format is to some extent specified by law. 1.2 Budgets are laws, and must be passed through the legislature in accordance with prescribed procedures. 1.3 Budgets provide legal authority for the executive to incur expenditure within specified ceilings and according to laid down procedures. 1.4 Budgets provide legal authority to raise revenues.	Budget reporting standards should set out model legal requirements for budget documents as presented to the legislature and made available to the public.
2 Political significance	2.1 Budgets define the fiscal stance of government, borrowing and taxation policies, and spending priorities. These decisions are the essence of politics. A government budget is not just a management tool; it is also a political statement.	Budget reporting standards should require transparent information that enables informed political discussion.

Characteristic	Consequent features	Relevance for budget standards
3 Multiple purposes	3.1 Budgets are fiscal tools used for economic management. This is linked to, but separate from the government's need to manage its own revenues and expenditures. Fiscal policy often conflicts with operational and social objectives. 3.2 Budgets are the tool by which policies and plans are translated into operational activities. 3.3 Budgets are the management tool for allocating resources in accordance with such plans, policies and the ongoing requirements to fund a substantial government machine. 3.4 Budgets are a management tool to achieve operational efficiency and value for money in the execution of government activities. 3.5 These multiple purposes are reflected in the need to develop budget classification methodologies that meet multiple analytic requirements.	Budget reports need to reflect the multiple purposes of budgets. Comments are linked to the points in the preceding column: 3.1 Budget documents that provide transparent information on fiscal impact of budget 3.2 Budget documents in a format suitable for translation into activities, e.g. provide expenditure information in a format that accords with government structures and responsibilities 3.3 Budget documents to transparently identify resource allocation decisions, for example to programmes, geographic regions, by gender or social group 3.4 Budget documents particularly to facilitate ex-post evaluation of value for money 3.5 A published budget classification document that enables multi dimensional analysis. Budget information available in formats (spreadsheets, XBRL), that facilitates analysis

Characteristic	Consequent features	Relevance for budget standards
4 Budget as driver of the financial management process	4.1 Because of the legal, political and multi dimensional nature of the government budget, it drives the whole financial management process. This contrasts with commercial budgets, which are little more than forecasts, and where reported results tend to be the driver. 4.2 This, the structure of the accounting system and especially the chart of accounts, is driven by the budget classification. 4.3 Budgets drive the business activities of governments - the term “budget execution” describes the process. Hence the difficulty of achieving a demand driven customer focus in government activities.	This has a number of implications: Financial reports must compare incurred to budgeted expenditure. Need to be able to track budgets as they change, e.g. through virements or supplementary budgets. What should be comparator in financial reports, original or modified (flexed) budget? Chart of accounts must be based on budget classification.
5 Unrequited revenues and expenditures	5.1 There is no automatic link between revenues raised and funds expended - these are separate policy decisions, i.e. they are unrequited. 5.2 Hence the budget/accounting model is not an input-output model in the way it is for commercial entities - this is a primary reason why financial management has not historically had the significance in government that it has in commerce. 5.3 The public sector has sought to address this issue through the development of non-financial performance measures.	Budgets need to clearly identify separate revenue raising and expenditure decisions - these should not be “netted off” because this obscures the separate decisions involved. There is an issue of the extent to which performance measures should be linked to, or incorporated in, the budget process and reports.
6 Budget time periods	6.1 For most countries the legal budget process is linked to the government fiscal year. 6.2 The recent recognition to move to a medium term budget framework is typically not recognised in law. The issue arises of the legal status of medium term budget reports.	Reporting standards need to recognise possible alternative scenarios for relationships between, and legal status of, annual and medium term budget documents. Might recommend alternative approaches or just allow alternatives.

Characteristic	**Consequent features**	**Relevance for budget standards**
7 Cash based budget most easily linked to fiscal impact and budget execution process	7.1 Cash budgets directly measure the fiscal impact of the budget, and can be directly translated into cash ceilings for budget execution and expenditure management. 7.2 This in part explains why cash budgeting has persisted despite the clear inadequacies of cash accounting as a financial management tool, and even in some cases budgets continue to be cash based when accounting has moved to an accrual basis. 7.3 Hence an important need for standard setting is to address how accrual budgeting can meet the requirement for cash based information. 7.4 Cash based budgets make meaningful balance sheets impossible, but nevertheless much of the balance sheet information on assets and liabilities is essential for effective financial management. How can this discrepancy be addressed?	This is a very fundamental issue, which is at the heart of much of the debate about the use of cash accounting for government. Indeed, it is difficult to see how for any country this can be adequately addressed without starting from the budget perspective. For budget standards there are a number of issues: Will the standards accept a different basis (cash or accrual) for budget from accounting? If accrual based, what additional reports are required to (i) measure fiscal impact, and (ii) translate budgets into expenditure ceilings? If cash based, what budget reports are required on assets and liabilities (and contingent liabilities)?
8 Multiple stakeholders	8.1 The concept of stakeholders for government financial information can be seen as a multi-dimensional matrix. 8.2 Levels of stakeholders can be seen in terms of proximity to information - the executive, legislature, government officials, citizens with direct fiduciary relationships with government (taxpayers, suppliers), voters, all citizens of the country. 8.3 External stakeholders, e.g. international organisations (European Commission for EU countries, IMF, etc). 8.4 Specific interest groups, e.g., poor people, women, disabled.	The concept of transparency means the legitimate information needs of all stakeholders needs to be recognised and information provided in a manner that facilitates their ability to interpret and analyse financial transactions.

APPENDIX L

SWEDISH STANDARDS REGARDING ACTUAL TO BUDGET REPORTING

Provided by Claes-Goran Gustavsson, a member of the Budget Reporting Steering Committee.

The Swedish standard setting procedures are very much linked to the legal framework. Basically there has to be stipulations in law. There are no stipulations regarding accounting in the constitution. For central government there are basic stipulations in the State Budget Act. These concern the governments reporting obligations. GAAP shall be the basis for the accounts. As regards agencies there are stipulations in a government ordinance. The Financial Management Authority has issued supplementary regulations to the ordinances. Thus, the standards have the form of regulations and are bound to specific formats.

With regards to regional and local governments, there is a basic law (Local Governments Accounting Act) where GAAP is prescribed to be followed. The law also states that in case the accounts diverge from standards given by a standard setting body for the local government sector that shall be stated as well as the reasons for the divergence. As a consequence there is a standard setting body established called the Local Governments' Accounting Standards Council.

Local Governments Accounting Act

The law states: "The report of the directors will contain a statement of the outcome related to the budget established for the running activities." There are no further standards issued by the council.

State Budget Act

Follow-up, forecasts and outcome

38 §
On at least two occasions in the course of the fiscal year, the Government shall submit forecasts to Parliament concerning the outcome of state budget revenue and appropriations, and state debt. The Government shall explain significant discrepancies between budget amounts and estimated outcome.

39 §
At the latest four months after the end of the fiscal year, the Government shall submit a report to Parliament on the preliminary outcome of state budget revenue and appropriations. The Government shall explain significant discrepancies between budgeted amounts and the preliminary outcome.

40 §
As soon as possible, but no later than nine months after the concluded fiscal year, the Government shall have an annual report presented to Parliament. The annual report shall contain

a statement of financial performance, a statement of financial position and a cash flow statement. It shall also contain the final outcome of state budget revenue and appropriations.

Ordinance concerning the Annual Reports and Budget Documentation

Section 2. General provisions relating to the annual report

Art 1. The agency shall submit an annual report to the Government for the preceding financial year no later than February 22 each year.

Art 4. The annual report shall consist of

- A performance report;
- A statement of financial performance;
- A statement of financial position;
- An appropriation report;
- A cash flow statement; and
- Notes.

The agency's annual report shall also contain a summary of important information from the statement of financial performance, the statement of financial position and the appropriation report. The summary shall also contain information on the loan limit, appropriation credit and certain key indicators. In its annual report the agency shall also provide information on other circumstances of significance for the Government's follow-up and appraisal of operations.

Section 6 Appropriation report and cash flow statement

Art 1. In the appropriation report the agency shall report on the outcome of the appropriations that the agency has at its disposal and the income headings that the agency shall report on in accordance with the breakdown made in the Government approval document or other decisions of the Government, or the agency that has delegated the right of disposal. The outcome shall be compared with the amount allocated or delegated per appropriation or appropriation item and with the estimated amount for each income heading. An analysis shall be made of discrepancies.

The appropriation report shall also show the extent to which the agency, on the basis of special authority granted to it, has ordered goods or services or approved grants, compensation, loans or the like that will entail expenditure in following financial years but which are not covered by appropriations at the disposal of the agency. The appropriation report shall also show how the agency has complied with other financial conditions laid down by the Government.

In **supplementary regulations from the National Financial Management Authority,** the format of the Appropriation Report is prescribed:

Appro-priation	Starting carry over amount	Budget allocation	To others allocated amounts	From government reallocated amounts	Used part of admitted exceeding	With-drawals	Total disposable amount	Expend-itures	Revenue	Final carry over amount

(Notice a carry over system greatly influences the format. Notice also that revenues are rare. They normally are not accounted for against appropriations but in the statement of financial performance.)

APPENDIX M

BUDGET PREPARATION IN DENMARK

Provided by Christian Iver Svane, member of the Budget Reporting Steering Committee.

1. The Budget cycle

The Budget Preparation Process in Denmark follows generally the same pattern every year. In the following this is illustrated through the Preparation of the Budget for the year 2004.

The Preparation of the Budget for 2004 began in early 2003, shortly after the Parliament in December 2002 approved of the Budget for 2003, and while the spending ministries are putting their final hand to the fiscal accounts for 2002.

This indicates that from the first preparations of the Budget Proposal it takes about 1 year before the Parliament decides on the Budget and about 2½ years before the fiscal accounts can be presented to Parliament.

In addition to this multi-year Budget, estimates for the fiscal year have been presented in the appendixes to the previous three years Budgets.

The overall schedule is illustrated in the following table:

January	Ministry of Finance examines Budget preconditions and proposes overall Budget targets
Early February	Break down of overall Budget targets to ceilings for consumption and income transfers for each ministry
Early May	Line ministries give their draft Budget Proposals to The Ministry of Finance
May - June	Ministry of Finance performs technical scrutiny of the Budget Proposal and holds discussions with line ministries on the financing of new initiatives etc.
August	Last minute estimates of the economic situation and the influence on the Budget Proposal
End of August	Presentation of the Budget Proposal
Early September	First Parliamentary discussion on the Budget Proposal
Early November	End to political negotiations on the Budget Proposal

Mid November	Minister of Finance proposes the Governments amendments and changes to the Budget Proposal (including the result of the political negotiations).
End of November	Minister of Finance presents amendments due to a final estimate of the economic situation and the influence on the Budget Proposal
Mid December	Third and final Parliamentary discussion on the Budget Proposal

2. Institutions in the Budget Process

The Preparation of the central Government Budget in Denmark is done in co-operation between several levels of Government. The different authorities play their own special role - not only in the preparation of the Budget Proposal, but also in implementing the Budget, and controlling the outcome.

- The authorities and the functions they perform can be found in every country. A closer study will however show differences with regard to Procedures used in the Budget preparation and appropriation Process, and during Budget implementation, follow-up and control.
- Actual influence that the different authorities have at different occasions during the Process.

This presentation will give an introduction to the authorities and their role in the Danish Budget and appropriation system.

Parliament

The Parliament is the central appropriation authority. According to the Danish constitution no expenditure may be paid without a prior appropriation from the Parliament, and no tax may be collected if it is not decided in a law.

As for the Budget procedures the Danish constitution states that the Budget Proposal must be presented to Parliament at the latest four month prior to the beginning of the fiscal year.

The Parliament cannot make its own Budget Proposal, but it is entitled to decide changes to the Governments Budget Proposal before finally adopting the Budget.

The Parliaments Finance Committee functions as the appropriation authority during the fiscal year. It is also in the Finance Committee discussions on the detailed contents of the Governments Budget Proposal are taken. Usually the Parliamentary debate on the Budget Proposal follows a broader perspective on the economic policy.

When the Budget Proposal has been adopted by Parliament and the fiscal year has begun, changes to the appropriations in the Budget can be implemented through applications to the Parliaments Finance Committee. Such applications must contain a full explanation to why a change is necessary, how it will be financed e.g. through cuts in other appropriations or reserves. Furthermore an application must bee approved by the Ministry of Finance before it can be sent to the Finance Committee.

This procedure makes the Danish appropriation system very flexible because most applications to the Finance Committee are passed within 1-2 weeks. As a special Danish practice all applications passed by the Finance Committee during the fiscal year are combined in one supplementary appropriation-act by the end of the fiscal year.

Government

At Cabinet-level only a few general economic discussions are taken during the year. Generally most economic discussions in the Government including Finance Policy and Economic Programmes are taken in the Cabinets Economic Committee (a group of 6 ministers where the Minister for Finance presides). In specific matters this Committee can call on other ministers.

In January the Cabinets Economic Committee decides on ceilings for the coming year (i.e. spending limits for each ministry). This discussion also includes a broader economic discussion on the global economic targets.

In June the Cabinet discusses the result of the Budget Preparation Process and decides on the Budget Proposal for presentation to Parliament.

Ministry of Finance

The Ministry of Finance are coordination the Budget Process. It is the Minister of Finance who presents the Budget Proposal to Parliament on behalf of all cabinet ministers.

Under the Danish system no cabinet minister can contact the Parliament or its Budget committee in appropriation issues without a prior acceptance from the Minister of Finance.

The functions of the Ministry of Finance in the Budget Process can be divided into four major tasks.

- To make Guidelines and Directions to be used by the spending ministries when drafting the Budget.
- To collect draft Budget Proposals from the ministries and combine these to the final Government Budget Proposal.
- To follow-up on Government revenue and spending and make economic forecasts and calculations as preparation for Government decisions on economic policy.
- Through the Agency for Economic Management to ensure the accounting in the agencies and to present the fiscal accounts after the end of the fiscal year.

The first three functions are necessary to ensure that the Minister of Finance has the background to present a coherent economic policy based on actual projections of the Fiscal Balance for the Central Government.

Due to practical considerations the functions of accounting are placed with the Agency for Economic Management. This is to ensure the best possible use of computer technology, but also due to financing considerations. In Denmark the Ministry of Finance does not make money transfers to spending agencies. The agencies have access to draw directly on the Central Bank. The accounting and payment systems gives the agencies regularly updated reports on how much have been spent of the appropriation. These reports are also sent to the relevant ministry.

Spending ministries

All Government administration in Denmark is based on the law of responsibility of each cabinet minister. The law determines that the minister are politically responsible for all decisions taken within his area, but does not prohibit a delegation of decision-power to lower levels within the ministry.

This implies that all appropriations decided by Parliament are given to a minister. From this also follows that every spending decision in the agencies are taken on the Ministers responsibility.

The spending ministries therefore have two major functions in the Budget Process.

- They have to present a draft Budget Proposal for the ministry and all its agencies to the Ministry of Finance.
- They have to follow-up on the actual Budget and take action if an agency has difficulties to keep the given appropriations.

If a spending ministry during the Budget follow-up finds it necessary to apply for a change to an appropriation, the application and the financing must be approved by the Ministry of Finance before it can be submitted to Parliament.

Spending agencies

The spending agencies are where the actual spending of the appropriations decided by Parliament is done. In the Danish Budget system they are involved in several parts of the Budget Process.

As mentioned above they operate on behalf of the relevant minister and on his responsibility. The amount of decision-power delegated from the minister to the agencies can differ from ministry to ministry. This also applies to spending decisions.

In most cases the Budget Process with in a ministry starts with the minister asking the different agencies for draft Proposals to the Budget for their operations. Later in the Budget Process agencies usually are asked to help in the Process of giving priority to marginal spending reductions or expansions.

During the fiscal year the spending agencies have to control spending and follow-up on the allocated appropriations. If this follow-up shows that the given appropriations are about to be exceeded the agency must either take actions to reduce spending or apply for a raise of the appropriation. Such an application cannot be sent directly to the Parliament Finance Committee, but must go through the relevant minister and approved by the Ministry of Finance.

3. Establishing Budget preconditions

As mentioned in the first section the Budget Process begins approximately one year prior to the beginning of the fiscal year.

Before the actual drafting of the Budget Proposal can be set in work, several preconditions have to be determined. These preconditions are all based on an economic analysis of the Danish economy.

This analysis is first of all used to see what will happen if no policy-actions are taken. In other words the analysis determines the statistical basis for the Budget preparation.

As an appendix to the Budget for the current year, multi-year budget estimates are presented to Parliament.

In the multi-year budget estimates activity-based factors have already been implemented. Among these are factors are demographic developments such as the number of old-age pensioners and the number of students at higher education’s, but also other factors e.g. results of political agreements on the number of police officers and the level of expenditure to foreign aid programmes are implemented.

Furthermore the results of the latest economic analysis regarding cyclical expenditure i.e. unemployment benefits and some social welfare programmes also are included in the multi-year budget estimates.

What the new economic analysis provides are new estimates with regard to cyclical expenditure and forecasts of the inflation.

As the multi-year Budget estimates are provided in the same price-level as the Budget for the current fiscal year. It is important to have an estimate of the inflation to determine the price-level for the coming fiscal year. Furthermore it is important that the same forecast of the inflation is used in all ministries and agencies during the Budget preparation to ensure the consistency of the Budget Proposal.

The economic analysis is the basis for forecasts of the inflation on

- Salaries and wages
- Working expenses
- Construction expenditure
- Entitlement expenditures (income transfers)
- Tax basis (for collecting income-tax, VAT etc.)
- Revenues (other than taxes)

The Ministry of Finance distributes these forecasts to all Government agencies from the beginning of the Budget Process. Later on these Budget preconditions are only changed if an economic analysis shows large and important deviations.

4. Setting up overall Budget targets

Since the mid-eighties the Budgetary Process in Denmark has been under reform and the expenditure control strengthened. The general framework of the Budget Process is the setting of ceilings for each spending ministry, within which they have to present their Budget Proposal to the Ministry of Finance.

The system of ceilings consists of two spending limits. One for consumption and one for income transfers. Beneath the spending limit for consumption there is a special limit for salaries, and beneath the limit for income transfers is a sub-limit for discretionary expenditure programmes.

An important part of the system with ceilings is that the allocation of the spending limit lies with the spending ministries. The Ministry of Finance controls the overall spending limits and whether the spending ministries keep their ceilings.

The Budget Process starts in the beginning of January with an evaluation of the latest economic of the Danish economy with the purpose of establishing an acceptable overall expenditure level.

In the beginning of February the ceilings for the individual spending ministries are decided by the Cabinets Economic Committee.

During the 1980s the main fiscal objective was to reduce and eliminate the deficit and at the same time hold the non-cyclical expenditure at the same level in real terms. Due to demographic changes this implied a strong fiscal policy. Since 1993 the fiscal objective has been re-evaluated. Growth in non-cyclical expenditures must be beneath the growth in the economy and priority has been given to deficit reduction and in the latest years with surplus to debt reduction.

It is to ensure that these fiscal objectives are in line with the proposed overall spending limit, that the economic analysis are evaluated by the Ministry of Finance before the ceilings are prepared and proposed to cabinet.

But apart from the economic analysis of the economy the Ministry of Finance also evaluates the Budget for the current year with respect to technical aspects as:

- Expected change in expenditure due to demographic conditions
- Actual spending in the preceding year
- New estimates for income transfers

In this Evaluation Process the Ministry of Finance also takes into account the expected expenditure development in the different spending programmes as presented in the multi-year Budget estimates.

Furthermore the Budget for the spending ministries is evaluated aiming at finding spending programmes, where cuts can be proposed. Targeted cuts proposed by the Ministry of Finance will however only become effective if the relevant spending ministry adopts them.

However the Ministry of Finance does incorporate the Proposals in the ceilings presented to the Cabinets Economic Committee. This commits the spending ministries to incorporate the cuts, come up with other Proposals or negotiate a raise to their ceilings.

Finally an important part of the evaluation Process is to find the level of total expenditure that can be accepted with the overall target of a growth in Government expenditure that is below the growths in the economy in mind.

Based on the above-mentioned considerations and evaluations The Ministry of Finance prepares a decision paper for the discussion in the Cabinets Economic Committee with Proposals of ceilings for the different spending ministries.

A part of this decision paper is the allocation of possible targeted spending reductions or proposed analysis of spending programmes.

The Cabinets Economic Committee decides to the decision paper in the beginning of February. After deciding on the ceilings the spending ministries are given approximately three month to prepare their draft Budget Proposal within the decided ceilings.

Upon receiving the draft Budget Proposals from the ministries the Ministry of Finance will make analysis and technical scrutiny of the requests. A part of this Process is to make sure that Budgets are kept within the ceilings.

APPENDIX N

INFORMATION ABOUT THE FRENCH BUDGET

Provided by Sophie Mahieux, member of the Budget Reporting Steering Committee.

In France, like in other jurisdictions, the Government's budget is primarily a document issuing financial authorizations (revenue authorization, expenditure authorization), with corresponding estimated amounts on the revenue side, or maximum amounts on the expenditure side.

Therefore, that legal document cannot be only considered as a prevision document, presenting projections of revenue and expenses in the future, as it can be the case for a public or private company.

The French budget's structure is supported by two major presentations of the authorized expenditures:

- Expenditures are presented by functions (defence, culture, foreign affairs, etc.),
- Expenditures are also presented by nature (personal, equipment, etc.)

The French budget covers the whole of central government. Other levels of government, and the social security system, present their own budgets, based on different legal rules. In the French case, central government means central administration and local branches of the central administration. That also means that the budget is a "general budget," melting all the government's revenue and all the government's expenditure in the same document, with some minor exceptions.

The French budget is based both on the cash basis and on the commitments basis (formulation and execution stages). For reporting purposes, the financial statements are based on the accrual basis, and present a reconciliation chart between budgetary cash execution and general purpose financial statements, and between these elements and national income accounting charts.

The French budget is adopted on an annual basis, but a special report presents a multi-year projection of expenditures and revenues. Changes in the budgetary scope are explicitly presented each year.

During the year, the Supplementary Budget presents details on all the changes in appropriations since the initial Budget Act.

Finally, the Budget Review Act shows the final outturn of the budget, compared with the initial budget.

Performance indicators are to be in the budget step by step from now on to 2006.