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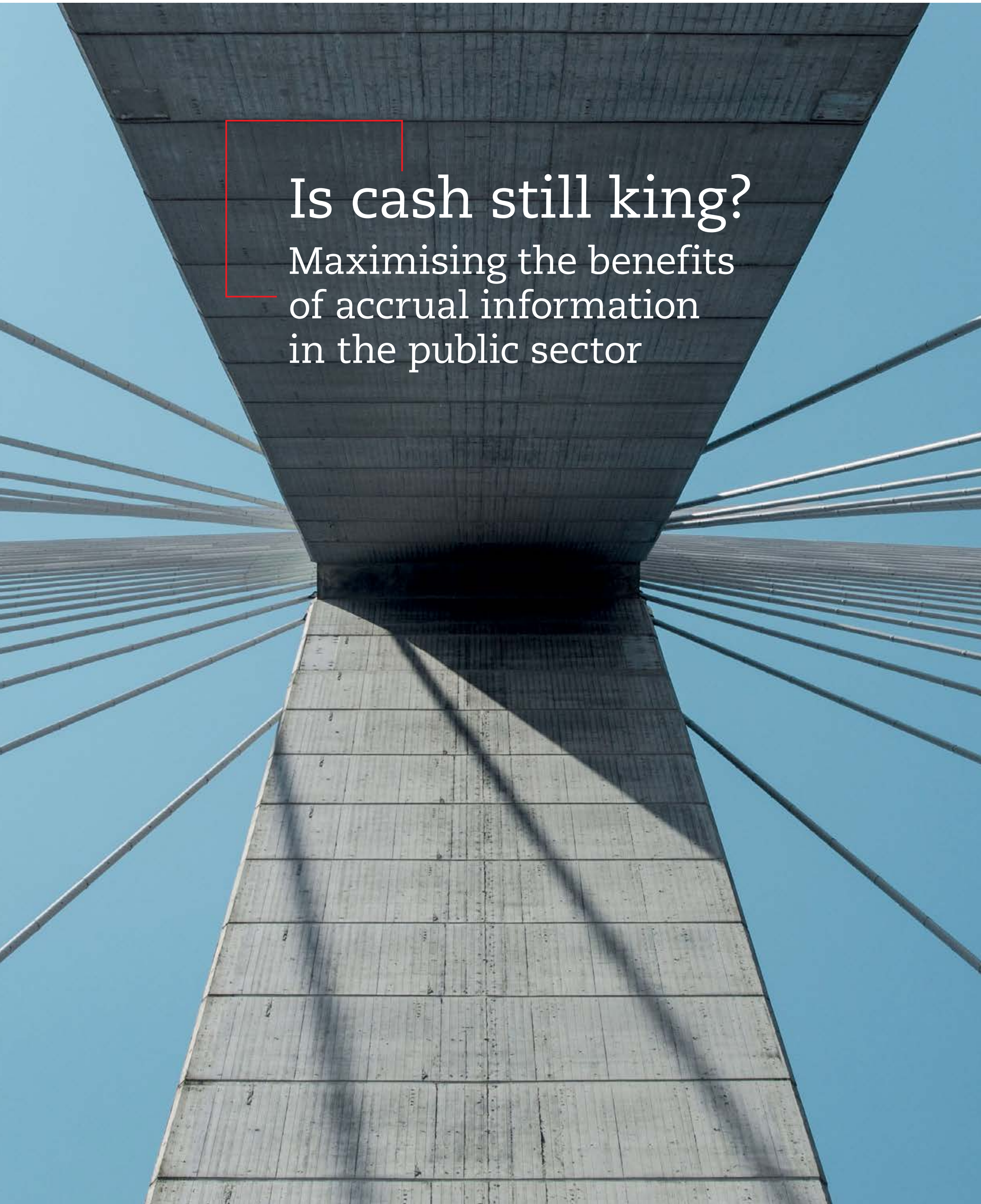
Is cash still king?

Maximising the benefits of accrual information in the public sector



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IFAC (the International Federation of Accountants) is the global organization for the accountancy profession dedicated to serving the public interest by strengthening the profession and contributing to the development of strong international economies.

Comprised of over **175** members and associates in more than **130** countries and jurisdictions, IFAC represents almost **3 million** accountants in public practice, education, government service, industry, and commerce.

Over four decades, IFAC has represented the global profession and supported the development, adoption, and implementation of international standards that underpin the contributions of today's global accountancy profession. IFAC has maintained a long-term approach to building and strengthening a global accountancy profession that supports transparent, accountable, and sustainable organizations, financial markets, and economies.

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Is cash still king?

Maximising the benefits of accrual information in the public sector

About this report

There is a global transition underway, where governments are moving from a cash to an accrual basis for their financial reporting. This report offers lessons learned from jurisdictions that have implemented accruals, with the intention that this global transition to accruals creates real value and is more than a 'compliance exercise'.

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Foreword

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Pensioners without pensions. Schools without students. Wells without water.

These are just a few human consequences that can result – and *do* result – when governments don't have the financial information necessary to make the best long-term decisions for their citizens.

Cash accounting, which 75 percent of governments around the world use in some form, is of course useful. But ultimately, cash accounting doesn't present the most accurate picture of a government's financial health, nor does it enable decision makers in the public sector to adequately plan for the development, delivery, and maintenance of the services, programs, and infrastructure on which people rely. And that, in turn, leads to a breakdown of trust in governments.

Accrual accounting creates the ability to recognize, value and manage public sector assets and liabilities. A government using accrual accounting has, for example, the mechanism to record where its wells are and assign them value based on their working condition – crucial in assessing whether they are delivering lifesaving water for people. In cash accounting, conversely, the construction costs are recognized in year one, but after that visibility is lost. There are essentially no records to help track the utility of the well, whether it needs maintenance, whether there are funds for more wells. This is an actual example discussed in this report, and one that reminds us of the very tangible impacts that accrual accounting systems can have on human lives.

While wells might be the order of the day in some jurisdictions, other economies would benefit from public sector accrual accounting that enables the effective management of liabilities. For example, this would be crucial to the health of a pension system or the development of a carbon offset program. Regardless of the application, accrual accounting and budgeting is a game changer. It's why we, as IFAC [and ACCA], are so committed to the support, adoption, and implementation of International Public Sector Accounting Standards (IPSAS) that underpin public sector accrual accounting, and to the development of a robust profession with the capacity to understand, implement and manage such systems.

We are very encouraged that the *2018 International Public Sector Financial Accountability Index* found that 65 percent of governments surveyed have implemented accrual accounting, or plan to implement it by 2023.

The report that follows not only confirms that a complete public sector transition to accrual accounting will serve the public interest, but also contains 30 specific recommendations to improve accrual implementation.

To the finance professionals and public sector decision makers who are leading this important transition, we commend you and support you.

Contents

Executive summary

The foundation of good decision making is having the right information. Most government decisions have a financial aspect and knowing what the government owns and owes, as well as understanding the economic reality of its activities, improves the quality of the decisions made.

Accruals-based accounts provide more complete information than cash-based accounts and around the world there is a drive for governments to implement accrual accounting. The 2018 International *Public Sector Financial Accountability Index Status Report* (IFAC and CIPFA 2018) found that many central governments (40% of those surveyed) are planning to implement accrual accounting by 2023. The finance professionals and public sector leaders in these countries are the intended primary audience for the present report – where they will find 30 recommendations to improve accrual implementation in Chapter 4.

BENEFITS OF ACCRUALS IN THE PUBLIC SECTOR

The experts consulted for this project identified transparency, accountability, fiscal credibility and the production of decision-useful information as the overriding benefits of accruals implementation. The benefits achieved depend on the level and type of implementation. Table I.1 sets out the benefits and level of complexity arising from different models of financial reporting and budgeting.

Governments reporting and budgeting on a cash basis (Column A) can achieve basic fiscal discipline through the allocation of cash budgets. Column B describes the benefits observed for governments reporting on an accrual basis but still operating cash budgets, where governments are able to support better long-term and fiscally sustainable decision making than when working purely on a cash basis. Column C shows the benefits obtained by jurisdictions operating on an accrual basis for financial reporting and budgeting, where, in addition to the benefits of Column B, this approach puts finance at the heart of government decision making.

The experts noted a higher degree of complexity resulting from using inconsistent bases for appropriations, budgeting and reporting, which reduces the comparability between governments' financial information and can obstruct proper financial accountability.

TRANSPARENCY, ACCOUNTABILITY, CREDIBILITY AND VALUE FOR MONEY

The information created by reporting public accounts on an accrual basis creates opportunities for improving accountability and transparency. This view resonated with the global community of experts interviewed for this project. This new information facilitates conversations by decision makers and the public on the appropriate allocation of public resource.

Several of the experts said that moving to accruals-based accounts and, in particular, following International Public Sector Accounting Standards (IPSAS), means that information is being produced in a consistent manner across the public sector, making the information more accessible and comparable between entities. Some experts also commented that having accruals-based financial reports made them understandable by more people as they are more comparable with private sector accounts.

The transition to accrual accounting can improve the fiscal credibility of a government, and for less mature or

TABLE 1: Benefits and complexity arising from each accounting and budgeting basis

	(A) CASH ACCOUNTING AND CASH BUDGETING	(B) ACCRUAL ACCOUNTING AND CASH BUDGETING	(C) ACCRUAL ACCOUNTING AND ACCRUAL BUDGETING
BENEFITS	• Provides basic fiscal discipline • Simpler / intuitive for non-financial staff and the public	Facilitates public scrutiny • Improved accountability • Provides fiscal credibility Achieving value for money and financially sustainable decision-making • Managing assets well and accounting for the maintenance backlog • Managing liabilities and identifying fiscal risks • Reducing fiscal illusions and improving incentives • Supporting long-term thinking	The benefits in Column B **PLUS** Puts finance at the heart of decision-making • Embeds performance management • Improves medium-term forecasting and planning o Further enhances fiscal credibility • Effective project management across government • Embeds the finance function in day-to-day decision-making
LEVEL OF COMPLEXITY	**Low**	**High**	**Medium**

developing economies the move to accrual accounting can lead to increased confidence in public financial management.

At the same time, the implementation of accrual accounting can create barriers to effective transparency if the information included cannot be understood.[1] There is therefore, a key message for governments: that they must consider how best to communicate the new information arising from accrual accounting.

Experts also noted that accrual accounting can strengthen the accountability mechanisms in government. Parliamentary committees have played a role in holding governments to account using the new information provided by accrual accounting.

MANAGING ASSETS WELL AND ACCOUNTING FOR THE MAINTENANCE BACKLOG

Generally, public sector assets are held because they are needed for the delivery of public goods or services and would likely need to be replaced if they were damaged. Cash-based accounting can discourage maintenance whereas, through financial reporting, accrual accounting recognises the cost associated with deterioration in the condition of assets. New information available through accrual accounting aids in identifying where asset maintenance is inadequate.

Accrual accounting information can also be helpful when an asset comes to the end of its useful life and is useful for decision makers in understanding where resource should be allocated to finance the replacement of assets. This reporting can be helpful in improving the management of assets and ultimately improving the quality of public services derived from government assets.

MANAGING LIABILITIES AND IDENTIFYING FISCAL RISKS

Accruals can benefit public sector organisations by providing information to improve the management of liabilities and allows governments to take decisions that support their objectives without burdening future generations with unmanageable debt. For governments to maintain a sustainable financial position, effective management of their liabilities is necessary. The experts consulted have provided examples of policy discussions that were better informed by accrual information.

Accrual accounting also creates new information on contingent liabilities, which can be helpful for governments in identifying fiscal risks. Analysis by the International Monetary Fund (IMF) shows that realised contingent liabilities can have a substantial impact on public sector balance sheets.

REDUCING FISCAL ILLUSIONS AND PERVERSE INCENTIVES

Experts identified examples of fiscal illusions (ie accounting devices that give the illusion of change without its substance). Information generated by accrual accounting can dispel these illusions and can support sustainable decision making in public finance.

The move to accrual accounting can help in creating a fiscal framework with targets that recognise the impact of decisions on the public sector's balance sheet. Without this, there will be significant temptation to shift costs outside the scope of fiscal targets – even where such a decision would not provide good value for money. The benefits of having a strong net worth position suggest that governments should consider using net public sector wealth as a key indicator in setting their fiscal rules.

Whole-of-government accounts, prepared using accruals, give a more holistic picture of a government's financial position. It is only possible to provide a full financial picture of the resources and risks for the public sector if there is full consolidation, which must include state-owned enterprises (SOEs) at 'whole of government' level.

The additional information provided through accrual accounting means that government decision makers are better

1 See the work by David Heald on the difference between nominal and effective transparency. For example, see Heald 2015.

> **By implementing accrual budgeting alongside accrual reporting, governments will realise a series of benefits that flow from putting finance at the heart of decision making.**

informed on the range of liabilities and risks facing the public sector – and can then consider what steps should be taken to reduce or mitigate these challenges.

SUPPORTING LONG-TERM THINKING AND PLANNING

There are clear examples of how governments can use the information generated through accrual accounting to support their long-term planning and policymaking.

It is no surprise to see that governments that use accruals-based accounts take a longer-term view of their finances than those that rely on a cash basis. Strong balance-sheet management supports low borrowing costs and provides flexibility for governments to respond to emerging pressures, and allows them to absorb fiscal shocks.

Accrual accounts are useful in informing governments' fiscal sustainability reports, or intergenerational reports, which can be used to project the fiscal position into the longer term. Having an accruals-based balance sheet provides the baseline.

ACCRUAL BUDGETING: PUTTING FINANCE AT THE HEART OF DECISION MAKING

Although many governments are planning to move to accrual accounts for their financial reporting, few adopt accrual accounting in the preparation of their budgets and there are inconsistencies in the use of accruals in appropriations, budgets and financial reporting. By implementing accrual budgeting alongside accrual reporting, governments will realise a series of benefits that flow from putting finance at the heart of decision making.

The implementation of accrual budgeting is required to embed the finance function fully in day-to-day decision making. For finance to drive decisions, accrual budgeting must be included in the implementation road map, to embed the function in day-to-day decision making.

Accounting and budgeting on the accrual basis facilitate frequent, often monthly, budget monitoring reports. This allows for more transparency and the opportunity to identify issues early. It has also enabled reforms that can lead to better and more informed resource allocation decisions and to more meaningful information being available to the public to track progress towards intended outcomes. This approach puts the needs of the people at the centre of investment decision making.

The benefits of accruals implementation – achieving value for money, facilitating public scrutiny, and putting finance at the heart of decision making – are all derived from the creation of new decision-useful information. The accrual basis supports decision-makers in the public sector by providing new information that reduces fiscal illusions and allows for more regular reporting to embed performance management.

The benefits highlighted are supported by improvements in the quantity and quality of financial information. The experts interviewed cited a range of examples of how accruals had produced decision-useful information, no matter the stage of country maturity.

OBJECTIVE SETTING

The experts consulted for this report agreed that the implementation of accruals is a long-term project in the public sector, and clarity of direction is important. No two jurisdictions begin the journey of reform with the same capabilities or with the same motivation, and it is important that they acknowledge this in setting the objectives they seek to achieve through reform.

The experts also noted that the implementation of accrual accounting should not be considered in isolation. Instead, it requires consideration of the wider system benefits that could be achieved, as well as the interventions that will support the implementation of accruals.

> Creating decision-useful information that is trusted requires a strong challenge function to review the progress of the reforms.

Many experts described the need to postpone or remove certain portions of implementation in order to address politically sensitive issues or technical challenges. This approach is helpful in building a multi-staged execution in implementing accruals, but at the same time this should not create the justification for removing important, if challenging, aspects of accrual reporting and budgeting.

It is important to allow sufficient time for planning and gap analysis to create a road map that is achievable but ambitious over the long-term. There must be realism about when certain milestones and benefits will be achieved and periodic checkpoints along the way. Such a plan could also include how governments transition from cash appropriations to accruals.

The implementation of accrual accounting requires constant iteration and development. A mindset of continuous improvement is needed.

STAKEHOLDERS

One of the distinguishing features of the public sector is the existence of a broader range of stakeholders compared to private sector organisations. As well as citizens, there are donors, funders, service users, civil society groups, ratings agencies, NGOs and other government bodies. A variety of stakeholders need to be engaged in the process of accruals implementation. Creating decision-useful information that is trusted requires a strong challenge function to review the progress of the reforms. It is also important to educate potential users of the accounts and to help them contribute positively to the narrative about the public finances.

The experts consistently referenced the need for the 'buy-in' of senior leadership and politicians as high-level champions for the reform. Cross-party political support is also needed to sustain support for the transition to accruals. For a reform agenda to be successful, it is critical that finance officials identify these internal advocates and communicate the stakeholder-specific benefits that each group will receive through accruals implementation.

SYSTEMS

It is important to consider the systems underpinning accrual accounting, as these are key enablers that will support the creation of decision-useful information. It is critical that governments consider how incentives can be built into their systems to encourage the use of decision-useful information.

A frequent consideration by the experts was whether the financial management systems underpinning accrual accounting would be centralised or devolved to departments. Pragmatism has played an important role in the approaches taken to adoption of new systems. It is important to be clear at the outset on the expectations of the line ministries or departments.

The experts also argued that changing government structures and new information requirements must be considered in deciding what systems will be most appropriate in supporting the creation of decision-useful information. The experts recommended that consideration be given to the integration of budgeting, accounting and government finance statistics into the same system, to enable the use of budgeting information for comparison purposes. This requires in-depth engagement across government to discover what systems might meet the jurisdiction's needs.

Many reflected the belief that the production of accrual information should be created to a common standard so that the process can become more routine. Officials and public sector leaders should consider where additional expenditure on systems can produce good value for money and where bespoke or expensive changes may be unnecessary.

> Governments transitioning to accruals may also need to develop a training programme so that they can 'grow their own' rather than relying on the marketplace to supply sufficient talent.

SKILLS

Having professional finance staff who can produce analysis based on accrual accounting information can provide decision makers with a better long-term view of their policy decisions and can help improve the sustainability of public finances.

Building internal capacity requires more than increasing the number of qualified accountants. Governments must understand what they need their accountants to do in an environment driven by decision-useful information. Governments do not need lots of expensive external support, but they do need to get the right external support.

Governments will need to develop remuneration packages that are sufficient to attract and retain accountants with the necessary skills, knowledge and experience. Governments transitioning to accruals may also need to develop a training programme so that they can 'grow their own' rather than relying on the marketplace to supply sufficient talent. All this might be described as establishing an attractive career path for professional accountants in the public sector.

Internal training needs to extend beyond preparers to include auditors, members of parliamentary committees, human resource professionals, and procurement officials. Importantly, for accrual information to be most useful, training needs to cover the interpretation of this information by a broader pool of stakeholders.

Finally, there is a need to consider the balance between the systems supporting accrual reform and the ability to retain skilled staff in a public sector entity. Those countries currently undergoing accruals implementation can consider whether a capacity gap could partly be addressed through larger investment in appropriate systems that can augment the abilities of less-skilled preparers and users.

CONCLUSION

The production of a public sector balance sheet can provide more information that could improve the economic outcomes in a country. Analysis by the IMF shows that improving a country's net worth can provide substantial benefit, including paying lower interest on debt and having shorter and shallower recessions (IMF 2018).

Accrual accounting is not the end objective. It is a corollary to the objective of improving performance, both in delivering services and in managing the balance sheet of the government. This research shows that accrual accounting provides new decision-useful information that is leading to better decisions by government and enabling new discourse that supports stronger financial management in the public sector.

Introduction

Governments receive money from taxes, grants, loans and a wide range of other sources and they spend it on delivering services to, and building infrastructure for, citizens. Taking decisions on the basis of how much cash has been received and spent severely limits governments' ability to achieve value for money. Therefore, in the case of financial reporting, cash is not king.

If government decision makers, whether politicians or officials, have accrual information on the assets and liabilities associated with their services and projects they can factor it into their decisions to obtain the best possible value for money for their citizens. This report contends that cash management is still an important part of broader financial management, but is not the cornerstone of financial reporting or performance management in government.

The International Public Sector Financial Accountability Index, published by IFAC and the Chartered Institute of Public Finance and Accountancy (CIPFA) in November 2018, found that 65% of governments planned to report on an accrual basis by 2023. This means that approximately 40% of central governments around the world are in the process of transitioning to full accrual accounting, a truly momentous global transition.

Implementing accrual accounting is a complex and challenging project. There are many lessons that governments can and should learn from the experience of governments that have already completed their transition to accrual accounting. This report is not about whether a government should or should not adopt accrual accounting. Instead, it is intended to be used by those who are on the journey and seeks to share lessons on how to make the best use of accrual information, from countries that have fully implemented accruals.

Governments that are on the journey to implement accrual accounting, and those that have so far not begun the journey, can consider how best to use the information they will get from accrual accounting for the public good. Finance officials in these countries can learn best practices that will maximise the value of accrual reporting and/or budgeting once it has been implemented. This report helps those governments and finance officials by showcasing ways that governments from around the world are currently using accruals-based information to help address difficult challenges in the provision of public services.

This report is based on research that addressed the following questions.

1. What have governments achieved by way of benefits following the implementation of accrual accounting? (See Chapter 2).

2. What goals and objectives did governments set themselves to generate better information for the benefit of citizens as part of adopting accrual accounting? (See Chapter 3).

3. What lessons can governments undergoing the implementation of accrual accounting learn, about how |to get the best use of information from accrual accounts, from those who have already completed this journey? (See Chapter 3 and Chapter 4).

4. What lessons can governments learn about how best to structure their implementations, including processes, training, and technology, to maximise the benefit of accrual accounting? (See Chapter 3 and Chapter 4).

The roundtables involved experts from different levels of government who have direct experience of deriving benefits for citizens from information that is available as a consequence of implementing accrual accounting in the public sector.

The research evidence was gathered in three ways. **Roundtable discussions** were held in three countries (the UK, Canada and Australia) that have implemented accrual accounting in their public sectors to ascertain lessons learned that can be shared with governments that are in the process of implementation. The roundtables involved experts from different levels of government who have direct experience of deriving benefits for citizens from information that is available as a consequence of implementing accrual accounting in the public sector.

The roundtable discussions were based on a discussion guide to ensure similar topics were covered in each of them. They gave the participants the opportunity to discuss how objectives or goals for producing information to benefit citizens were set as part of the accrual accounting implementation; to identify specific applications of accrual accounting information for the benefit of citizens; and to reflect on and share best practices.

Semi-structured expert phone interviews were held with 12 experts in seven countries: Austria, Canada, New Zealand, Slovakia, Switzerland, Tanzania and Zimbabwe. These interviews covered the same topics as the roundtable discussions, adding more depth and a broader range of real-life examples to the evidence base.

The face-to-face and telephone evidence was supported by a desk-based **literature review**. This review was used to inform the context and to outline potential benefits and recommendations directed at governments and finance professionals derived from reported experiences or lessons learned.

The findings of the research, and recommendations flowing from them, make up the bulk of this report. To set the scene, the next chapter describes the current reporting environment for governments around the world.

1. A time of transition: the current reporting environment

'Accrual accounting information… provides a comparative advantage to entities that possess and employ it'. **(Rowles 2004)**

Good public financial reporting is essential to addressing the problems highlighted by global economic and fiscal crises. It informs government policy and helps to make national economies, and public services, more sustainable and resilient over the long term. Accruals-based accounts provide more complete information than cash-based accounts and IFAC and other institutions encourage governments to implement accruals-based accounting. Furthermore, IFAC and ACCA support IPSAS as the only set of internationally recognised standards for accrual accounting in the public sector.

Ian Ball, ex-CEO of IFAC,[2] commented that: 'it seems unfathomable that, for an entity as complex as the government, anything would do except accrual accounting and budgeting'. Public sectors are by their nature large and complex, but also need to provide stability and sustainable foundations for any prosperous society. The adoption of accruals is a cornerstone of good governance and can support countries working to improve their systems of public financial management (PFM).

WHAT IS ACCRUAL ACCOUNTING IN THE PUBLIC SECTOR?

Given the experts' views on the necessity of accruals, it is important to define what we mean by cash or accrual accounting in the public sector context. The simplest way of preparing accounts is to include transactions only when money is paid out or received. Accounts drawn up in this way are said to be prepared on the cash basis or the receipts and payments basis.

Although relatively straightforward to do, cash accounts do not give the full picture of an organisation's finances at any specific time. They do not show if the organisation is owed a lot of revenue from its debtors (whether they are customers or taxpayers), nor whether goods or services have been acquired on credit and there are invoices to be settled, nor what assets are owned by the organisation and whether the organisation is managing and making best use of its assets, or if money has been borrowed and must be repaid with interest.

From a private sector perspective, cash-based accounts do not show whether a profit or loss has been made and this makes them unsuitable for businesses. For governments and public sector organisations, not being able to determine whether a surplus or deficit has been made may not be as immediately critical as in the private sector and hence many governments maintain their accounts on the cash basis.

Around the world there is a drive for all governments to draw up their accounts on an accrual basis because, unlike the cash basis, it gives a fuller picture of an organisation's financial position and financial performance by bringing into the accounts all the revenue, expenditure, assets and liabilities that comprise the government's financial position at a defined point in time.

Accrual accounting (also known as the 'income and expenditure basis' of accounting) is a system which recognises income and expenditure transactions in the period they are earned or incurred rather than at the time when payments are received or made. This has the advantage that income for a period is shown against the expenses taken to generate the income. It enables the production of a balance sheet (also called a statement of financial position) that shows the value of assets and liabilities at any given time.

2 Ian was also the chair of IFAC's Public Sector Committee, which was replaced by the International Public Sector Accounting Standard's Board (IPSAS) in 2004.

The inference is that comparatively economically developed countries in the OECD were more likely to be reporting on an accrual basis.

IMPLEMENTATION OF ACCRUALS AROUND THE WORLD

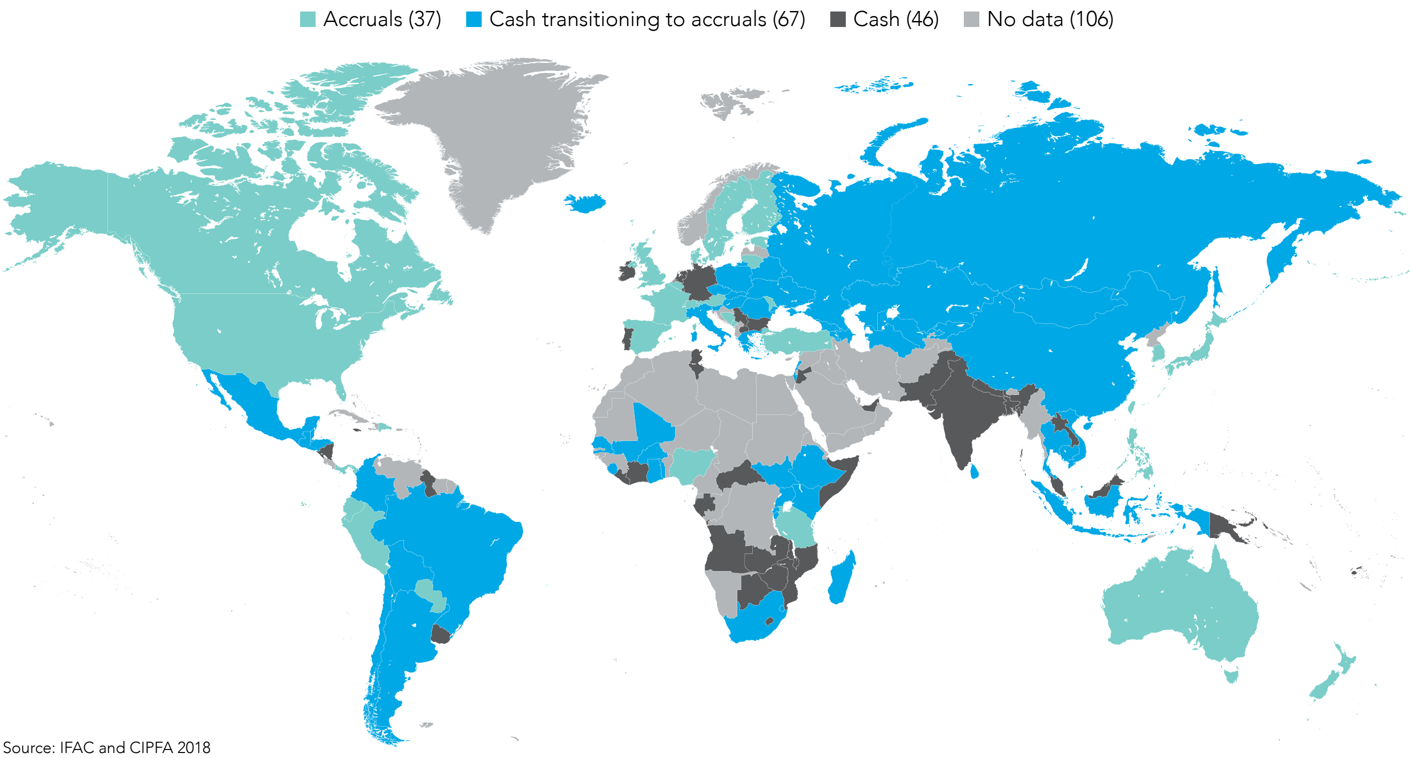
The *International Public Sector Financial Accountability Index 2018 Status Report* ('Status Report'), published by IFAC and CIPFA (2018), provides a comprehensive view on the current accounting arrangements for 150 central governments and sets out their plans for the five years from 2018 to 2023. Of the 150 governments taking part in the *2018 Status Report*, 37 used accrual accounting for financial reporting basis, 46 used cash accounting and 67 (45%) were in the process of transitioning to accrual accounting (IFAC and CIPFA 2018). Some of this latter category were close to the end of the process, and were expected to prepare their first accruals-based accounts for the 2018 financial year.

Countries using accruals-based accounting at that time in Europe included Austria, France, Spain, Switzerland, Sweden, Finland, the UK, and Turkey. In Africa there were only two countries using accruals: Nigeria and Tanzania. In the Americas, there were Canada, the US, Ecuador, Peru, and Paraguay; in Asia, there were Japan, South Korea and the Philippines. Finally, in Australasia, Australia and New Zealand use accruals. Since the *2018 Index* was released, more countries have published accrual balance sheets, including Chile and Colombia.

The Organisation for Economic Cooperation and Development (OECD) completed a similar survey of its 34 member countries in 2016. Its subsequent report, *Accrual Practices and Reform Experiences in OECD Countries*, stated that around 75% of OECD member countries used accrual accounting (OECD and IFAC 2017). Therefore, compared with the global results identified in the *2018 Status Report* (IFAC and CIPFA 2018), the inference is that comparatively economically developed countries in the OECD were more likely to be reporting on an accrual basis.

The OECD report also identifies that there are differences in the extent to which countries use accrual accounting. Most member countries prepare balance sheets that include tangible non-current assets, such as infrastructure, but only a minority include, for example, natural resources.[3] On the liabilities side, a

FIGURE 1.1: Current financial reporting basis from the International Public Sector Financial Accountability Index



Source: IFAC and CIPFA 2018

3 IPSASB (2019) has a project on natural resources in its current workplan.

> Only 15 of the 37 governments using accruals for accounting reported that they prepare their budgets on the accrual basis.

significant number of countries do not include amounts owing related to public-private partnerships or the liabilities relating to government employees' pensions.

For budgeting, only around 25% of OECD countries prepared their budgets on the accrual basis, although practices differed. Not all those countries prepared, for example, a budgeted balance sheet. Therefore, even when the *2018 Status Report* (IFAC and CIPFA 2018) cites a country as reporting on an accrual basis, there can still be considerable variation in practice across jurisdictions.

CURRENT FINANCIAL REPORTING FRAMEWORK

The *2018 Status Report* also shows the financial reporting framework used by the 150 jurisdictions (IFAC and CIPFA 2018). Of the 37 countries that used accruals for their financial reporting in 2018, 19 (51%) used International Public Sector Accounting Standards (IPSAS), either directly (five countries), indirectly via their own national standards (five countries), or as a reference for their national standards (nine countries).

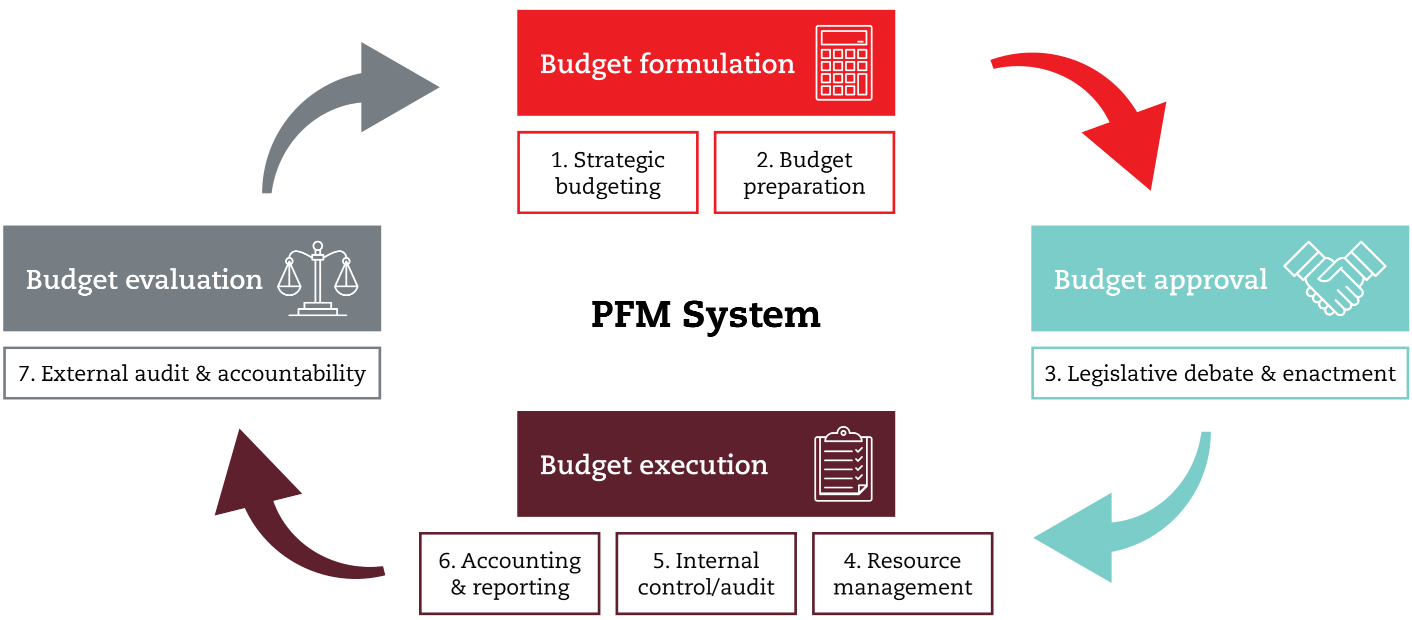
The *2018 Status Report* also shows that there will be a significant increase in the number of countries that will be referencing IPSAS in the production of their accounts – of the 98 governments projected to be reporting on accruals by 2023, 72 (73%) will be making use of IPSAS in some form by 2023.

THE ROLE OF ACCRUALS IN THE PUBLIC FINANCIAL MANAGEMENT SYSTEM

The *2018 Status Report* makes the observation that using accrual accounting as the basis of financial reports does not necessarily mean that a government will prepare and execute its budget on the accrual basis. Only 15 of the 37 governments using accruals for accounting reported that they prepare their budgets on the accrual basis.

The management of public finance typically has many stages in any one jurisdiction, but Figure 1.2 provides a simplified view of a PFM system. The implementation of accruals for financial reporting is only part of PFM system, with reporting on an accrual basis typically only affecting stages 6 and 7 in the simplified system shown in Figure 1.2 (ie the financial reporting and external audit of those accounts). The use of accruals-based budgets extends the scope of accruals-based information in the PFM significantly (stages 1 and 2, 4 and 5 in Figure 1.2).

FIGURE 1.2: A simplified view of a typical PFM system



Source: Adapted from Andrews et al. 2014

> The index shows that 40% of countries intend to complete the transition to accrual accounting by 2023. These countries are the primary audience for this report.

Furthermore, appropriations — the authorisation of a government entity to spend public money (stage 3 in Figure 1.2) — is a critically important mechanism for a government to use to control its expenditure. A large majority of the OECD countries use cash appropriations and the OECD report authors suggest this may be because they 'are wary of the volatility and discretion in accrual valuation when it comes to control over resources spent by ministries and departments' (OECD and IFAC 2017: 9).

Subject matter experts interviewed for this research argued that there were advantages for governments in consistently applying an accrual basis through the entire PFM system. They strongly supported this approach for producing rich, decision-useful information for governments (see Chapter 2 below).

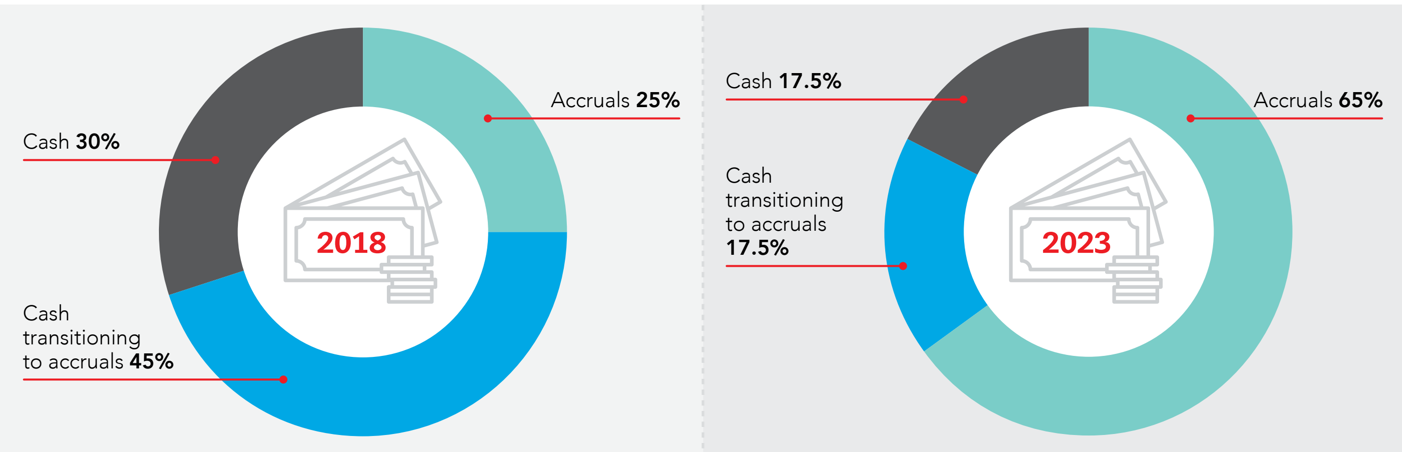
LOOKING AHEAD

Over the few years to 2023, the number of countries reporting on the accrual basis is expected to increase from 37 to 98. The largest increases are projected to be in Africa, where it is forecast to rise from 2 countries to 19 and Asia where is will rise from 6 countries to 21. There is also a substantial shift occurring in Latin America, where most countries plan to move to accruals-based accounts by 2023. Over the same period, the number of countries using cash accounting is expected to fall from 46 to 26, so there will be some new countries undertaking the process of adopting accruals, even if this is not complete by 2023.

The motivation for this significant shift to accruals is debatable. In *IPSAS Explained*, Thomas Muller-Marques Berger (2018: 47) argues that the motivation for reform in developed countries is often intrinsically driven (eg from a desire to improve the information available for political decision making), while developing economies are often driven by extrinsic motivations – such as enhancing trust and credibility.

Figure 1.3 shows that a considerable shift was planned between 2018 and 2023 from the 2018 dominance of cash accounting towards accrual accounting. As Allen Schick, professor at the University of Maryland School of Public Policy, rightly observed *'in the past, [accruals-based accounting] information was "good to have", now it is "must have"'* (Schick 2013). The index shows that 40% of countries intend to complete the transition to accrual accounting by 2023. These countries are the primary audience for this report: the next two chapters will set out the benefits of decision-useful information and the lessons learned, derived from roundtables and interviews with experts in the countries that have completed accruals implementation.

FIGURE 1.3: Global aggregate of 2018 vs future (2023) financial reporting basis



Source: IFAC and CIPFA 2018

2. The benefits of accruals in the public sector

This chapter outlines the wide variety of benefits that accrual accounting information can bring to public sector organisations.

Primarily, these benefits relate to better public service delivery, where better information improves the decisions made within the organisations, ultimately leading to improvements in performance and value for money. There are external reporting benefits, too. The users of financial reports get more and better information to use in the decisions they make as service users, lenders, or lobbying groups.

ACCRUAL ACCOUNTING IS NOT THE END GOAL

Experts across ACCA and IFAC's global networks were asked what the primary benefits of implementing accruals were in the public sector. In identifying these benefits, it became clear that implementing accrual accounting should not be considered the end goal – but instead a means of supporting a range of other objectives, such as improving government performance and more effectively managing public sector assets.

For example, Bailey Church, a partner at KPMG Canada, said: 'it has to be about how accrual accounting supports the achievement of other mandates and visions'. The narrow objective of producing accounts is clearly insufficient. Ian Ball echoed this view by saying that, in the case of New Zealand: 'accrual accounting was not the objective. It was a corollary to the objective, which was improving performance, both in terms of delivering services, but also managing the balance sheet of the government'. Many of the experts consulted identified transparency, accountability and better information for making decisions as the overriding benefits that have been achieved in moving to accruals.

BENEFITS BY ACCOUNTING AND BUDGETING BASIS

There is also evidence that these benefits will vary, depending on the level and type of implementation. Table 2.1 sets out the benefits and levels of complexity arising from different models of financial reporting and budgeting. Governments reporting and budgeting on a cash basis (Column A) can achieve basic fiscal discipline through the allocation of cash budgets. It is also a comparatively simple basis that is more easily understood by non-financial staff and the public.

Column B describes the benefits observed for governments reporting on an accrual basis, but still operating cash budgets (which is a common arrangement among OECD countries, for instance). There are a range of benefits that can arise here, such that governments are able to support long-term, financially sustainable decision making. With this comes a level of public scrutiny, through the creation of new channels of accountability and by providing fiscal credibility. Nonetheless, as Bailey Church of KPMG, Canada, explained: 'Where you adopt accrual accounting, but not budgeting, you do get certain benefits in terms of the reporting and the transparency around financial information, but you do not truly see the shift in decision making'.

Finally, Column C shows the benefits observed by jurisdictions operating on an accrual basis for both financial reporting and their budgeting process. Taking this approach is instrumental in putting finance at the heart of government decision-making, as public officials will be best placed to respond to financial information that is made available through budget execution using accrual

TABLE 2.1: Benefits and complexity arising from each accounting and budgeting basis

	(A) CASH ACCOUNTING AND CASH BUDGETING	(B) ACCRUAL ACCOUNTING AND CASH BUDGETING	(C) ACCRUAL ACCOUNTING AND ACCRUAL BUDGETING
BENEFITS	• Provides basic fiscal discipline • Simpler / intuitive for non-financial staff and the public	Facilitates public scrutiny • Improved accountability • Provides fiscal credibility Achieving value for money and financially sustainable decision-making • Managing assets well and accounting for the maintenance backlog • Managing liabilities and identifying fiscal risks • Reducing fiscal illusions and improving incentives • Supporting long-term thinking	The benefits in Column B **PLUS** Puts finance at the heart of decision-making • Embeds performance management • Improves medium-term forecasting and planning o Further enhances fiscal credibility • Effective project management across government • Embeds the finance function in day-to-day decision-making
LEVEL OF COMPLEXITY	**Low**	**High**	**Medium**

accounting. By focusing on performance management through accrual accounting and budgeting, governments will benefit from improved effectiveness through performance and project management, and further improve value for money.

There is no doubt that cash accounting and budgeting are the simplest options. It is more complex to complete accrual accounts, and the users of the accrual information require extra knowledge and training to understand it. This additional complexity must be counterbalanced by the benefits that the experts identified from creating accrual information.

In certain respects, the mixed approach of accrual reporting and cash budgeting can be viewed as the most complex of the three options. This is because it requires government entities and decision makers, such as ministers, to operate across dual accounting bases for appropriations, budgeting, and the reporting of their entities' financial positions. Experts commented on the risks of this mixed approach. For example, Veronica Povey from the UK Treasury asked: 'What's the incentive to do accrual accounting well, if you are not budgeting on an accrual basis? Otherwise it could just become that theoretical exercise that you do at the end of the year. You do not get the same broad buy-in or accountability'.

The experts noted a higher degree of complexity resulting from an inconsistent basis between appropriations, budgeting and reporting – which will reduce the comparability between governments' financial information and can obstruct proper financial accountability.

The remainder of this chapter describes the benefits of accrual accounting identified by ACCA and IFAC's global network of experts, using the structure of Table 2.1 to understand at what stage of maturity these benefits occur.

COLUMN B: BENEFITS OF ACCRUAL ACCOUNTING, WHILE BUDGETING ON A CASH BASIS

Transparency and facilitating public scrutiny

The information created by reporting public accounts on an accrual basis creates opportunities for improving accountability and transparency. This view resonated with the global community of experts interviewed for this project. This is particularly the case where the new information presented in accrual accounting facilitates conversations by decision makers and the public on the appropriate allocation of public resource.

Bernhard Schatz saw that accrual accounting 'provides [opportunities for] public scrutiny and also means that the government will get questioned and contested on that new information'. Lucia Kasiarova explained the range of new information made available through accrual implementation in Slovakia:

> *'Everyone in the public sector now must produce financial statements that are publicly available, with consolidated statements at a department level. There is increased transparency through annual report of the Slovak Republic. There is transparency over state-owned enterprises, which was never done before. With the audit of the accounts there is increased confidence in the numbers. Overall there is increased availability and quality of financial information'.*

The additional information made available through accruals has provided new avenues through which key stakeholders can understand government activity. At the same time, the implementation of accrual accounting can create barriers to effective transparency.[4] The increased technical complexity of accrual accounts means that sharing more information will not always result in better political discourse on the use of public resource.

4 See the work by David Heald on the difference between nominal and effective transparency (eg Heald 2015).

> **Accountability is a critical element of good governance and the delivery of effective public services. At its core, it is about the relationship between the state and its citizens; setting out the ways in which the state is answerable for its actions.**

Therefore, governments must consider how best to communicate the new information arising from accrual accounting. This is acknowledged by Tanzania's Neema Mssusa, who said that: 'we have been able to give too much information to the citizens, information which was not there before. I sometimes ask myself, if the information which we are providing to the citizens, to the parliament, to the politicians, to the government is understandable?'

Nonetheless, several of the experts said that moving to accruals-based accounts, and in particularly following IPSAS, means that information is being produced in a consistent manner across the public sector, making the information more accessible. In addition, Lucia Kasiarova said that 'the [accrual] information is more understandable by more people as it is more comparable with private sector accounts', and this was echoed by Andreas Bergmann from Switzerland, who in commenting on the background of Swiss ministers said 'most parliamentarians are not full timers. Most of them work in a company… they're more likely to understand the normal double-entry bookkeeping environment'.

It was noted that accrual accounting can strengthen the accountability mechanisms in government. Accountability is a critical element of good governance and the delivery of effective public services. At its core, it is about the relationship between the state and its citizens; setting out the ways in which the state is answerable for its actions (Controller and Auditor General of New Zealand 2016). This is particularly important for the public sector finance function, which has a critical role to play in managing the use of public resources for the benefit of citizens. This was supported by an official from the Commonwealth Government in Australia, who said 'the big change [following accruals implementation] has been in the balance sheet focus in resource management and, obviously, accountability for individual entities, and that's passed on to decision makers'. Parliamentary committees have played a role in holding governments to account by using the new information provided by accrual accounting. This is evident through the work of the Public Accounts Committee in the UK (see Chapter 3 below for more on this) and in other jurisdictions, including Tanzania, where Neema Mssusa said of parliamentary committees: 'They represent the citizens, and as a result, they are the ones who will hold the government accountable'.

Fiscal credibility

The transition to accrual accounting can also improve the fiscal credibility of a government. Vicky Rock, director of public spending at the UK Treasury, noted that 'in the fallout of the [2009] financial crisis there was a lot of interest from credit rating agencies in the IFRS [International Financial Reporting Standards] accounts and the position of the UK public sector's balance sheet, which helped in preventing further credit downgrades during the crisis'. Working from an internationally accepted set of standards, such as IPSAS, also supports the comparability of accounts between jurisdictions. This international comparability can further reinforce fiscal credibility – as countries are able to benchmark their financial performance with international peers.

For developing or less mature economies, the move to accrual accounting can lead to increased confidence in PFM. In Slovakia, the move to accrual accounting was part of a package of reforms aimed at producing multi-year, results-oriented budgets to improve the debt and liquidity systems and, as explained by Lucia Kasiarova, 'to get acceptance of accrual accounts as part of broader objectives around improving the reputation of Slovakia and to be considered for [admission to the] European Monetary Union'.

In addition, the production of a public sector balance sheet can provide more information, which improves economic outcomes in the country. Ian Ball, the ex-CEO of IFAC, argued that 'net worth is the most comprehensive measure of fiscal position that a government can have'. There is evidence in the literature that the net worth perspective is beneficial for the broader economic outcomes in a country. In late 2018, the IMF *Fiscal Monitor* published a report which estimated that, globally, governments had public assets

Most government decisions have a financial aspect and knowing what the government owns and owes, as well as understanding the economic reality of its activities, improves the quality of the decisions that are made.

worth over 200% of GDP. Figure 2.1 shows the result of adopting a net wealth view of a nation's financial position. Using this lens, Japan – with a notoriously high public-debt-to-GDP ratio – has a net wealth position near zero. Other countries, such as the UK and Portugal, have substantial negative net worth in excess of 100% of GDP. The IMF analysis also shows that improving a country's net worth can provide substantial benefit, including paying lower interest on debt and having shorter and shallower recessions (IMF 2018).

Achieving value for money and financially sustainable decision-making

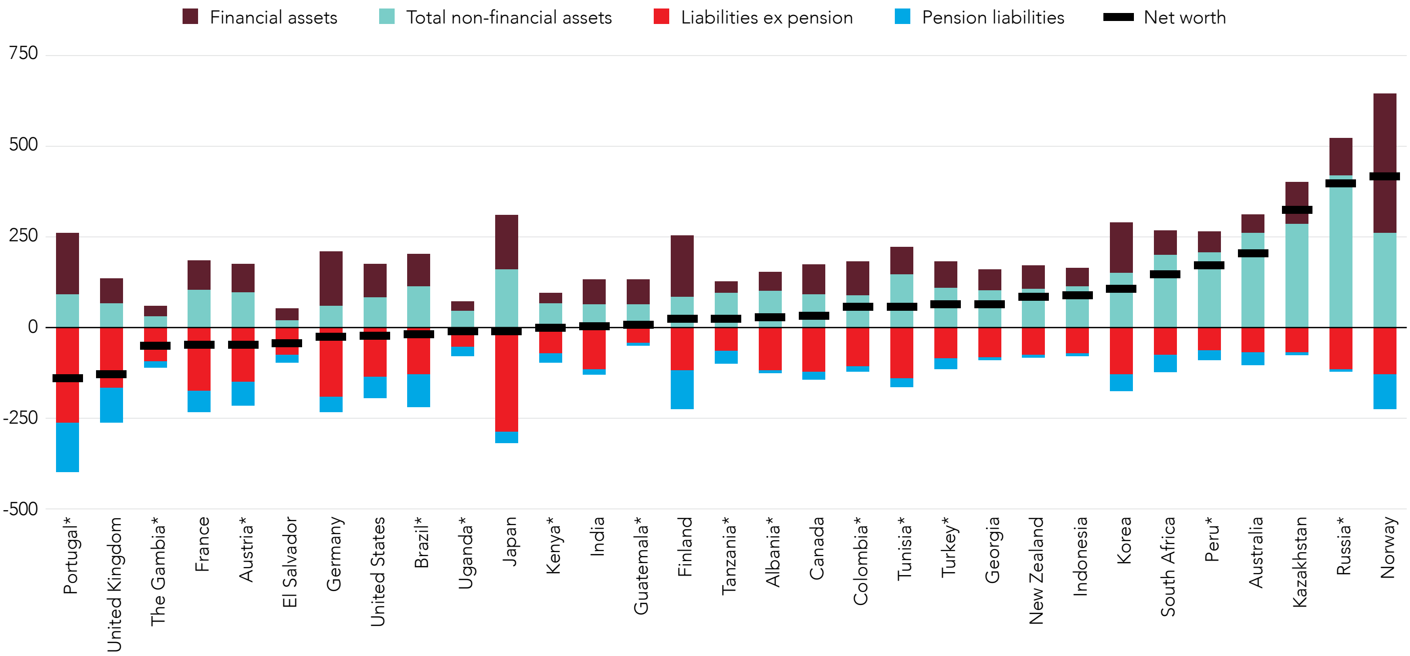
The foundation of good decision making is having the right information. Most government decisions have a financial aspect and knowing what the government owns and owes, as well as understanding the economic reality of its activities, improves the quality of the decisions that are made. Similarly, using accrual information to make good decisions about the relative value for money of different alternatives involves properly understanding the costs of policy options for government. For jurisdictions adopting accrual accounts this can arise through a better understanding of the assets owned and how they are being used in provision of public services. This was summarised by Ross Smith, Program and Technical Director of the IPSAS board: 'If you do not know what you have, you cannot manage it. Many claim that there are way other ways and information available, however, without proper accrual accounts there will always be information gaps'.

Accrual accounting addresses these information gaps and provides the information required to improve value for money and financially sustainable decision making. This occurs through the ability to:

- manage assets better and account for the maintenance backlog
- manage liabilities and identify fiscal risks,
- reduce fiscal illusions and perverse incentives, and
- support long-term thinking and planning.

These four aspects of the benefit of financially sustainable decision making are illustrated in the following four sections, using experts' comments.

FIGURE 2.1: Public sector balance sheets (percentage of GDP)



Source: Reproduced from IMF 2018.

*Based on a single year of data, in most cases compiled as part of the Fiscal Transparency Evaluation: Albania, 2013; Austria, 2015; Brazil, 2014; Colombia, 2016; The Gambia, 2016; Guatemala, 2014; Kenya, 2013; Peru, 2013; Portugal, 2012; Tanzania, 2014; Tunisia, 2013; Turkey, 2013; Uganda, 2015.

> Accrual accounting recognises the wear and tear of non-current assets through impairment if there is a deterioration in the condition of assets.

a) Managing assets well and accounting for the maintenance backlog

In the private sector non-current assets are valued, in general, on their potential to generate income in the future. There are some public sector organisations, such as SOEs, which invest in non-current assets in order to generate future income, but generally public sector non-current assets are held because they are needed for the delivery of public goods or services. These non-current assets often have a long lifespan (such as roads, sewer systems, power grids) and provide services to the public that are so important they would likely need to be replaced if they were damaged.

It is important that non-current assets are properly managed and maintained. Cash-based accounting can discourage maintenance since it would be recognised as a cost only if money is spent on maintenance. Accrual accounting recognises the wear and tear of non-current assets through impairment if there is a deterioration in the condition of assets. As Portugal's Joao Carlos Fonseca, noted: 'You can have risks when the assets are not being properly maintained'.

The UK's approach to accrual reporting has provided new information on the state of the government's assets and aids in identifying where asset maintenance is inadequate. Similarly, Eliza McLaren, Corporate Accountant from the Regional Municipality of York in Canada, said that in Canada 'accrual accounting definitely highlights proper asset management'. The accrual budgeting approach means that maintenance expenditure needs to be considered for assets that are constructed or acquired for use by the public sector. 'It's not just "now you build something", but "now you're going to have something in your budget next year to maintain it"'. Understanding your assets also allows a discussion on stewardship, in particular considerations of accompanying risk and with that the insurance and security over assets.

Libby Stratford from Australia succinctly summarised this by asking 'if you have never valued an asset in the first place, how do you then assess risk to it?'

Accrual accounting information can also help when thinking about what to do when an asset comes to the end of its useful life. As mentioned above, it is often the case that the asset needs to be replaced for public services to continue to be delivered. Eliza McLaren described how accrual accounting information can help government organisations to understand that assets on the books need to be replaced at some point. This information is useful for decision makers in understanding where additional resource should be allocated to finance the replacement of the assets.

Neema Mssusa highlighted an example in Tanzania where accruals-based information has been used to challenge the performance of infrastructure projects. In this case, the valuation of assets, and the use of impairments, entered the debate on the value for money derived from public projects:

> *'So officials [were] saying that we have water wells; we did 20 this particular year. But then we went further to say, okay, but is there water? If you built that, but there is no water, then it doesn't have any benefits to the public. And it probably is impaired, and should not be recorded'.*

The use of impairments provided a new mechanism for identifying assets that were not providing value to citizens, such as wells without water or incomplete schools. This reporting can be helpful in improving the management of assets and ultimately improving the quality of public services derived from government assets.

Maintaining a sustainable financial position requires public entities to deal with the uncertainties and risks that are inherent in a government's activities.

b) Managing liabilities and identifying fiscal risks

One of the objectives of PFM is to maintain a sustainable financial position. This requires the effective management of a government's liabilities, while also identifying – and working to mitigate – the fiscal risks that could affect the financial position of the government. As Bernard Schatz from Austria explains:

> *'You have a plan to balance your budget, and then something unexpected [often] happens. Perhaps, you need more money for pensions, or you need more for a legal claim you have to settle. So, your budget planning will always be disturbed by this kind of future cash need you had not anticipated. And that's where accrual accounting comes in'.*

Maintaining a sustainable financial position requires public entities to deal with the uncertainties and risks that are inherent in a government's activities. The implementation of accrual accounting has had important implications for policy discussions in several of the jurisdictions represented by interviewees for this project. Ian Ball gave an example from New Zealand, where a decision was made to move public servants off a defined-benefit pension scheme. He said accrual information enables 'high quality financial decisions that reflect real resource use not just cash flow. If you're building up a pension liability, that's part of your financial position and you need to be accounting for it. It seems to me that better information facilitates better decisions and better accountability'.

Similarly, in Austria provisions have informed the policy debate. Austria is currently failing to meet the terms agreed with the European Union on carbon emissions, which prompted the debate on the need for a provision. Bernhard Schatz commented that through accrual accounting 'the consequences of not meeting promises becomes more transparent. These debates create urgency and awareness. [Accrual accounting] also gives you information for decision making, so that if you, for example, reduce carbon emissions under a trading scheme you can reduce the respective liability and show success. This kind of liability management is a really important feature [of accrual accounting]'. These two examples highlight how accruals can provide new information to decision makers that can influence important areas of public finance.

Accruals can benefit jurisdictions by providing information to improve the management of liabilities. This was observed in New South Wales (NSW) Australia where, in the 2018/19 Budget (see NSW Government 2019: Chapter 8,), the state became the first in Australia to establish a sovereign wealth fund, the NSW Generations Fund (NGF). This initiative is intended to help the government maintain sustainable debt levels consistent with a triple-A credit rating, helping support current and future generations. The government established this dedicated debt retirement fund to provide a sustainable approach to debt reduction. NSW Australia takes an active approach to balance sheet management through the NGF, which is intended to support the government's infrastructure programme without burdening future generations with unmanageable debt.

Box 2.1: NSW Generations Fund video case study

ACCA and IFAC produced a series of video case studies showcasing good practices in PFM from around the world. Scan the QR code to learn more about the Generations Fund in NSW Australia. ■

Accrual accounting also creates new information on contingent liabilities, which can be helpful for governments in identifying fiscal risks.

Accrual accounting also creates new information on contingent liabilities, which can be helpful for governments in identifying fiscal risks. A participant the UK roundtable noted that guarantees on private investment were historically offered as an uncosted policy option – but, with the implementation of accrual accounting, these guarantees are recorded as contingent liabilities that could affect the balance sheet and budget were the liabilities to crystallise.

Independent fiscal policy institutions, such as the Office of Budgetary Responsibility (OBR) in the UK, use accrual information in their fiscal risk reports[5] in order to understand the fiscal risks that could put pressure on the public finances in the medium term. Analysis by the IMF shows that realised contingent liabilities can have substantial impact on public sector balance sheets. Between 1990 and 2014, the IMF recorded 230 contingent liability realisations with an average fiscal cost of 6.1% of the affected country's GDP. Significant contingent liabilities in the financial sector created particularly large fiscal costs for public sectors, with one jurisdiction facing a financial sector liability of 56.8% of GDP (Bova et al. 2016).

c) Reducing fiscal illusions and perverse incentives

A publication by the International Monetary Fund defines fiscal illusions as 'accounting devices that give the illusion of change without its substance, or that make the change appear larger than it actually is' (Irwin 2012). There are many examples of fiscal illusions, such as the 'fire sale' of an asset that is counted as revenue, where the information generated by accruals will mitigate the illusion and can support sustainable decision making in public finance. The analysis identified that cash accounting produces fiscal illusions that can be manipulated through (i) changes to the accounting boundary, (ii) the timing of payments, (iii) the classification and recognition, and (iv) reductions in net worth.

(i) Accounting boundary. It is only possible to provide a full financial picture of the resources and risks for the public sector if there is full consolidation, which must include SOEs at 'whole of government' level. This full picture of liabilities enabled a discussion in the Swiss Parliament about government borrowing, particularly on the raising of debt through SOEs, where consolidated accrual information provided a full picture of government borrowing.

TABLE 2.2: Average fiscal cost of contingent liability realisations, 1990–2014

TYPE OF CONTINGENT LIABILITIES	NUMBER OF EPISODES	NUMBER OF EPISODES WITH IDENTIFIED FISCAL COSTS	AVG. FISCAL COSTS (% GDP)	MAXIMUM FISCAL COSTS (% GDP)
Financial sector	91	82	9.7	56.8
Legal	9	9	7.9	15.3
Subnational Government	13	9	3.7	12.0
SOEs	32	31	3.0	15.1
Natural disaster(s)	65	29	1.6	6.0
Private non-financial sector	7	6	1.7	4.5
PPPs	8	5	1.2	2.0
Other	5	3	1.4	2.5
Total	**230**	**174**	**6.1**	**56.8**

Source: Bova et al. 2016

5 For example, the UK OBR publishes detailed fiscal risk reports, such as OBR 2019.

It is only possible to provide a full financial picture of the resources and risks for the public sector if there is full consolidation, which must include SOEs at 'whole of government' level.

Andreas Bergmann stated that:

> *'In total, the consolidated liability position in Switzerland was about four times the non-consolidated government bond position. And so [the consolidated information] might caution the shifting [of debt to state-owned enterprises] and I think that's certainly one of the main benefits. That we haven't seen very much shifting going on in Switzerland and having accruals in place certainly helped [us in] not committing this error'.*

The UK's *Whole of Government Accounts 2017/18* provides another illustration of the need for a full financial picture to avoid fiscal illusions that could hinder decision-making. Figure 2.2 shows the reconciliation between public sector net debt (PSND) and the total net liabilities from the UK's *Whole of Government Accounts*. Many officials and external stakeholders to government (eg media) focus their attention on the PSND, which was reported as £1.779bn in 2017/18. The adjustments in Figure 2.2 show a more consolidated view of the UK government results in total net liabilities that are £786bn higher than the PSND, at £2.565 trillion. The *Whole of Government Accounts*, prepared using accruals, give a much more holistic picture of the UK government's financial position compared to PSND.

FIGURE 2.2: UK Whole of Government Accounts (WGA) 2017–18 PSND to total WGA net liabilities

	2017-18 £bn	2016-17 £bn	2015-16 £bn
Public Sector Net Debt (National Accounts)	**1,779**	1,727	1,603
Add liabilities not recognised in National Accounts:			
Net public sector pensions liability	**1,865**	1,835	1,425
Provisions	**422**	322	306
PFI contracts	**33**	33	33
Adjust assets measured differently in national accounts:			
Asset Purchase Facility	**(200)**	(127)	(50)
Unamortised premia on gilts	**54**	51	38
UK Asset Resolution (UKAR) net impact on net debt	**(10)**	(24)	(30)
Add assets & liabilities excluded from measure of PSND:			
Property, plant and equipment	**(1,208)**	(1,168)	(1,120)
Investment property	**(20)**	(18)	(16)
Intangible assets	**(36)**	(35)	(33)
Trade and other receivables	**(42)**	(49)	(37)
Prepayments and accrued income	**(103)**	(91)	(87)
Inventories	**(10)**	(9)	(10)
Investments	**(52)**	(51)	(50)
Trade and other payables	**53**	51	51
Accruals and deferred income	**62**	59	55
Deduct liabilities not yet recognised in WGA			
Housing associations	**-**	(70)	(67)
Other adjustments including eliminations	**(22)**	(15)	(25)
Net liabilities (WGA)	**2,565**	2,421	1,986

Source: HM Treasury 2019: 237

It is better, therefore, to use accrual accounting, which identifies liabilities and puts a value on them so that the organisation can plan its finances in a sustainable way that can enable it to meet its liabilities.

Failure to identify liabilities exposes an organisation to risks. It is better, therefore, to use accrual accounting, which identifies liabilities and puts a value on them so that the organisation can plan its finances in a sustainable way that can enable it to meet its liabilities. As Andrew Evans, Head of Public Expenditure Classification Branch at HM Treasury UK, explained: 'Having accruals is helpful in understanding the boundary of the public sector, which you do not necessarily have in a cash environment. It creates conversations around liabilities the government are exposed to that might not otherwise be accounted for'.

The additional information provided through accrual accounting means that government decision-makers are better informed on the range of liabilities and risks facing the public sector – and can then consider what steps should be taken to reduce or mitigate these challenges.[6]

(ii) Timing. Bernhard Schatz from Austria described a different type of fiscal illusion: one that is created by the manipulation of the timing of government payments. Governments using cash accounts can be tempted simply to postpone their payments to suppliers or lenders in order to choose the financial year in which the transactions appear. In doing this, the government will 'incur additional costs, interest costs, usually with [its] suppliers, but [they] just agreed to pay next year, or up to five years later' and this could well be worse value for money than making the payment at its original due time. This is a typical feature of fiscal illusions that occur in a cash accounting environment: not only is the financial position misstated, but this often comes at the cost of poorer value for money in order to achieve the illusion.

(iii) Classification and recognition. Ken Warren, the chief accounting adviser from the New Zealand Treasury, explained that the introduction of accruals-based information has improved decision making in government by setting out the proper classification of transactions. For example, recognising that monies contributed to a project, where the expectation of repayment is likely to be suspended, are grants rather than loans. As a result of this change in classification, the government was able to makes decisions based on a better understanding of the financial consequences of these payments.

Public-private partnerships (PPPs) represents a policy area where the accurate recognition of liabilities is important. PPPs are a major mechanism used by governments to deliver large-scale infrastructure and other capital projects. In the UK the Private Finance Initiative (PFI) policy was a specific implementation of PPPs. The PFI began in the early 1990s and, for many years, PFI projects were accounted for as long-term service contracts (like operating leases) without any recognition of assets or liabilities on the balance sheet. As Olivia Halliday, of UK's HM Treasury noted, accrual accounting means 'we are more aware of the long-term costs arising from PFI'. The information made available through accrual accounting gave the UK's past chancellor of the Exchequer, Philip Hammond, 'compelling evidence' that PFI did not provide value to the taxpayer (Hammond 2018).

(iv) Reducing net worth. Relying exclusively on cash accounting can give the illusion that a project or programme is better value for money than it really is. This is particularly important in cases where governments are working within predetermined fiscal limits that do not account for changes to the balance sheet (see Box 2.2 on fiscal rules).

Joao Carlos, a principal staff member from the IPSAS board, set out the fiscal illusions that can result in the mismanagement of assets.

> *'Why is the asset register not enough? Because when you sell an asset you get the cash and say "I'm okay". But it doesn't show your net profit or loss. In a cash environment the fiscal illusion is really powerful because a sale shows that I'm cash rich, but doesn't show whether I gained or lost – the overall impact on the organisation's financial position and financial performance'.*

6 See the next section for a discussion of fiscal risks.

> '[Accruals] makes you think about the future, not just the here and now'.
>
> Veronica Povey
> UK Treasury

The information provided through accrual accounting means that government decision makers will be made aware of the balance sheet implications of a financial decision. The benefits of having a strong net worth position, as described in the IMF study on page 20, suggest that governments should consider using net public sector wealth as a key indicator in setting their fiscal rules.

d) Supporting long-term thinking. Cash-based accounts recognise transactions at the point where cash is disbursed or received. There is no concept of assets that have value over the coming weeks, months or years, nor of liabilities that must be settled at some future date. Accrual accounting puts values on assets (current and non-current) and liabilities on the statement of financial position (or balance sheet). It is no surprise, then, to see that governments that use accruals-based accounts take a longer-term view of their finances. Veronica Povey from the UK Treasury discussed how the changeover to accruals created the impetus to think much more about the long term. '[Accruals] makes you think about the future, not just the here and now'. Governments have many non-current assets, such as land or property, plant and equipment. Daniel Tuck-Martin, the Senior Advisor of the UK Finance Insight Team suggested that knowledge assets and the student loan

Box 2.2: Fiscal rules and accrual accounting

An OECD study identified that in many countries policymakers and the general public tend to have limited interest in accruals-based financial information. It was suggested that this is because the net lending figure, which is the difference between cash spending and cash receipts, is often seen as the key performance measure or target and can be the focus of the political debate. These measures are often used by political parties in establishing 'fiscal rules', or promised limits on public spending.

A recent report by the Resolution Foundation, a UK-based think tank, provided a helpful framework for considering how governments should set out their fiscal rules. The first key lesson identified in the report is that 'what gets excluded gets exploited' (Hughes et al. 2019). Many governments have accumulated substantial off-balance sheet liabilities and continue to accumulate non-debt liabilities (including public sector pensions), while most fiscal rules do not measure the impact of these liabilities on the public finances. Ian Ball noted that in New Zealand:

'Gross debt on [New Zealand's] balance sheet is equivalent to less than 20% of the total value of assets and liabilities combined, which is a very small proportion of the balance sheet. So, if you hold people accountable for all of the assets and liabilities that the government has, you need to have a balance sheet in order to do that'.

The move to accrual accounting can help in creating a fiscal framework with targets that recognise the impact of decisions on the public sector's balance sheet. Otherwise, there will be significant temptation to shift costs outside the scope of the fiscal targets – even where such a decision would not provide good value for money. ■

Box 2.3: The Asset and Liability Committee in NSW Australia

The NSW government (2016a) announced in its 2016/17 Budget the creation of an Asset and Liability Committee (ALCO), the establishment of a Financial Risk Management Group within the Treasury, and its intention of implementing public sector financial asset and liability management. ALCOs are typically established within banks and other financial organisations for advising on suitable asset and liability management policies and supervising their implementation. With this expertise, the government can receive advice on key decisions about the state's assets and liabilities, unlocking the value of the state's balance sheet. The approach described weighs the risk and return objectives at a whole-of-government level through the development of a whole-of-state risk appetite statement and having a strong, disciplined and whole-of-government approach to the management of balance sheet and fiscal risks.

NSW's view is that a strong balance sheet supports low borrowing costs and attracts the widest range of potential investors to the state's debt issuance and private financing for capital projects. It also provides flexibility for the government to respond to emerging fiscal and economic pressures, providing capacity for the government to absorb adverse fiscal shocks or raise debt in a fiscally sustainable manner. A strong balance sheet and triple-A credit rating also facilitate the state's other financial management reform goals.

ACCA and IFAC produced a video case study of the ALCO in NSW Australia, as part of series documenting good practices in PFM from around the world. To learn more, scan the QR code to hear more about this initiative in NSW. ■

Although New Zealand maintains a strong net worth position in excess of 40% of GDP, its politicians still require information about the long-term implications of the current policies.

book were examples where the addition of accrual information supported long-term decision making by governments.

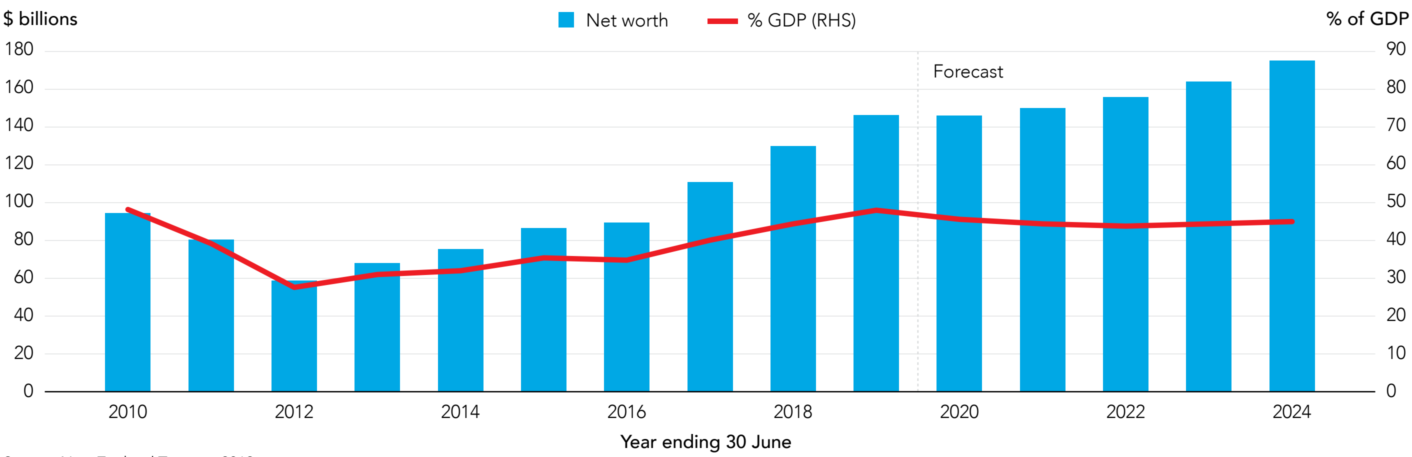
In advanced cases, governments can produce intertemporal balance sheets to explain the long-term fiscal implications of their policy decisions. For example, the New Zealand government produces forecasted financial statements that project what its balance sheet will look like in the future. Ken Warren, chief accounting adviser at the New Zealand Treasury, advised that taking this long-term view has meant that there is an intensifying focus on the cost of an asset versus the benefits derived from that asset. This includes measuring the use of the asset, the condition of the asset and whether the asset will meet future demands. This information is being used to inform the New Zealand government's investment plan. By using accrual information, the New Zealand government focuses on how the balance sheet needs to change to meet future demands.

New Zealand has adopted the new wealth perspective advocated above, one which Dag Detter, a former director of Sweden's Ministry of Industry, suggests can allow for a doubling in infrastructure investment (Detter and Folster 2017). This can be seen, for example, in the *Half Year Economic and Fiscal Update 2019* published in December 2019 (Treasury 2019). Figure 2.3, taken from the publication, shows New Zealand's Crown net wealth is forecast to grow over the next five years from $139.8bn to $174.9bn, while remaining at about 44% of the country's GDP. The growth is expected to come from operating balance surpluses.

Although New Zealand maintains a strong net worth position in excess of 40% of GDP, its politicians still require information about the long-term implications of the current policies. ACCA's 2019 report, *How Accountants Can Bridge the Global Infrastructure Gap*, noted that analysis by the New Zealand Treasury showed the current policy framework would produce recurring deficits that were forecasted to reduce the nation's net worth to almost –57% of GDP over a period of 40 years (Metcalfe and Valeri 2019). Having professional finance staff who can produce this kind of analysis, based on accrual accounting information, can provide decisions makers with a better long-term view of their policy decisions and can help improve the sustainability of public finances.

The production of accrual accounts is also useful in informing governments' fiscal sustainability reports, or intergenerational reports, which can be used to project the fiscal position in the longer term. These reports show what would happen if the government did not change its policies, given forecasted economic conditions.

FIGURE 2.3: New Zealand's Crown Net Wealth 2010–2024



Source: New Zealand Treasury 2019

> In particular, balance sheet measures look only at the impact of past government activity, but they provide an important baseline on which future projections can be built.

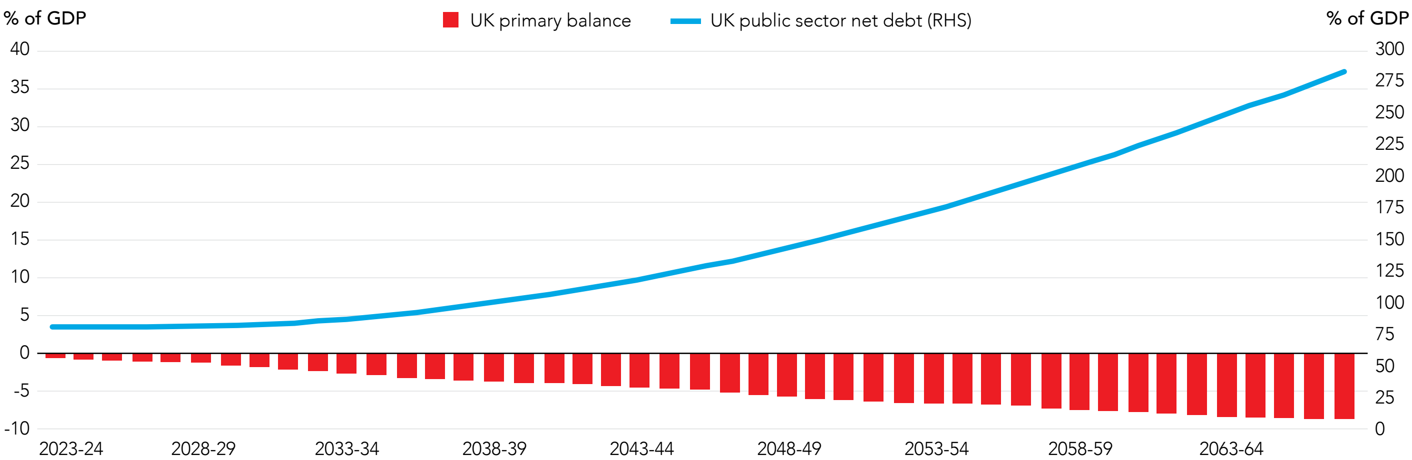
In the UK, the Office for Budget Responsibility (OBR), an independent entity within the public sector, produces a *Fiscal Sustainability Report* (OBR 2018). In this report, the OBR looks beyond the medium-term forecast and asks whether the UK's public finances are likely to be sustainable over the longer term. In doing so, the OBR looks at the fiscal impact of past government activity, as reflected in the assets and liabilities on the public sector's balance sheet, and at the potential fiscal impact of future government activity, by making 50-year projections of all public spending, revenues and significant financial transactions, such as government loans to students. The *Fiscal Sustainability Report* uses the public sector balance sheet as its baseline and uses information based on accruals.

By way of example, Figure 2.4 shows the OBR's forecasted PSND and primary balance for the UK out to the 2067/68. Under the current policy environment, the OBR forecasts that the UK's primary balance[7] will deteriorate to 8.6% of GDP in 2067/68. In addition, the OBR projects that PSND will rise from approximately 80% of GDP in 2022/23 to 282.8% of GDP in 2067/68. The OBR notes that there are limits to what public sector balance sheets alone can tell us about fiscal sustainability. In particular, balance sheet measures look only at the impact of past government activity, but they provide an important baseline on which future projections can be built.

Similarly, in 2016 NSW published its third *Intergenerational Report* (NSW Government 2016b). This report, which is produced every five years, is also built on accruals-based financial information, including accruals-based forecasts as set out in each year's annual budget. The report shows projections of the fiscal position over the 40 years following publication and is based on forecast economic, demographic, workforce and housing data. The report also highlights choices, opportunities and challenges for government, to inform future decision making.

While there are many similarities between the way in which these long-term reports have been developed, the *UK Fiscal Sustainability Report* (OBR 2018) is built on accruals-based financial reports but not budget information (although the majority of budget information is developed on an accrual basis) and the *NSW Intergenerational Report* (NSW 2016b) is built on accruals-based financial reports and budgets. Having an accruals-based balance sheet is the baseline for both. These are clear examples of how governments can use the information generated through accrual accounting to support their long-term planning and policymaking.

FIGURE 2.4: OBR's baseline projections of the UK's primary balance and public sector net debt (PSND)



Source: OBR 2018

7 The difference between non-interest government revenues and spending.

By implementing accrual budgeting alongside accrual reporting, governments will realise a series of benefits that flow from putting finance at the heart of decision making.

COLUMN C: BENEFITS OF ACCRUAL ACCOUNTING AND BUDGETING

Governments and public sector entities that use accruals for budgeting as well as accounting and financial reporting can derive the benefits shown in Columns B and C of Table 2.1 (page 18). By implementing accrual budgeting alongside accrual reporting, governments will realise a series of benefits that flow from putting finance at the heart of decision making. These benefits are explored in below.

Putting finance at the heart of decision making

The implementation of accrual budgeting is required to embed the finance function properly in day-to-day decision making. Vicky Rock, the director of public spending at HM Treasury, argues that 'managing the budget strengthens the hand of finance. So if you want the finance function to be drivers of decisions, then accrual budgeting is critical to making sure that the function is a key element of decision making'. By aligning accrual accounting and budgeting, the experts noted that this consistent basis:

- embeds performance management in public sector organisations,
- improves medium-term forecasting and planning, and
- supports effective project management across government.

a) Embedding performance management

If a government uses accruals for its financial reporting but budgets on the cash basis, it will be very difficult to produce regular budget monitoring reports on the accrual basis. Accounting and budgeting on the accrual basis facilitate frequent, often monthly, budget monitoring reports. This allows for more transparency and the opportunity to identify issues earlier in the financial year.

The experience in New Zealand (Figure 2.5) is that accrual accounting and budgeting enabled an improvement in performance management. Ian Ball framed 'performance in government' in two ways:

> *'One was as an organisation that delivered services to citizens. And that's analogous to the view of performance that a customer of a company would have if you were buying a car, for example. How good was the car relative to what you've been promised? But the other dimension of it was if you viewed it from the perspective of the owner of the organisation, which is quite different. Where you're interested in things like: Are we maintaining capital? Do we have a good risk-management strategy? Are we appropriately defining the scope of our business?'*

FIGURE 2.5: Performance in government – a New Zealand perspective

The outcomes-focused budgeting approach is also expected to encourage public sector agencies to coordinate and collaborate with each other so that resources are optimally pooled to serve the needs of communities.

This two-pronged approach to embedding performance management was established in the early days of accruals implementation, when the New Zealand government was facing budget deficits. Ken Warren explained that Ruth Richardson, the Minister of Finance:[8]

> *'Supported the new performance-based accountability system. She had a clear idea of how she was going to use it, to give her the information needed to progress her objective to eliminate the fiscal deficit without tax increases. After three years New Zealand was back in balance. This required successive budgets using information from 800 output classes to challenge, for example, whether those costed outputs were needed, could be reduced, could be done cheaper, done differently or whether users could pay. This use of performance-based information effectively embedded the system in New Zealand with measurement of assets and liabilities part of the New Zealand financial infrastructure'.*

This information was used at a whole-of-government level and a departmental level. Ian Ball explained: 'Departments had to start measuring and monitoring and having good information about exactly what the accruals numbers were because they had to use those to measure their performance against budgets and appropriations'. The requirement for departments to use accrual information demonstrates how New Zealand's reform put finance at the heart of decision making.

Other jurisdictions are also using performance-based information. In NSW Australia there is a progressive move to outcome budgeting, with the focus on the impact on citizens for the money spent, rather than on inputs. As reported in the New South Wales 2017/18 Budget document (NSW Government 2017) the NSW government embarked on a multi-year transformation of the way it manages and measures its annual expenditure. This transformation was about providing better outcomes for the people of New South Wales – more transparency and accountability for expenditure, and better value for money. NSW intended the reforms to assist the government in making better and more informed resource allocation decisions and to lead to making more meaningful information available to the public, to track progress towards these outcomes. NSW envisages that financial and performance information will evolve and improve over time as the needs of the people and the demand for government services changes and as information becomes more sophisticated.

The outcomes-focused budgeting approach is also expected to encourage public sector agencies to coordinate and collaborate with each other so that resources are optimally pooled to serve the needs of communities. This approach puts the needs of the people at the centre of investment decision making. Sean Osborn from NSW Treasury said that these reforms are intended to change the conversation from 'we spent more money on education', to 'we spent money on education and these were the outcomes for citizens'. The outcome budgeting model builds on experience in NSW of commissioning outcomes, and on international evidence and experience of moving towards performance budgeting from countries such as Canada, the UK, New Zealand, the US, and the NSW government.

b) Improving medium-term forecasting and planning

Australian states and territories and New Zealand are among jurisdiction that annually prepare accrual budgets for the next year and forecasts for the next three years. This provides a projection for the government's finances and a connection between what is happening in the current year with what is expected in the next few years.

8 The minister of finance at the time of the reform in New Zealand.

The benefits of accruals implementation – achieving value for money, facilitating public scrutiny, and putting finance at the heart of decision-making – are all derived from the creation of new decision-useful information.

In New Zealand, Ken Warren explained:

> *'There is a cycle of financial information that links together budgets and accounts. The annual budget, which includes the remainder of the current year, next year and a further three years, is prepared on an accrual basis. Following the production of the year-end accounts, the budget and forecasts for each of the future years is updated. These updated accrual-based forecasts are then used to set the budget strategy and fiscal strategy for the forthcoming budget. All information is presented in the same format'.*

By aligning reporting, planning and fiscal strategy to the accrual basis, New Zealand was able to embed the use of accrual information.

Accrual budgeting is also used in Austria to improve medium-term forecasting and planning. Bernhard Schatz said: 'I'm very happy that we introduced accrual budgeting at the same time as the core reporting. Why would you report on one system and plan on another?' The use of accrual budgeting alongside accrual accounting can lead to enhanced fiscal credibility. The use of a consistent basis in budgeting and reporting can also improve the quality of forecasting, as officials are working from a comparable basis and will have more current and forecasting financial information in order to improve their financial forecasts.

c) Supporting effective project management across government

Veronica Povey from UK Treasury explained how project management has become more effective in the UK public sector as a result of budgeting on the accrual basis. She said: 'large project teams now understand their payments and accruals. This provides a much more disciplined route to good financial management on some of our big projects. Without accruals you have a potential lack of control'. This is an improvement over former times when project managers might regard their multi-year budget as a single authorisation and spend the money whenever they wanted rather than having regard to financial years.

Policy debates, as well as the detailed project management, inform the scope of projects. Bernhard Schatz explained: 'we had a debate in Austria, just to give an example, on fighter planes. And politically, there were a lot of parties who said, "we don't need them, and we can abolish them". And yes, we could do that, but it would give away service potential in the billions of euros'. Therefore, the use of accruals can provide for the proper scoping and management of large government projects and has the potential to produce considerable savings across government.

Decision-useful information through accruals implementation

The benefits of accruals implementation – achieving value for money, facilitating public scrutiny, and putting finance at the heart of decision-making – are all derived from the creation of new decision-useful information. The accrual basis supports decision makers in the public sector by providing new information that reduces fiscal illusions and allows for more regular reporting to embed performance management.

All the benefits highlighted above are supported by improvements in the quantity and quality of financial information, which was achieved through the implementation of accrual accounting and/or budgeting. The experts interviewed cited a range of examples of how accruals had produced decision-useful information, regardless of the stage of accrual implementation maturity. Therefore, the following chapter will focus on the lessons learned by those who have implemented accruals and on the key enablers for producing decision-useful information.

3. Creating decision-useful information

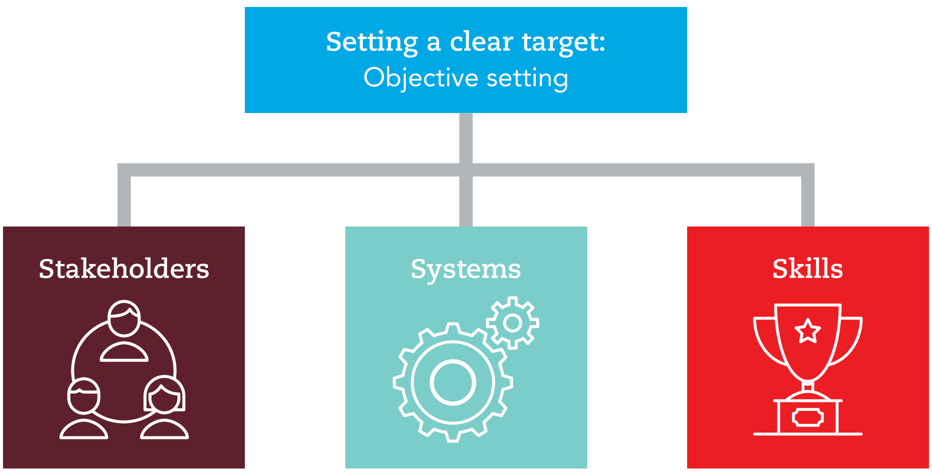
The production of decision-useful information is critical to achieving the range of benefits cited in Chapter 2. Participants from the roundtable discussions and the experts interviewed provided their perspectives on the key enablers and lessons learned through the implementation of accrual accounting in their jurisdictions. The discussions focused on objective setting, stakeholder engagement, systems and process, and capability and skills.

SETTING A CLEAR TARGET: OBJECTIVE SETTING

The experts agreed that the implementation of accruals is a long-term project in the public sector, but clarity of direction is also important. Therefore, at the outset of accruals adoption, governments should consider the objectives they seek to achieve through reform. The experts demonstrated that each jurisdiction had followed its own path in implementing accruals, reflecting the local context, but the research did reveal insights across five areas:

- acknowledging the varied starting points
- taking a whole-system approach
- building long-term road maps
- creating multiple checkpoints at which to measure success, and
- the need for continuous improvement.

FIGURE 3.1: Key enablers of decision-useful information



For less mature markets, the motivations can be born of the need to develop credibility and to access donor funding.

Acknowledging the varied starting points

There are many reasons for a jurisdiction to adopt accrual accounting and, as a consequence, the context for each accruals implementation is different in not only the motivation for change, but also the starting point.

In New Zealand the move to accrual accounting was driven by a reforming government that was frustrated with existing public sector processes and wanted better information to support its decisions. There had been cases where the bureaucracy had undermined the ability of the government to operate because of controls that were not ultimately in the public interest. Ken Warren explained: 'an example of the previous detailed cash budgeting system getting in the way of good management included the inability to purchase equipment to support the processing of data for use in negotiating a trade agreement as the IT budget was overspent, despite the overall budget being underspent. This bureaucracy undermined the ability to carry out effective trade negotiations'. In Austria, the motivations were similar. Bernhard Schatz explained that 'the Minister of Finance at that point in time felt that Austria lacked the instruments to make sustainable decisions after Austria had been running deficits for decades'. In both cases, governments sought to use accrual accounting and budgeting to produce new decision-useful information that could be relied upon to drive performance management in the public sector.

In Switzerland the motivation was more pragmatic. Andreas Bergmann explained: 'the main objective in Switzerland was to align the federal government with states and local government [that] had been producing accruals-based accounts for years. Many ministers at the federal level have experience of the lower levels of government and so their experience was in accruals not cash'.

The experience of public sector leaders at other levels of government made the case for federal implementation.

In Australia, which had been using accruals-based accounts in the public sector for some time, there was a shift in the basis of the standards. Sean Osborn from NSW Treasury in Australia explained that 'after some corporate issues overseas and in Australia, the government determined that Australia would adopt IFRS.[9] In NSW, Australia the key aims of adopting accrual accounts were to support decision making and, in doing so, remove inefficiencies and reduce complexity through standardisation, and to create a balance sheet. The objective was to produce information that would allow public sector organisations to think across reporting periods rather than within them, to support forward planning.

For less mature markets, the motivations can be born of the need to develop credibility and to access donor funding. For Slovakia, Lucia Kasiarova explained that the strategy was: 'part of broader reforms aimed at being able to deliver multiyear, programme budgeting; to improve the debt and liquidity systems; and to introduce the accrual accounts as part of broader objectives around improving the Slovak public sector management system and to be considered for European Monetary Union'. Clearly, no one jurisdiction begins the journey of reform with the same capabilities or with the same motivation, and it is important to acknowledge this in setting objectives for the reform.

Taking a whole-system approach

The transition to accruals should not be considered in isolation. Ross Smith, Program and Technical Director at the IPSAS board, argued that: 'An added benefit to the improved information an accrual accounting reform exercise brings, are the broader PFM improvements, when they are part of a comprehensive reform project'.

9 The Australian Accounting Standards Board adopts a sector-neutral approach, with like transactions treated in the same way for all entities. Australian Accounting Standards include sector-specific paragraphs where the needs of particular types of entity require a difference in treatment.

Many experts described the need to postpone or remove certain portions of implementation in order to address politically sensitive issues or technical challenges.

He went on to say that:

> *'We often hear from countries that make investments in staff training as part of their reforms, to produce more qualified accountants. Cash accounting jurisdictions sometimes lack trained accountants in the public sector. Therefore, in addition to the benefits you get from the improved accrual information, broader benefits to the PFM system as a whole can be achieved'.*

The implementation of accrual accounting should not be considered in isolation. Instead, it requires the experts leading implementation to consider the wider system benefits that could be achieved, as well as what interventions will support the implementation of accruals.

This view was shared by officials in Australia in their reflections on the implementation of accrual accounting. It was noted that planning and implementation can be affected by complex legal issues that can flow into how you are able to interpret accrual accounts. Marsha Guthrie from NSW Treasury said that one of the key lessons learned is 'Don't think of accrual accounting implementation in isolation – instead think about the whole enterprise, the whole structure. Everything else underpins it: all of our internal policies, reporting structures, the systems'. As a consequence, the lesson learned from NSW Australia was that other governments should consider their entity structure, understand what they actually want to achieve and design it accordingly: ideally, transitioning to a single system over time in order to reduce complexity.

At the beginning of implementation, New Zealand set the objective of moving to a performance-based accountability system. Ken Warren, chief accounting adviser at New Zealand Treasury explained:

> *'New Zealand wanted central government to operate using principles already established in profit-oriented corporations in the public sector. Therefore, the government needed to know what it owned and what it owed. So New Zealand had a citizen perspective at the start of its reforms, but it was really part of thinking about performance as part of a performance-based accountability system that essentially ministers would drive'.*

This approach provided a clear view of the 'why' to underpin the new framework.

Building long-term road maps

Many experts described the need to postpone or remove certain portions of implementation in order to address politically sensitive issues or technical challenges. This approach is helpful in building a multi-staged execution when implementing accruals, but at the same time this should not create the justification for removing important, if challenging aspects, of accrual reporting and budgeting.

It is therefore important to create an achievable road map, while remaining ambitious over the long term. For example, both state and public sector pensions are excluded from Austria's accrual accounts, given the difficulty of including these within the project timetable, but experts noted that it would have been good to include a 'sunset clause telling us "by 2025, you will have these as well"'. From a Canadian perspective, Bailey Church commented that: 'my greatest advice would be to have a long-term vision, but break it up into digestible bits that can be implemented – so you're not overwhelming the system. I think the worst thing you can do is to force the journey when the capacity is not fully there'.

In Slovakia the approach taken was to produce a gap analysis on public sector reporting as part of the planning phase.

As part of building the road map there must be realism about when certain milestones and benefits will be achieved.

This work was carried out by an external expert and sponsored by the World Bank. It took Slovakia three years to complete detailed planning, including analysis of the accounting legislation. In a similar vein, Tanzania took advantage of transition periods set out in new standards to allow information to be gathered over a five-year period. Neema Mssusa from Tanzania said 'the objectives defined at the beginning have been realised, although there were changes over time to reflect new knowledge. Through the National Board of Accountants and Auditors the requirements of what information should be published were agreed and targets set'. This demonstrates that road maps do not need to remain static and should reflect the changing circumstances of the jurisdiction. It is important to give sufficient time for planning and gap analysis in building a long-term road map to successful implementation.

As part of building the road map there must be realism about when certain milestones and benefits will be achieved. Andreas Bergmann from Switzerland said:

> *'You need to show the benefits to get the process started, but I would not oversell the benefits publicly because it takes quite a long while until you will have some high-quality financial statements based on full accruals. And if you oversell that, even before you start, that might lead to disappointment. And of course, that can create frustration or also undue pressure on the process'.*

A road map could also include how governments transition from cash appropriations. A number of legislatures vote annual appropriations with both cash and accrual information, with the view that this has helped parliamentarians move from cash-based information to accruals-based information. Andreas Bergmann from Switzerland said: 'So this [phased approach] helped in terms of not having too much resistance from the cash fans in any decision body because they still had their cash information to hand, and so the ones more keen on accruals could use the accrual information'. He cautioned that '10 or 12 years later we still have people referring to cash. So perhaps maybe we should have turned it off. But I think at the very beginning it was helpful to maintain both types of information'. It is therefore worth considering in advance how the jurisdiction will fully transition from cash to accruals, and what information should be reported using both accounting bases.

Creating multiple checkpoints at which to measure success

In building implementation road maps, governments should also consider setting periodic checkpoints where they can evaluate progress. For example, Bailey Church from KPMG Canada set out the Canadian experience by arguing that:

> *'it is vital to have a long-term road map for the implementation of accrual accounting. I don't think in most countries you can do it as a "big bang", where you move everything over. It needs to be supported by a long-term view of the different phases, successes and milestones. And if I think of our example here in Canada, we went from modified cash to full accrual accounting in 2000/2001. But it wasn't until about seven, eight years ago, that we even had concepts around quarterly reporting in government departments'.*

Admire Ndurunduru from Zimbabwe reinforced the point that checkpoints are critical to supporting the journey to implementation and the production of decision-useful information. 'In the implementation strategy plan, we have measures of success and have specific trigger points, where we say we want certain objectives to be achieved. The plan will then identify whether this has happened or not or is lagging behind'.

Few jurisdictions have had the capacity to transition to accrual accounting in a single 'big bang'. Therefore, in constructing a road map and setting objectives, officials should consider the natural checkpoints on the journey to full accruals. This long-term view allows for this substantial reform project to be broken down into more achievable phases and creates the opportunity for periodic review.

> Accrual information is important and useful for these stakeholders since it will show them the full financial position of their government and public sector organisations.

Checkpoint for external review
Austria set out in law the requirement for having an external evaluation of the new accrual system. Bernhard Schatz stated that: 'In our budget law, we had a clause that there will be an external evaluation of the system after five years… so we had an external evaluation body, including the IMF, the OECD, and two universities'.

The review was divided into three parts. First, the IMF focused on fiscal transparency. In the second area for review, the OECD covered budgetary management and performance budgeting. Finally, the third part of the review, completed by two universities, focused on the financial management and reporting system. This external, multi-party approach added additional legitimacy to the review process, while also providing an opportunity for reflecting on the result of accruals implementation. For example, the OECD report sets out 11 key recommendations on how the Austrian government can improve its budgetary management and performance budgeting processes, while also acknowledging the "balanced, inter-connected set of budgetary governance arrangements" in place (OECD 2018).

Adopting an attitude of continuous improvement

The experts in the study acknowledged that the implementation of accrual accounting would require constant iteration and development. In effect, there is no end point – instead, there is a need for a mindset of continuous improvement in the running of a country's PFM systems.

From the UK experience it is clear that a significant amount of upfront resource was required before a broader set of government stakeholders began to engage with the new information created through accruals implementation. Olivia Halliday explained that 'We had to build up the trust that the information was reliable and useful. And it really demonstrates that this is a journey. Now that we have demonstrated that we can publish [accrual accounts] for a number of years, that [accruals] is reliable, we can start to use it to see trends and effectively manage assets'. This mindset of continuous improvement will support the professionals implementing accruals by helping to identify new opportunities for creating and using decision-useful information in the public sector.

THE ROLE OF STAKEHOLDERS

One of the distinguishing features of the public sector is the existence of a broader range of stakeholders than for private sector organisations. As well as citizens, there are donors, funders, service users, civil society groups, ratings agencies, NGOs and other government bodies. Accrual information is important and useful for these stakeholders since it will show them the full financial position of their government and public sector organisations.

The experts from ACCA and IFAC acknowledged the need for robust stakeholder engagement in order to implement accrual accounting successfully in the public sector. The section above on target setting conveys the varied motivations for initiating reform but, irrespective of motivation, a variety of stakeholders need to be engaged in the process – both advocates and those providing constructive challenge.

Advocacy

The experts consistently referenced the need for the 'buy-in' of senior leadership and politicians – high-level champions for the reform. It is also essential to have cross-party political support to sustain the support for the transition to accruals. For a reform agenda to be successful, it is critical that finance officials identify these internal advocates and communicate the stakeholder-specific benefits that each group will receive through accruals implementation.

In Slovakia, the minister of finance, external experts and the World Bank have been influential, and the reforms are also supported by all political parties. With this support, the objectives have remained constant throughout and the reforms were achieved in line with plan. In another example of advocacy, Neema Mssusa from Tanzania commented that 'we are still proud of the fact that in one of the last speeches of the previous president of Tanzania, His Excellency talked about the benefits that accrual information provided'.

To make the best use of accrual information, finance officials need to engage with complementary experts who can benefit from the reform.

At the same time, to maximise the benefit of decision-useful information, finance professionals will need to engage with their colleagues to explain the benefits. Matthew Rowe, Senior Finance Advisor at the UK Treasury, argued that 'you really need finance people who are able to explain those benefits and you need to reach out to the broader organisation. Because it requires changing behaviours, not just from finance people, but across the board'. To make the best use of accrual information, finance officials need to engage with complementary experts who can benefit from the reform. This engagement should include actuaries for employee pensions and valuers for property, plant and equipment. To meet this need in New Zealand, the reform was accompanied by a major marketing campaign. Ken Warren explained that:

> *'Part of the marketing strategy was intended to educate potential users of the accounts and to help them contribute positively to the narrative on the public finances. This included the analysts of government information, macroeconomists, business journalists and credit rating agencies. They all needed to be converted to accrual accounts as a means of providing better information for decision making'.*

To achieve effective reform, advocates are also needed at the entity level in government. An example of this occurred in Austria, where Bernhard Schatz noted that:

> *'Entities that had real estate were [among] the biggest supporters of the accounting reforms as it helped provide new arguments in budget negotiations and provided evidence on the size of the maintenance backlog. It also supported discussions about over- and under-investing, and the visibility of depreciation provided another indicator about the ongoing need for investment'.*

By building this network of advocates, countries transitioning to accruals will be maximising the use of accrual information and sustaining the support for the reforms through each phase of implementation.

Challenge

Creating decision-useful information that is trusted also requires a strong challenge function to review the progress of the reforms. For example, as Slovakia has implemented accruals, staff have treated it as a learning exercise, embracing audit findings to improve outcomes. By law, the accounts are audited by private sector auditors, and these auditors have worked constructively with line ministry staff. Josef Hýbl from Deloitte in Slovakia, in reporting on the success of the arrangements, noted that there were 100 modifications to the accounts at the beginning, which has already been reduced to 36. This external challenge function is useful in improving the quality of the financial statements, while also increasing the credibility of the financial information.

In the UK, the Public Accounts Committee (PAC) in the House of Commons has received and assessed the UK government's Whole of Government Accounts (WGA) in each year of its publication. While supporting the objectives of WGA, the PAC has provided challenge to the process of producing the accounts and, importantly, to how the information being produced by WGA is being used by the government. For example, in its report on the 2016/17 WGA (PAC 2019), the PAC challenged the amount of time taken to produce WGA and the impact of delays on the usefulness of the information, the potential for including additional information that it considers useful to the reader in the notes to the accounts, and its commentary in the performance report. In its report on the UK WGA, the UK's supreme audit institution, the National Audit Office, has noted that the government is using WGA to enhance decision making, but that there is more to do to embed the WGA as part of government's routine financial management (H.M. Treasury 2019: Chapter 6). The WGA was used to inform the UK Treasury's balance sheet review and the Office for Budget Responsibility's reports on fiscal sustainability and fiscal risks.

> There is variability in the implementation of systems and on the decision about whether to run a centralised system or empower departments to produce the accrual information themselves.

THE ROLE OF SYSTEMS

The expert community concurred that it is important to consider the systems that will support the implementation of accrual accounting and the creation of decision-useful information. This is a foundational enabler since, as Joao Carlos from Portugal and a principal at the IPSAS board put it: 'if we don't get the basics right, we will never achieve the wider benefits'.

Central vs devolved implementation

A frequent consideration of the experts was whether the financial management systems that support accrual accounting would be centralised or devolved to departments. Overall, the experts largely agreed that in the initial implementation of accruals, departments should be empowered to create the systems required to produce their own accrual information that could be shared with the centre.

Ian Ball explained that:

> *'We decentralised the financial information systems to departmental level, and they had to run their own systems on the basis that they were accountable for what they did. The Treasury required departments to provide information for budgeting, for reporting, etc. So long as that was done reliably, then we didn't care what information was generated internally. And we did that on the basis that running the New Zealand Defence Forces is not the same as running a small social policy ministry'.*

At the same time, this preference for devolved systems requires checks to be put in place to maintain data consistency. Daniel Tuck-Martin, from the UK Treasury, commented that: 'data standards [are a key enabler], as there needs to be an understanding of what people are using and trying to make that as consistent as possible'. Therefore, it is important to be clear at the outset about the expectations of the line ministries or departments. One UK participant suggested that the best practice is empowering colleagues across government through clear guidance and common toolkits, with sufficient feedback loops to inform good practice across government.

There is variability in the implementation of systems and on the decision about whether to run a centralised system or empower departments to produce the accrual information themselves. In Slovakia, each ministry has its own information system. At the beginning there was a positive decision, based on pragmatism and cost, not to have one system. Each ministry had its own system package that could be easily adapted for accrual accounting. Lucia Kasiarova, from the Slovakian Ministry of Finance, said: 'As things have progressed, the view is now that unless you put in one central system you won't be able to make better use of the accounting data, consolidation and access to information. The central accounting system also makes the consolidation and access to information easier'. Slovakia is currently in the process of centralising its accounting information system as there are many intra-government transactions and manual processes. Also, the quality of finance systems at a departmental level is varied and not consistent across central government. There is an aspiration that the production of accrual information will create a common standard so that the process can become more routine.

Officials implementing accrual accounting should consider whether they have a sufficient mandate for consolidating their accounting systems.

System support for accruals-based information

In Austria, SAP adapted for cash accounting was implemented ahead of the reforms. Elements that were removed were then reintegrated for the accruals reforms. There were already subsystems, such as an asset register. The same instance of SAP was used by all entities, so no integration was necessary. Bernhard Schatz said:

> *'we had a debate about whether to develop the current system or start from scratch. We decided to go for developing the system because people were just used to the system and because of additional training efforts to get them educated on [the] new system. So, it was quite a pragmatic decision'.*

This issue of implementation cost was raised by the Swiss expert, because in Switzerland systems were the largest cost item of the reforms. There were previously 17 different systems, which were diverse and costly. As part of the reform, a new system was built – but lessons were learned. Andreas Bergmann noted that: 'money and time was spent on implementing a module for amortised cost of financial instruments, but the difference was very small. Materiality needs to be considered and with hindsight this shouldn't have been done'. More cost-efficient systems can produce information that is materially, if not precisely, accurate. Officials and public sector leaders should consider where additional expenditure on systems produces good value for money and where bespoke or expensive changes may be unnecessary. He also suggested that those implementing accruals consider:

> *'the integration of budgeting, accounting and [Government Finance Statistics (GFS) into] the same system, so that you can use the budgeting information for comparison purposes. This will allow for reclassification for GFS purposes and similar requests later. It is down to the operational issues, that can save you a lot of money later on'.*

In Australia, smaller jurisdictions and agencies moved to a single system, but not in larger states such as NSW. Having a single software application can improve the level of support, and upgrades can be done throughout at the same time. In NSW, there has been subsequent consolidation of systems, which those concerned described as beneficial. What has been challenging is achieving this consolidation without a mandate. Clinton Gould from NSW noted that the 'consolidation of systems has worked where people have owned it, seen the benefit and where it has been driven from the top'. Therefore, officials implementing accrual accounting should consider whether they have a sufficient mandate for consolidating their accounting systems.

Marsha Guthrie offered some lessons learned in this respect from NSW Treasury. She advised that for systems: 'don't discount how much time it will take to complete these changes. I would always suggest piloting as much as you can, doing things in parallel before you actually move over'. Clearly, these lessons require additional time in an implementation plan – where systems need to be rigorously assessed and piloted.

In order to improve outcomes, certain jurisdictions built incentives for effective financial management into their new systems.

Reporting flexibility

The experts also concurred that changing government structures and new information requirements must be considered in deciding what systems will be most appropriate in supporting the creation of decision-useful information. For example, Marsha Guthrie from NSW Treasury reflected that: 'we talk about the machinery of government, and we talk about the way information is evolving, but we build very rigid systems designed at a point in time – systems need to be flexible to changes in business processes, organisational structures, and new information and accounting requirements'. In addition, Joyce Evans – the chief financial officer (CFO) of a local government in Canada – noted that 'municipalities are not one business, but many businesses with lots of different responsibilities. So it's hard for us to find [a system] that fits everybody'. It will be challenging to accommodate the diversity of operations and reporting requirements, but this requires in-depth engagement across government to understand what systems might best meet the jurisdiction's needs.

Building in incentives

The experts gave a variety of examples demonstrating how the accrual basis provides new information that can improve decision making. In order to improve outcomes, certain jurisdictions built incentives for effective financial management into their new systems. For example, Ian Ball explained that in New Zealand: 'In the [reform] of the whole system, we were conscious of what incentives this would provide [for] departmental managers and indeed, on ministers. We introduced the capital charge because it was designed to give organisations the incentive to use capital more efficiently than they did'.

New Zealand's capital charge was designed to address high levels of redundant assets in the public sector, and helped to drive efficiency. If an agency sold redundant assets and passed the proceeds to the Treasury, this reduced the organisation's capital charge.

In comparison, Bernhard Schatz from Austria saw the lack of incentives in their system as a lesson learned. He stated that: 'One thing we didn't do is think about the incentives in place for people to use the information for their internal decision making and if we had we would have reinvented the budget process. With the current system, there wasn't a huge incentive to use new information for your own purposes'. This view was supported by the experts in Switzerland, where the accruals environment provided information on provisions at an earlier stage. Andreas Bergmann asked:

> *'When do you approve a provision? Is it at the moment you provide for something or is it at a moment when the cash is released to pay? I think it is useful to have that information beforehand and not just in a very last moment when the payment is released'.*

It is critical that countries currently transitioning to accruals consider how incentives can be built into their systems to encourage the use of decision-useful information.

THE ROLE OF SKILLS

The last of the enablers is capability and skills. It is clearly essential that there are professional accountants in the public sector who can produce accrual information and managers (and politicians) who can understand the information and advice they receive in order to make good decisions.

Within this sub-section we consider several aspects of what is required in meeting the capability and skills requirements in creating decision-useful information in an accrual environment. Getting the right skills for reform requires governments to consider how they will:

- build internal capacity within the public sector
- establish career paths, and
- receive the right external support.

In addition to having a vision, governments and public sector organisations will have to identify the skills and knowledge gaps within their personnel and commission training to fill the gaps.

Building internal capability in the public sector

The adoption of accrual accounting requires more professional accountants. This starts with the need for a professional accountant to lead the finance function; as Vicky Rock said that in the UK, 'one of the changes that has followed the adoption of accruals-based accounting is that now it is a requirement for finance directors to have a finance qualification'. If having accrual information is going to lead to better decisions about the use of the public sector's limited resources it is imperative that there is a cultural change at the level of senior management.

Bailey Church commented on the increased number of professional accountants in government. As Ian Ball explained, it would be strange if a government running a cash-based system had enough accountants to operate an accrual system.

> *'Why would you have the accounting expertise you need to produce accrual-based financial statements if the accounting system was a cash-based accounting system run by the Treasury? So as in every other country, in my view, there should be no expectation that there are sufficient [human] resources at the start of implementation'.*

Ian Ball noted that an enabler of successful implementation in New Zealand was 'flexibility in recruitment', which allowed for the hiring of qualified staff from the private sector at market rates. Recruitment managers were given more flexibility over salaries and conditions than is the norm in public sector organisations. This flexible approach can support accelerated implementation, but other jurisdictions cited plans for developing the required talent internally. For example, in discussing the situation in Austria, Bernhard Schatz commented on how initial gaps in internal capability were addressed and the challenges that lie ahead in continuing to build capability over time. 'In our system the salary scheme between the public sector and the private sector is so different, that actually it is really challenging to get somebody from the private sector'.

Building internal capacity requires more than increasing the number of qualified accountants. Governments must understand what they need their accountants to do in an environment driven by decision-useful information. Bailey Church outlined the transformation from a transactional focus to something more strategic.

> *'It's really shifting from being a bookkeeper focused on data entry to having a strategic view of information. This means knowing why we're gathering the information, knowing what the information means, and knowing its value in decision making. That strategic focus is essential to really advancing the finance function'.*

In addition to having a vision, governments and public sector organisations will have to identify the skills and knowledge gaps within their personnel and commission training to fill the gaps. Some of the training may be internal courses where experts share their knowledge. Some of the training, however, is likely to be external, consisting of formal training courses. The nature of external training is changing so that now there are online courses (such as *ACCA's Certificate in Public Financial Management* and *Certificate in IPSAS*) that are more flexible, and potentially more cost effective, than traditional classroom learning.

In Tanzania there has been a significant focus on building internal capability. Neema Mssusa explained that: 'the main

Governments transitioning to accruals may also develop a training programme so that they can 'grow their own' rather than relying on the marketplace to supply sufficient talent.

thing was to make sure that the accountants were enabled to do it themselves', but even so more could have been done. A lesson learned in Tanzania was that internal training also needs to extend beyond preparers to include auditors, members of parliamentary committees, human resource professionals, and procurement officials. Importantly, the training needs to cover the interpretation of the accrual information by a broad pool of stakeholders.

The timing of training was also considered. Ken Warren, chief accounting adviser at the New Zealand Treasury, commented that:

> *'A key lesson for others is starting to invest in capability and capacity ahead of the reform. This was a key enabler in New Zealand where staff trained through an early adoption of accruals in the Audit Office were then able to provide technical capacity and a central capacity to support the reforms in the rest of government'.*

This experience suggests that governments would do well to consider which staff can act as effective enablers of reform and focus early training interventions on this group.

Establishing career paths

Having identified the need for an increase in the number of professional accountants in order to operate an accrual accounting system, governments need to develop strategies for acquiring them. Initially there may be an urgent need to hire qualified and experienced accountants, possibly as external consultants (see the next sub-section). Governments will need to develop remuneration packages that are sufficient to attract and retain accountants with the necessary skills, knowledge and experience. Governments transitioning to accruals may also develop a training programme so that they can 'grow their own' rather than relying on the marketplace to supply sufficient talent. All this might be described as establishing a career path for professional accountants that is attractive. Admire Ndurunduru said this is something that has been happening in Zimbabwe: 'The Public Service Commission is aligning career development with the professional qualifications. This means getting a professional qualification has an immediate impact on your role – creating the right incentives for public sector workers to pursue a qualification'.

Receiving the right external support

The implementation of an accruals-based system is a significant reform that will transform government. The experts believe that this implementation requires external support. Their view was, however, that governments do not need lots of expensive external consulting, but they do need to get the *right* external support. Ian Ball described the New Zealand experience, where: 'Implementation involved a mix of recruiting new people into government departments, using the skills of software providers, and training people internally'.

Even though external consultants are essential, the experts warned of the risks of becoming reliant on them, as they will eventually leave, taking with them their domain knowledge. At some point the government's finance team have to be able to take over the management and operation of the accrual system.

External support does not only have to come in the form of paid consultants. Government ministries and departments may have other people who can contribute. In the UK, for example, government departments and their agencies have governing boards that often include members from outside the public sector. Veronica Povey from the UK Treasury explained that this group's knowledge and experience could be tapped to help with the implementation of accrual accounting. 'The non-executive board members from the private sector probably can engage with a set of [accrual] accounts much more intelligently than they could with some opaque, traditional government accounting. If you think about balance sheet exposure, private sector experts understand the issues'.

Finally, there is a need to consider the balance between the systems supporting accrual reform and the ability to retain skilled staff in that public sector entity.

A clear insight here is that members of governing boards, often coming from the private sector, can be looked to as early adopters of accrual information – creating opportunities for using this new information at a strategic level in the public sector.

The experts also acknowledged that where there is a lack of capable personnel, a government may need to use external suppliers. It is possible, though, that internal teams can undertake some of the change-management work. Ian Ball gave one example:

> *'We had a team of what we called 'financial management assurance' people. They were auditors, basically, who worked with departments to help them get systems in place. It was primarily advisory, but at a certain point, those people had to sign off that the department had a system in place that would enable it to receive and monitor appropriations'.*

This 'internal advisory' model can provide support on cross-government accruals implementation without the significant costs associated with external consultants.

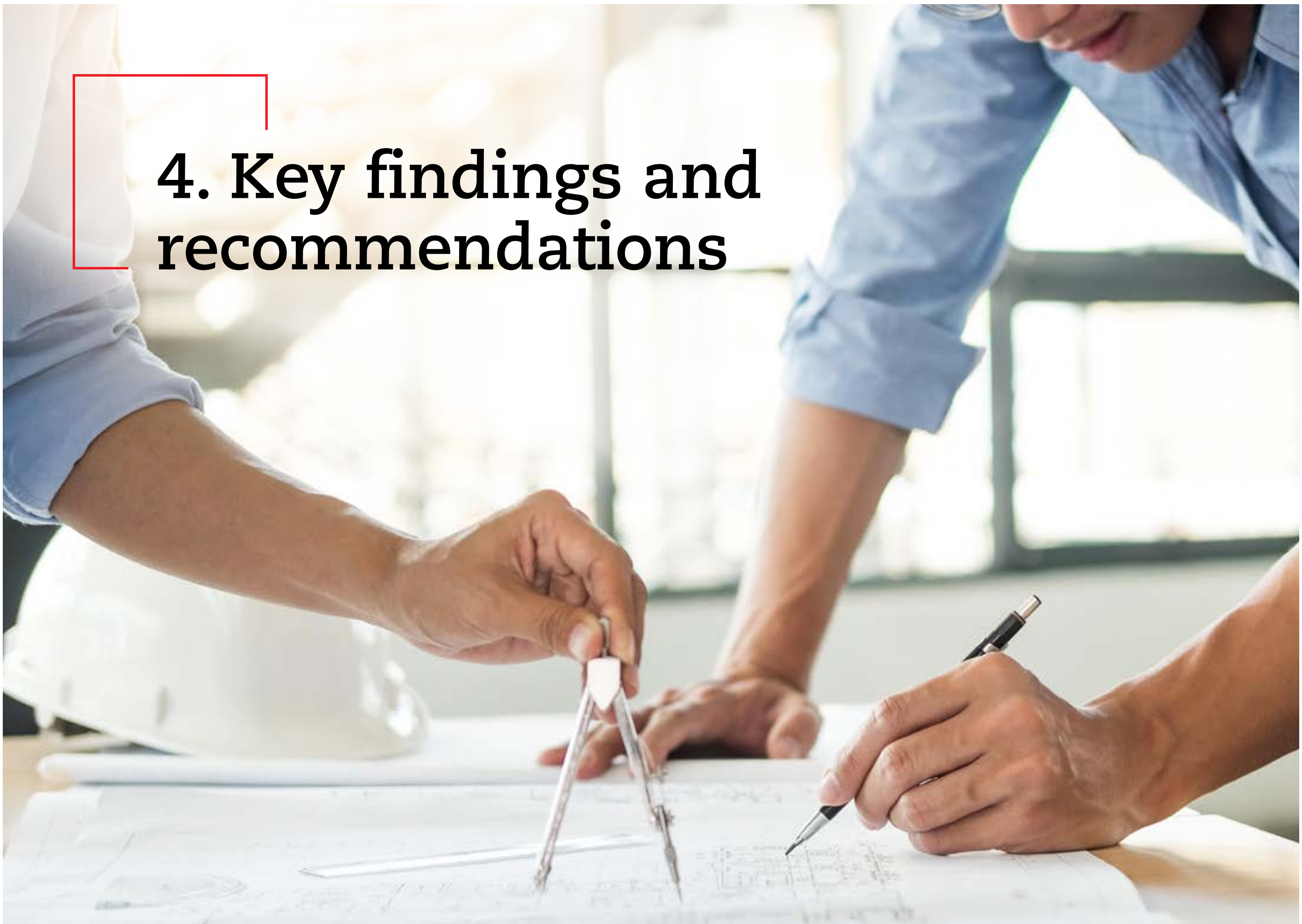
BALANCING THE RIGHT SYSTEMS AND SKILLS

Finally, there is a need to consider the balance between the systems supporting accrual reform and the ability to retain skilled staff in that public sector entity. Ross Smith describes the skills challenge that certain countries face where some jurisdictions "really struggle to get qualified accountants at all because the profession is underdeveloped and there may even be the absence of a local accounting member body. In those cases, even the private sector struggles to find qualified accountants, and if the public sector trains and develops them, the private sector often hires them away'.

In response to this challenge he noted that: 'some jurisdictions may try to implement better information systems that can be operated by a less sophisticated user than a qualified accountant, so that they can still capture the high-quality accrual accounting information… In effect, some jurisdictions can mitigate the impact of human resource capacity issues by investing in information systems'.

Those countries currently undergoing accruals implementation can similarly consider whether a capacity gap could partly be addressed through larger investment in appropriate systems that can augment the abilities of less-skilled preparers and users.

4. Key findings and recommendations



The *2018 Status Report* (IFAC and CIPFA 2018) established that a significant global transition is under way, with countries moving from cash to accruals. This present report has produced a substantial body of findings and recommendations by engaging with experts from jurisdictions that are the most mature in their implementation of accrual accounting. The following summarises the key findings and recommendations.

KEY FINDINGS

- By 2023, the number of countries reporting on the accrual basis is expected to increase from 37 to 98 (this represents 40% of the 150 countries included in the *2018 Status Report* (IFAC and CIPFA 2018)).
- The motivation for reform in developed countries is often intrinsically driven (eg to improve the information available for decision making), while developing economies are often driven by extrinsic motivations – such as enhancing trust and credibility.
- The benefits and complexity arising from accruals varies by implementation. See Table 2.1 (page18) for more information, but in summary:
  - cash accounting and budgeting are the simplest basis but provide the least decision-useful information
  - accrual accounting and cash budgeting form the most complex basis, but create new information that helps in achieving value for money, facilitates public scrutiny, and supports sustainable decision making
  - accrual accounting and budgeting create a 'medium level of complexity', depending on the consistency achieved. This environment, in addition to the benefits from implementing only accrual accounting, puts finance at the heart of decision making and allows governments to embed performance management.
- The benefits of accruals implementation highlighted in this report – achieving value for money, facilitating public scrutiny, and putting finance at the heart of decision-making – are all derived from the creation of new decision-useful information.
- The key enablers for producing decision-useful information are (i) setting a objectives and planning, (ii) engaging stakeholders, (iii) creating effective systems, and (iv) developing the right skills.

Participants from the roundtable discussions and the experts interviewed provided their perspectives on the key enablers and lessons learned through the implementation of accrual accounting in their jurisdictions.

RECOMMENDATIONS

The implementation of accruals creates new information that can support governments in their decision-making. The experts have made recommendations on how to maximise the benefits of this accrual information, directing this advice to public finance officials and leaders in countries currently transitioning to accruals. In summary, the experts recommended that governments implementing accruals should:

1. adopt a 'net worth' perspective in setting fiscal rules, remembering 'what gets excluded gets exploited' (see Box 2.2, page 26)
2. improve asset management by using accrual information to highlight where asset maintenance is inadequate, as well as to identify decommissioning and replacement costs
3. use asset impairments to challenge the performance of public sector projects (see Chapter 2, page 17)
4. direct independent fiscal policy institutions to assess contingent liabilities and produce recurring fiscal risk reports
5. use accrual information as the baseline for producing intertemporal balance sheets and/or fiscal sustainability reports
6. plan to align the bases for budgeting, reporting and forecasting – as working from comparable bases will provide more current data that can improve financial forecasts
7. implement accrual budgeting in order to put finance at the heart of decision-making, while embedding performance management across government.

Participants from the roundtable discussions and the experts interviewed provided their perspectives on the key enablers and lessons learned through the implementation of accrual accounting in their jurisdictions. The discussions focused on objective setting, stakeholder engagement, systems and process, and capability and skills.

Setting objectives and planning

On objective setting and planning, the experts recommended that governments implementing accruals should:

8. consider the objectives of the reform, including what information will be used following implementation
9. complete a gap analysis and create an achievable road map, while remaining ambitious over the long term
10. develop a vision on how budget and appropriation systems are going to interface with accrual financial reporting and government finance statistics
11. plan to produce a fully consolidated balance sheet, as this provides a full financial picture of the resources and risks for the public sector; this must include SOEs at the whole-of-government level
12. build politically difficult facets of the reform into the road map from the beginning (eg through a sunset clause requiring the eventual recognition of employee pension liabilities)
13. consider setting periodic checkpoints for evaluating progress (eg through a legal requirement for external evaluation of the new accrual system, such as in Austria).

Engaging stakeholders

On engaging stakeholders, the experts recommended that governments implementing accruals should:

14. manage expectations, as it can take time to realise the benefits of the new accrual information
15. educate potential users on the reform and how they could benefit from it
16. find champions – individuals who can emphasise the value of accruals to doubters
17. foster a political consensus that accrual reporting is valuable, so that the reform does not stall with a change in government
18. include groups that provide a constructive challenge to the reform, such as auditors and legislative committees (eg the UK's Public Accounts Committee).

Creating effective systems

On creating effective systems, the experts recommended that governments implementing accruals should:

19. build incentives for effective financial management into the new system (eg imposing a capital asset charge)
20. consider where additional expenditure on systems produces good value for money and where bespoke or expensive changes may be unnecessary
21. consider piloting or running systems in parallel before fully transitioning to accruals
22. empower departments to select the systems for producing their own accrual information, which can be shared with central agencies
23. create documentation on data standards that can be shared with ministries or departments in order to maintain consistency for reporting and analysis.

Developing skills

On developing the right skills, the experts recommended that governments implementing accruals should:

24. identify the skills and knowledge gaps within their personnel, and commission training to fill the gaps
25. deploy a few experts centrally, in order to control consulting costs and support implementation across government
26. agree an approach to knowledge retention when consultants are engaged
27. provide training beyond the preparers (eg auditors, members of parliamentary committees, human resource professionals, and procurement officials) to create a broader pool of users of the accrual information
28. create clear career paths and reward professional accreditation in the pay structure
29. require government finance leaders to be professional accountants
30. consider the balance between the accrual systems and the ability to retain skilled staff in that public sector entity.

Conclusion

'Don't be afraid to admit that it's not easy, because it's not. We all had to learn and had to go through it, so look to the resources available, do your research, and if you do have those relationships with other [experts and preparers] – reach out to them'. **Eliza McLaren, Corporate Accountant, The Regional Municipality of York, Canada**

Government is complex. Although it is true that many of its transactions are easily accommodated within a receipts and payments model, many are not. This helps explain the significant shift by governments around the world from cash to accrual accounting – with 40% of the 150 countries analysed currently transitioning to accruals.

The experts interviewed by IFAC and ACCA agreed that accrual accounting produces useful information that improves financial decision making. No matter where a country is in developing its economic systems, the information that is generated by accrual accounting can help improve PFM. For those at the beginning of the journey this can manifest through better management of assets as officials understand what assets are owned, their condition and how they are being used. For those further down the path to implementation, information from accruals provides the baseline for a longer-term view of government finances, through intertemporal balance sheet management and sustainability reports. When combined with accrual budgeting, reforms can support a better understanding of the cost of government services and can support a performance-driven system that places finance at the heart of government decision making.

Governments make policy decisions to further social outcomes, respond to external events and comply with national and international laws. Accrual accounting provides additional information that improve PFM in all these areas. Cash information, in common with commercial businesses, remains important for governments in ensuring that bills and obligations are met as they fall due. Governments must still manage cash as part of their PFM – this cannot be abandoned as part of the transition to accrual accounting. It is often said that *'what gets measured gets managed'*. Accrual accounting results in the measurement of activities that would not otherwise fall within a cash environment. But none of this makes a real difference unless good, decision-useful information is produced from these measurements. With many governments either already directly or indirectly adopting IPSAS standards, and others planning to do so over the next few years, there is a fantastic opportunity to produce new information: information that can be used to make decisions, unlocking the power of accrual accounting.

Panel of international experts

ACCA and IFAC are grateful to the international experts listed below, who gave their time to contribute to this research project.

AUSTRALIA
Vincent Padgham
Libby Stratford
Sean Osborn
Clinton Gould
Marsha Guthrie

AUSTRIA
Bernhard Schatz

CANADA
Bailey Church
Eliza McLaren
Ross Smith
Joao Carlos Fonseca
Joyce Evans

NEW ZEALAND
Ian Douglas Ball
Ken Warren

SLOVAKIA
Lucia Kasiarova
Jozef Hýbl
Zuzana Letkova

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TANZANIA
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UK
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Vicky Rock
Andrew Evans
Olivia Halliday
Matthew Rowe
Daniel Tuck-Martin

ZIMBABWE
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Nelson Maseko
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