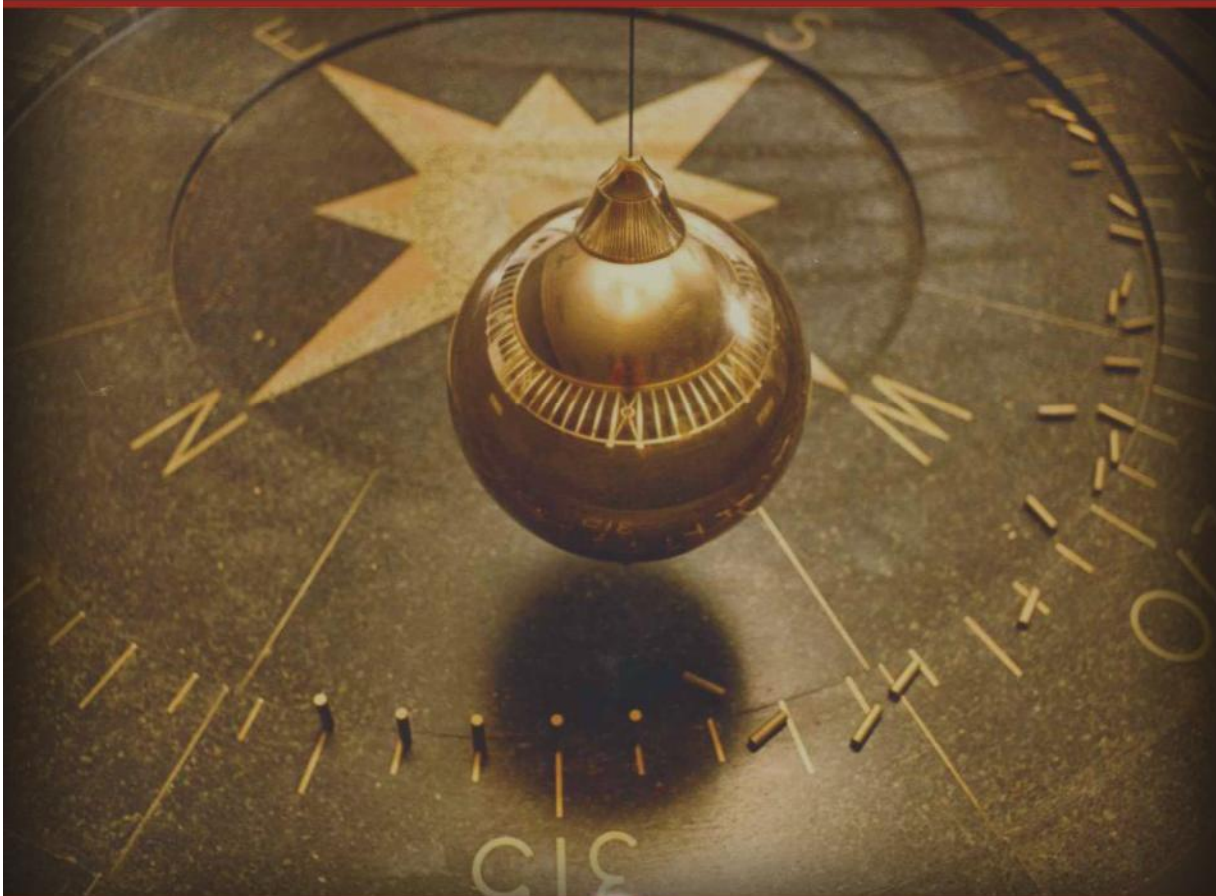


# Changing Times in Government Accounting

(A Status Paper)



Prepared By  
**Committee on Public Finance & Government Accounting**  
The Institute of Chartered Accountants of India  
(Set up by an Act of Parliament)  
New Delhi

Changing Times in Government Accounting  
(A Status Paper)

Prepared  
By

Committee on Public Finance and Government Accounting  
The Institute of Chartered Accountants of India  
(Set up by an Act of Parliament)



## FOREWORD

The global rise of Government Accounting is fundamentally due to the greater demand for accountability in a democracy and market economy. Accounting information can be used to monitor and enforce the terms of economic, social and political contracts. Over the last 25 years, there has been some notable institutional and conceptual innovations in government accounting, contributing to its greater visibility and influence.

Unlike in the private sector, where accounting is needed primarily to assess the profits (loss) earned (incurred) by an entity and changes in its net worth over a period, the primary objective of accounting in government is to ensure that the public finances of the country are managed in conformity with the directions of the legislature, in short establish the government's accountability for raising and spending public funds.

Although only a few countries have, so far successfully implemented a full accrual accounting framework, other countries ranging from transition economies in Europe to developing countries in the Middle East are considering such a move and are increasingly expressing an interest in receiving technical advice on various aspects of understanding such a major reform. I appreciate CA. Anuj Goyal and the Secretariat of the Committee for visualizing and bringing out this status paper.

I sincerely hope this status paper would be useful to various stake holders and find an acceptance among the members and other interested reader.

CA. Amarjit Chopra  
President

New Delhi



## PREFACE

In this era of globalization and economic liberalization the prevalent accounting standards, principles and practices are found inadequate to capture, measure and report the present day transactions and activities of a modern enterprise including government.

Accounting reforms are also on the way for conversion of government accounting system both at the Centre and in the States from traditional cash-based accounting to accrual-based accounting. Current government accounting system is primarily on cash-based accounting procedures introduced during the British colonial regime. Though appropriate modifications have taken place from time to time, the existing system is deficient in bringing transparency, completeness, user friendliness and enforcing accountability and performance.

It is evident that the accrual-based double-entry accounting system is more complex than the simple cash-based, single-entry system most urban bodies are used to. The shift to the new system will require more resources and training of personnel. But the fruits of labour will be worth the effort for the organisation, the government, and most importantly, for the citizens. Among the numerous changes in government accounting in recent years, the emergence of International Public Sector Accounting Standards (IPSASs) stands out as the most significant development.

The purpose of these papers is to highlight the importance of accounting reforms, the crucial need to change from cash to accrual system, single to double entry accounting, green accounting, role of CA's in government accounting reforms etc.

I also wish to place on record my sincere gratitude to CA. Amarjit Chopra, President ICAI and CA. G. Ramaswamy, Vice-President ICAI for their vision and support to the Committee on Public Finance and Government Accounting.

I sincerely appreciate the efforts put in by CA Shalini Jindal, Secretary, Committee on Public Finance and Government Accounting, Dr. Nikhil Saket, Sr. Assistant Secretary, Committee on Public Finance and Government Accounting and the entire staff of the committee for conceptualising and preparing the status paper.

I believe that these papers would be immensely helpful and beneficial to the various stakeholders, members of the profession and other readers.

New Delhi  
27-12-2010

CA. Anuj Goyal  
Chairman



CONTENTS	Pages
1. Government Accounting – An introduction	10
2. Purpose of Government Accounting	11-12
3. Government: Methods/systems	12-15
4. International perspective	16-17
5. Move towards accrual accounting: International experience	17-21
6. Overview of Accounting System in other countries	21-22
7. International Public Sector Accounting Standard Board	23-25
8. Lessons Learnt from International experience	25-26
9. Indian perspective	27
10. Principles of Government Accounting in India	28
11. Present Basis of Accounting	28-29
12. Limitations of the present system of accounting	29-31
13. Accrual Basis of Accounting	31-34
14. Benefits of Accrual Accounting	34-37
15. Rationale for moving from cash basis of accounting to accrual basis of accounting	37-38
16. Pre- conditions for implementation of accrual accounting	38-40
17. Measures involved in implementation of Accrual Based Accounting	41
18. Move towards accrual accounting : Position of India	41-47
19. Initiatives required to be taken by the Government	48
20. Key issues involved in transition	48-54
21. Costs of implementing Accrual Accounting	54
22. Time frame and Broad Work Plan	54-61
23. Accounting Reforms a Must	62-63
24. Rationale for a system of “Green Accounting” for India	63
25. Role of ICAI and its members	64-67
26. Conclusion	67-68
27. Bibliography	69



## **ABBREVIATIONS**

ASLBs–Accounting Standards for Local Bodies

CGDA–Controller General of Defence Accounts

CGA – Controller General of Accounts

C&AG – Comptroller & Auditor General

FMIS – Financial Management Information Systems

GAAP- Generally Accepted Accounting Practices

GASAB–Government Accounting Standards Advisory Board

GFMS–Government Financial Management Information System

IGAS–Indian Government Accounting Standards

IGFRS- Indian Government Financial Reporting Standards

IAS–International Accounting Standards

IASB–International Accounting Standards Board

IASC- International Accounting Standards Committee

IFAC–International Federation of Accountants

IFRS–International Financial Reporting Standards

IPSAS–International Public Sector Accounting Standards

IPSASB–International Public Sector Accounting Standards Board

IMF –International Monetary Fund

LMMHs–List of Major and Minor Heads

NMAM–National Municipal Accounts Manual

NMAVMM–National Municipal Asset Valuation Methodology Manual

RAB- Resource Accounting & Budgeting

ULBs–Urban Local Bodies

## Government Accounting – An Introduction

The process of globalization and economic liberalization that we are witnessing in India since 1991 is bringing about a unique and unprecedented change in the philosophy or role of the Government as well as in the relationship between the State and its citizens. Citizens are thinking more as consumers in relation to the Government. Governance is increasingly being seen as a participatory and contractual process in which citizens play a prominent role in designing, implementing and monitoring the public policies. In this scenario, it has become increasingly necessary for the Indian government to respond to the needs of its people by measuring their responses to Government initiatives. Also the Government is now expected to be more transparent and accountable in governance for achieving the ultimate objective of general welfare of citizens. This changing role or philosophy of the government demands that citizens in a democratic society deserve a fair account as to how their Government is managing the fiscal affairs of the economy, like the investors in a company who need a fair account of the company's financial affairs and performance.

Accountability and transparency are the twin basic objectives of an accounting system, which is becoming highly significant for the government accounting system in the post liberalization and globalization era. These are not only theoretically relevant but demanding immediate attention of the Government to make it a part and parcel of the Government financial reporting system. Government activities are generally concerned with provision of essential goods and services to citizens, social welfare measures, macro-economic management of the economy, pursuit of inter-generational equity, conservation of the nation's heritage and natural environment, management of government assets and liabilities, community welfare, social justice and economic prosperity of the people.

## Purpose of Government Accounting

Government accounting has three purposes. The basic purpose is to safeguard the public treasury by preventing and detecting corruption and graft. Corruption in government exists in various forms, and is nurtured by incentives (Rose-Ackerman, 1978).

This is an acute problem in economically poor and developing countries, but corruption is not limited to them (Rose-Ackerman, 1999). Citing a recent report by the International Monetary Fund (IMF) and the International Development Association, Thomas (2001, p. 38) observed that heavily indebted, poor countries 'lack the practices and procedures necessary for budgeting, monitoring, and reporting on the use of public resources. While it is tempting to link corruption with dictatorship, corruption can also occur in a democracy, despite the checks and balances built into the machinery of government to thwart and unearth fiscal misconducts. For example, more than a century after its Declaration of Independence, the United States still needed a municipal reform movement to emphasize basic financial record keeping to fight corruption in local governments (Ghan, 2001). The intermediate purpose of government accounting is to facilitate sound financial management.

Financial management includes activities such as collecting taxes and other revenues, paying bills, borrowing and repaying debts. In a well-run government, these activities are budgeted or otherwise planned. Their execution through duly authorized transactions is recorded in the financial accounting system. Reformers want governments to operate in an economical, efficient and effective manner. In that process, governments will also need a management or cost accounting system to find out the cost—or better still, the least cost—of providing government services. Almost 50 years ago, Herbert Simon and his associates counselled corporate controllers to go beyond their score-keeping function to direct management's attention to problem areas and help solve problems (Simon et al., 1954). The advanced purpose of government accounting is to help government discharge its public accountability.

Public accountability exists in three levels of principal-agent relationship: accountability of the bureaucrat to the chief executive, of the executive to the legislature, and of the government to the people. This purpose can be better achieved by increasing the agent's incentive to disclose and by lowering the principal's information costs. Downs (1957) cautioned that it is rational for voters to be ignorant because of the high cost of becoming informed. The purposes of Government accounting are labelled as 'basic', 'intermediate' and 'advanced' to convey the order of priorities in building the full capacity of a Government accounting system. Such a system is different from commercial accounting in some fundamental respects.

## Government : Methods/ Systems

The Government, as we all know, is not there to make profit. Neither is it a manufacturing organisation. Considering this, a school of thought has emerged that government accounting need not to be the same as commercial accounting. The advocates of this thought are of the opinion that an accounting system that records each and every transaction of the government which also has an inbuilt facility of comparing the budgeted figures with the actual, will serve the purpose. There is another school of thought which does not favour this view and is of the opinion that the accounting system should be such that in addition to the above it should be in a position to comment on the working of the government and also reflect on the assets and liabilities of the government. To put it in simple words the accounting system should be in position to generate relevant information for decision-making. The two schools of thought that are under reference are cash accounting and accrual accounting. In between these two, other methods of preparing the accounts have also been suggested in the recent past.

The methods or systems of preparing government accounts can be classified into four broad categories:

- Cash
- Modified Cash

- Modified Accrual
- Accrual

#### Cash Accounting :

The cash basis of accounting, measures the flow of cash resources. It recognises transactions and events only when cash is received or paid. Financial statements produced under the cash basis of accounting cover cash receipts, cash disbursements, and opening and closing cash balances. A cash accounting system has the advantage of being simple.

#### Modified Cash Accounting :

The modified cash accounting recognises transactions and events that have occurred by year-end and are normally expected to result in a cash receipt and/or disbursement within a specific period after year-end. Under this system, the accounting period includes a complementary period for payments (e.g., one or two months) after the close of the fiscal year. Receipts or payments over the complementary period that are related to the transactions of the previous fiscal year incurred during the fiscal year are reported as the revenue or expenditure of the previous fiscal year. Usually, this is achieved by keeping the books open during the complementary period. This aims at ensuring a greater conformity between the annual commitments made during a fiscal year and the payments that are reported as budgetary expenditures.

#### Modified Accrual Accounting :

The modified accrual accounting (sometimes also called as expenditure basis) recognises transactions and events when they occur, irrespective of when cash is paid or received. However, there is no deferral of costs that will be consumed in future periods.

Physical assets that will provide services in the future are written -off (or expensed) in the period of acquisition. Modified accrual and full accrual accounting (discussed subsequently) have the same accounting framework. The major difference, however,

lies in the time between the acquisition of goods and assets and their utilisation. Under modified accrual accounting, supplies are considered consumed and assets are written-off as soon as they are acquired. Under full accrual accounting, changes in inventories are recognized and assets are progressively depreciated according to their useful life.

#### Full Accrual Accounting :

Like modified accrual, the full accrual basis recognises transactions and events when they occur irrespective of when cash is paid or received. Revenues reflect the amounts that came due during the year, whether collected or not. Expenses reflect the amount of goods and services consumed during the year, whether or not they have been paid for during that period. Costs of assets are deferred and charged when the assets are used to provide services. Full accrual accounting is similar to the accounting system for private enterprises (commercial accounting). Expenses recognised by the full accrual basis of accounting should not be confused with actual expenditures. They are the costs of goods and services consumed as well as any increase of liabilities or decrease of assets over the accounting period (e.g. they include depreciation and losses, which can occur in the absence of transactions). Financial statements produced under a full accrual accounting system covers revenues; expenses (including depreciation); assets (financial and physical); liabilities; and assets (Schiavo- Campo and Tommasi, 1999). Under full accrual system the three statements that are normally prepared include, Operating Statement, Balance Sheet, and the Statement of Cash Flows. The number of the statements and the nomenclature by which these are called may differ from country to country.

The abilities of each basis of accounting in providing information that meets the objectives of financial reporting are summarized in Table 1.

**Table 1**

**Alternative Bases Accounting including Modification to those Bases-Ability Meet Objectives**

<b>Objective</b>	<b>Cash</b>		<b>Accrual</b>	
	<b>Cash Basis</b>	<b>Modifications to the Cash Basis</b>	<b>Modifications to the Accrual Basis</b>	<b>Accrual Basis</b>
Compliance with legally adopted budgets	Yes	Yes	Yes	Yes
Compliance with legal and contractual requirements, including spending limits.	Relating to cash requirements and limits.	Cash and near cash requirements and limits.	Cash and financial resources requirements and limits.	Cash and economic resources requirements and limits.
Source, allocation and uses of financial requirements.	Cash resources	Cash and near cash resources.	Cash and financial resources.	Cash and financial resources.
Financing and cash requirements.	Cash resources	Cash and near cash resources.	Cash and other financial requirements.	Cash and other financial requirements.
Ability to finance activities and to meet liabilities and commitments.	From cash	From cash and near cash	From financial resources	From economic resources.
Financial condition and change therein.	Cash position	Cash and near cash position.	Financial resources.	Financial and economic resources.
Financial performance in terms of service costs.	Information not reported.	Information not reported.	Limited information reported.	Provides information necessary to assess performance.
Source: Government Financial Reporting, Study 11, IIFAC Public Sector Committee.				

## International Perspective

The activities of the governments of various countries have enormously expanded over the last few decades. This has necessitated mammoth increase in the incurrence of expenditure and raising of commensurate resources by the governments. In turn, this has led to increased awareness about ensuring greater accountability of the government towards taxpayers and other segments of society. One of the means of ensuring public accountability is dissemination of relevant financial information about the operating activities of the government and its financial condition. Until the governmental activities were limited, this need was largely met by the financial information generated by what is known as cash basis of accounting. However, it is being increasingly felt in various countries that the financial information generated on the basis of cash basis of accounting does not meet the need of public accountability effectively. This realisation has led to reforms in government accounting since 1980 in many countries. The major focus of such reforms has been towards generation of relevant financial information for ensuring greater accountability of the governments. One of the most important features of these reforms has been shift from cash basis of accounting to variants of accrual.

There is no standardized global framework for the adoption and implementation of accrual government accounting. This has led to the questioning of the consistency and comparability of financial statements prepared and presented in different jurisdictions. Two approaches are widespread which deal with the issue of financial consistency and comparability across nation and organizations; the accounting approach and statistical approach. Whilst the former uses accounting standards for the preparation and presentation of general purpose financial statements, the later emphasizes the statistical bases for producing accounting information for economic analysis and policy making. Many countries have adopted both approaches providing widely different financial measurements. This does not seem to be an effective way of using resources. However, there are some promising bridges between them in applying and requiring consistent financial information. Harmonizing these two systems into a



single set of Government reports is a significant international issue in public sector accounting.

The last three decades have witnessed substantial efforts to reinvest the public sector around the world. Public sector reform ideas which started more of a political and ideological phenomenon such as "Thatcherism" (in the UK), "Reagonomics" (in the USA) and "Rodernomics" (in New Zealand) are becoming a reality (Broadbent and Guthrie, 1992). Collectively these public sector reform ideas have been referred to as "New public Management" (Hood, 1995; Guthrie et al., 1998, 1999, and 2005). Couched in the language of economic rationalism or neo-liberalism, new public management aims to replace the weberian approach to public administration with a management model which is used in private enterprise (Hood, 1995; Carlin, 2006).

### Move towards Accrual Accounting: International experience

In recent past, several countries have reformed their accounting system or are in the process of implementing reforms. It is evident that New Zealand, Australia, France, United Kingdom and United States of America are among the first to initiate accrual accounting in government. In addition to the above, Malaysia and Tanzania have also implemented accrual accounts at local government level. Canada is reported to be using modified accrual accounting and is moving towards a full accrual system.

In US the Governmental Accounting System is designed, inter alia, to present fairly and with full disclosure the financial position and results of financial operations of the governmental units in conformity with generally accepted accounting principles, which are based on accrual/modified accrual system of accounting. So far as US budget is concerned, now US is moving away from a strict cash budget towards a blend of cash and accrual concepts.

Germany has a long tradition of accounting regulation which has always been within the responsibility of the Legislature. Many changes have taken place in recent years in

the accounting environment as a result of European Regulations and numerous National Laws as a result of changes in capital market.

Brazil is currently undergoing a gradual process of converging its Accounting Standards with the International Financial Reporting Standards issued by the International Accounting Standards Board. A number of developments have recently advanced Brazil's progress towards IFRS. In March, 2006, the Central Bank of Brazil announced that as of 2010 all financial institutions under its supervision are required to prepare their consolidated financial statements in accordance with IFRS.

In Spain in 1998, the General Internal Audit and Accounting Office issued "Government Accounting Principles" (IGAE 1994).

The UK Government, from April 2001, heralded a new era in public sector financial management reform, with the full implementation of Resource Accounting and Budgeting (RAB). RAB is an accrual based approach to Government accounting and budgeting, which also reflects Parliamentary control and a move to focus on outputs, rather than inputs. The term "resource accounting" was devised to highlight that the change proposed by the UK Government goes wider than simply adoption of accrual accounting techniques. Other key aspects are the link between inputs and departmental aims, objectives and outputs.

In France, the development of accrual accounting was a strong priority for the French Ministry of Finance. This priority and the context in which it was to be applied was established by the new budgetary rules established by the Constitutional Bylaw 2001. Accrual accounting aimed to bring out a change that involves performance-oriented management, globalised allocations, managers' responsibility and accountability, and long-term management. However, French Government has decided to adopt 'dual' system which led to:

- A cash-based approach for the budget i.e. the recording of payments received and expenditures authorised or paid by a public accountant.
- An accrual-based approach for accounting, although currently only receipts are recorded on this basis.

The dual system thus combines the elements of cash-based accounting (budget accounts) and accrual accounting (financial accounts), although these were still not fully in place, particularly for accrual accounting. The aim of the French Government was that the accrual based general government accounts should be prepared from 1<sup>st</sup> January 2005 while maintaining the conventional budget presentation in terms of receipts and payments on cash basis.

New Zealand is perhaps the most accomplished nation in establishing the accrual-based Government accounting system. New Zealand now publishes Government accounts similar to those of private sector companies, the only Sovereign nation to do so. It introduced accrual accounting in early 1990s and published its first set of accounts on accrual basis for year ending June 1992. "New Zealand Inc" produces a balance sheet of assets and liabilities and an accrual-based operating statement of income and expenditure. These accounts, which are independently audited, encourage governments to focus on the longer-term consequences of policies.

These reforms have been labelled the most far-reaching and ambitious in the world.

Following are the benefits realized by New Zealand from the accrual accounting reforms:

- Shift to accrual accounting benefited improvement in cash management.
- Planning of savings could be made as it lead to elimination of idle cash balances.

- Better accounting for and management of accounts receivables.

These benefits far outweighed the costs involved in the transition to accruals accounting. Other benefits are listed as follows :-

- By providing adequate depreciation on capital assets spread over their useful lives, it was possible to ascertain the full costs of output production each year (by matching the relevant portion of capital costs to annual revenue flows) and compared with other years.
- This also helped in making comparisons with prices of alternative sources of supply available in both the public and private sectors. The system also helps to ascertain if cost is recovered for services provided and whether the recovery is adequate.
- Bringing assets into existence in the balance sheet has helped the Government in focusing attention on those assets which are no longer useful and can therefore be disposed of and increase the cash flows so that newer assets for increased production could be funded from these inflows without having recourse to funding from outside the Department.
- Bringing all assets and liabilities into the balance sheet provided the Government with an update of the fiscal position and the report did indicate that the external debt of the Government was a matter of concern.

In Canada, until the 1980's, Canadian Government budgeted and accounted for its financial affairs on a cash basis, and reported on them through a series of separate accounts and fund financial statements. Throughout the 1980's, Canadian Government significantly changed its financial reporting practices, moving from cash to accrual accounting. In the past, Canadian Government argued that the cash basis for

accounting best meets their needs. It's focus on cash flows enables them to monitor the spending and formed the basis of Government budgetary and expenditure control. However, it was realised that the cash basis of accounting simply did not provide sufficient information to assess a government's financial requirements. Focussing solely on a government's outstanding borrowings ignores other liabilities that will be just as much of a drain on a government's financial resources.

## Overview of Accounting System in other Countries

Countries that have set in motion the process of moving over to an accrual based accounting system are :-

- Fiji Islands
- Indonesia
- Marshall Islands
- People's Republic of China
- Philippines
- Republic of Korea
- Sri Lanka
- Mongolia

Table 2 depicts the overall status of accounting system adopted by different countries across the world:

**Table 2**

Country	Status		
	Full Cash Basis	Combination of cash and Accrual Accounting	Full Accrual Basis 1
Australia			√
Austria	√		
Belgium	√		
Cambodia		√	
Canada			√
Colombia			√
Czech Republic	√		
Finland		√	
France			√
Germany	√		
Greece	√		
Hungary	√		
Iceland		√	
<b>India</b>	√		
Indonesia		√	
Ireland		√	
Israel		√	
Jordan		√	
Kenya	√		
Mexico		√	
Morocco	√		
Netherlands	√		
New Zealand			√
Norway	√		
Slovak Republic	√		
Slovenia	√		
Suriname	√		
Sweden		√	
Turkey	√		
United Kingdom			√
United States			√

(Source : Transition to Accrual Accounting- technical Notes and Manuals by IMF, September 2009)

The above countries are generally following IPSAS 1 framework for presentation of financial statements.

## International Public Sector Accounting Standard Board

The mission of the International Federation of Accountants (IFAC), as set out in its constitution, is “to serve the public interest, IFAC will continue to strengthen the worldwide accountancy profession and contribute to the development of strong international economies by establishing and promoting adherence to high-quality professional standards, furthering the international convergence of such standards and speaking out on public interest issues where the profession’s expertise is most relevant.” In pursuing this mission, the IFAC Board has established the International Public Sector Accounting Standards Board (IPSASB) to develop high-quality accounting standards for use by public sector entities around the world in the preparation of general purpose financial statements. IPSASB develops accounting standards for public sector entities referred to as International Public Sector Accounting Standards (IPSAS). These IPSASs focuses on the accounting, auditing and financial reporting needs of national, regional and local governments to the related government agencies and the constituencies they serve.

The adoption of IPSASs or convergence by Governments will improve both the quality and comparability of financial information by public sector entities around the world. So far IPSASB has issued 31 International Public Sector Accounting Standards on accrual-basis accounting and an IPSAS on cash-basis of accounting, applicable to governments across the world which are listed as below.

### List of Accrual Based IPSAS

IPSAS 1—Presentation of Financial Statements

IPSAS 2—Cash Flow Statements

IPSAS 3—Accounting Policies, Changes in Accounting Estimates and Errors

IPSAS 4—The Effects of Changes in Foreign Exchange Rates

IPSAS 5—Borrowing Costs

IPSAS 6—Consolidated and Separate Financial Statements

IPSAS 7—Investments in Associates

IPSAS 8—Interests in Joint Ventures  
IPSAS 9—Revenue from Exchange Transactions  
IPSAS 10—Financial Reporting in Hyperinflationary Economies  
IPSAS 11—Construction Contracts  
IPSAS 12—Inventories  
IPSAS 13—Leases  
IPSAS 14—Events after the Reporting Date  
IPSAS 15—Financial Instruments: Disclosure and Presentation  
IPSAS 16—Investment Property  
IPSAS 17—Property, Plant, and Equipment  
IPSAS 18—Segment Reporting  
IPSAS 19—Provisions, Contingent Liabilities and Contingent Assets  
IPSAS 20—Related Party Disclosures  
IPSAS 21—Impairment of Non-Cash-Generating Assets  
IPSAS 22—Disclosure of Information about the General Government Sector  
IPSAS 23—Revenue from Non-Exchange Transactions (Taxes and Transfers)  
IPSAS 24—Presentation of Budget Information in Financial Statements  
IPSAS 25—Employee Benefits  
IPSAS 26—Impairment of Cash-Generating Assets  
IPSAS 27—Agriculture  
IPSAS 28—Financial Instruments: Presentation  
IPSAS 29—Financial Instruments: Recognition and Measurement  
IPSAS 30—Financial Instruments: Disclosures  
IPSAS 31—Intangible Assets



Cash Basis IPSAS :

Financial Reporting under the Cash Basis of Accounting

Significant changes in the international arena in respect of public sector accounting and financial reporting systems over the last two decades and their increasing convergence to accrual-based system of accounting have necessitated a review of prevalent government accounting practices in India as well.

The World Bank has been conducting gap analysis of Government accounting with cash basis IPSAS.

Lessons learnt from International experience

The implementation of accrual accounting in Government is a major exercise, particularly if it is done in a way that will provide maximum benefit to decision making processes and accountability to external users. The New Zealand Government's experience provides so many lessons at both macro and micro levels that it is difficult to distinguish the most critical.

However, probably the most important lesson is that the accrual accounting reforms can be done. There is no fundamental theoretical barrier for a Government which prevents the implementation of accrual accounting. Rather, there is much to recommend the development of accrual accounting in Government when it is implemented in the context of a regime which encourages management performance. This leads to the second major lesson. Accounting is important and exciting when it generates information that is used by decision makers. Conversely, without decision-makers demanding and using accrual information the implementation effort is far less likely to succeed. While the demand for accrual accounting information is likely to increase development of accrual information should be seen as an integral element of this reform and not a standalone.

At operational level a number of lessons can be highlighted:

- Commitment is critical. This requires a clear understanding that accrual accounting will not bring benefits as of itself but by providing richer information by improving the quality of decisions. The lesson is that commitment based on false expectations will not continue. The net fiscal costs of operationalizing accrual accounting systems compared with cash systems are relatively trivial. Over centralized accounting processes, with subsidiary elements that are more-or-less poorly integrated are surprisingly cumbersome and expensive when compared with the best private sector practices of centralized cash management, with streamlined financial management systems.
- Trade-offs will be necessary and therefore a shared understanding of key goals is required to make such trade-offs. An example is the Treasury decision not to engage in training for departmental financial managers despite one view that training was necessary to realize the benefits and reduce the risks associated with the new regime. In terms of the higher level objectives and other demands to achieve those objectives this was the right decision.
- Identify and respond to major risks. In the New Zealand setting these included the specification of the outputs of Government, the identification of all the assets in the Crown estate, defining the Government reporting entity and eliminating the build-up of processing backlogs. In the final analysis none of these issues was allowed to derail the implementation.
- Achieve major gains from leveraging off private sector accounting. By making use of GAAP the best of private sector off-the-shelf accounting software could be used and the pool of skills and expertise available to the financial management reform was sufficiently widened to cope with the new demands and make benefit from the new opportunities.

## Indian Perspective

Government accounting and financial reporting in India have a history of several centuries. Our current government accounting system, both in the Union and the States, derives its form and substance largely from the cash based book-keeping procedures, which were introduced during British times. We have, of course, modernized the system of data collection but have continued to remain essentially on a cash basis. While the variety and richness of the information being provided by the current system cannot be denied, the prevailing system in India is somewhat deficient on the dimensions of accountability and ease of use. Being primarily focused on inputs, the cash based system cannot be used effectively to fix accountability for performance. Transactions where no cash is paid or received are not recorded, even if value has been received or a liability contracted. Past transactions relating to assets and liabilities cannot be captured automatically but only through elaborate subsidiary information.

The result of these deficiencies is that it is difficult to keep an accurate track of assets and it is easy to understate liabilities. More significantly, Government departments that offer commercial goods and services quite often face the risk of not knowing their full cost as the current system does not automatically record and provide this information. These deficiencies result in weak stewardship, lack of transparency and an impaired ability to accurately predict the future cost of a current financial commitment.

## Principles of Government Accounting in India

The main principles according to which the accounts of the Government of India are maintained are contained in Government Accounting Rules, 1990; Accounting Rules for Treasuries; and Account Code Volume-III. Detailed rules and instructions relating to the forms of the initial and subsidiary accounts to be kept and rendered by officers of the Department of Post and technical department are laid down in the respective Accounts Manual or in the Departmental Regulations relating to the Department concerned.

### Present Basis of Accounting

Presently, the Government Accounting and Financial Reporting is based upon cash based system of accounting which in consonance with the basis followed for the formulation of the budget of the Government. Cash Basis of accounting denotes that the transactions in Government accounts represent the actual cash receipts and disbursements during a financial year as distinguished from amounts due to or by the Government during the same period. However, certain book adjustments may be specifically authorized by the Central Government on the advice of the Comptroller and Auditor General of India, as exceptions to the cash basis of accounting.

The basis of accounting being cash, the depreciation of physical assets and impairment losses are not recognized or expensed. The losses or write-offs of the physical assets at the end of their life are also not recognized or expensed in the accounts.

Under Cash Basis of accounting transactions are recorded when there is actual flow of cash. Revenue is recognized only when it is actually received. Expenditure is recognized only on the outflow of cash. No consideration is given to the "accrual" fact of the transaction. All cash received or spent during the year are taken into account even though some part of these may relate to different period.

Under this system the liabilities are not accrued for and there is no charge for the use of the capital asset and no distinction is made between the capital and non- capital expenditure. Each department of the government prepares an appropriation account showing how much was voted for that department by the Parliament for a given year and how much was spent under each head, showing explanatory notes for any major variances between estimates and actuals.

This system of accounting is noted for its simplicity, certainty and the linkage to the direct movement of the funds and as such needs less skill on the part of the accountant. Its whole focus is on cash management. The recognition trigger is simply the flow of cash. Budgetary and legislative compliance is easier under this system. It does not take cognizance of performance and output.

### Limitations of the present System of Accounting

In spite of its simplicity and ease of its application, the existing system suffers from the following limitations:

- It does not provide a complete picture of the financial position i.e. information on assets and liabilities are not available for fixed assets (land, building, machineries, defence, heritage assets etc.)
- No information about capital work-in-progress like dams, power plants, roads, bridges etc. is available.
- It does not give full information on current assets e.g. accrued income like outstanding royalty, fees, service charges, tax arrears etc.
- Comprehensive information is not available on government liabilities (pensionary commitments, interest due, bills payable.)

- Unit cost and total cost of services provided by the Government departments like health, education, water supply, transportation etc. is not ascertainable (as depreciation, interest etc. are not apportionable)
- It ignores certain transactions by not recording expenditure already incurred but payment not made e.g. supplies made, salary, telephone charges, overdue interest etc. and also revenue earned but cash not received e.g. license fees, services delivered (electricity, water etc.)
- It gives a wrong picture of income received, as advance tax receipts are recognized as income, which leads to incorrect measurement of Income.
- No weightage is given to the concept of 'matching' i.e. expenses of a specific period should be set off against the revenue of the same period.
- No disclosure is made about contingent assets and contingent liabilities which may turn into committed ones on account of guarantees given or letter of comforts issued by the Government.
- No information is provided about existing net liabilities of public enterprises and agencies outside the Government, although the latter cannot escape such liabilities.
- No disclosures are made for Accounting Policies on the basis of which Financial Statements are prepared.
- It provides room for fiscal opportunism e.g. tax revenues can be collected in excess during a particular period followed by high incidence of refunds together with interest; payments can be easily deferred and passed on to the

next financial year; revenue due in the future could be compromised by providing for one time payments.

- It permits practices like booking of transactions temporarily under the 'suspense account' head. But these exceptions have been misused affecting the quality and completeness of accounts and providing scope for manipulations.

Due to the above disadvantages, it is not possible to get the real picture of the Government financial performance and position. Hence Government Accounting reforms are needed to ensure greater transparency, accountability and to overcome the limitations of cash basis of accounting. Therefore, clearly there is a need to switchover to the Accrual Basis of Accounting.

### Accrual Basis of Accounting

It is a system of accounting in which transaction are entered in the books of accounts, when they become due. The transactions are recognized as soon as a right to receive revenue and/or an obligation to pay a liability is created. The expenses are recognized when the resources are consumed and incomes are booked when they are earned. Therefore, the focus is on the recording of flow of resources i.e. labour, goods, services and capital., the related cash flow may take place after some time (of event) or it may or may not take place in the same accounting period.

The key elements involved in accrual accounting

**Expenditure:** When expenditure is recorded on an accrual basis unpaid expenses are recorded as sundry creditors and brought forward to the balance sheet.

**Revenue:** When revenue is recorded on an accrual basis income not received is recorded as sundry debtors on the balance sheet with provisions for bad debts.

Assets and Liabilities: Simple rules of cost and longevity determine whether an asset is written off as expenditure in the year of purchase or capitalised and recorded in a fixed assets ledger. Depreciation is usually either by straight line or reducing balance over the life of the asset. Assets and liabilities are brought forward to the balance sheet and depreciation is netted off.

Financial and non-financial Assets and Liabilities: An economic and not an accounting distinction is made between financial and non financial assets and liabilities. Financial assets and liabilities are for example; investments and loans and non-financial assets and liabilities are for example land/property and compensation schemes. The major difference and difficulty in government is the determination of its' non-financial assets and liabilities, their valuation, longevity, method of depreciation and recording in the balance sheet.

### The Five Stages of Accrual Accounting

Stage	Characteristics
Default: No Accrual	-Cash <ul style="list-style-type: none"> <li>• Level of cash at the end of day, month, quarter, year</li> <li>• Cash receipt – cash disbursement during a period</li> </ul>
1 <sup>st</sup> Degree: Mild Accrual	-Current financial resources <ul style="list-style-type: none"> <li>• Accounts receivable</li> <li>• Taxes receivable</li> </ul> <hr/>



In general Government claims against others, convertible to cash within one year, net of allowance for uncollectible amounts

-Current liabilities

- Accounts payable
- Grants payable
- Benefits payable

In general, other claims against Government, requiring cash payments due within one year.

2<sup>nd</sup> Degree: Moderate Accrual

-Current financial resources

- Non-current financial resources- claims against others but not convertible to cash within 1-year

-Current Liabilities

- Long Term liabilities- others' claims against Government but not due within 1 year
  - Contingent liabilities- probable long-term claims
- 

3<sup>rd</sup> Degree: Strong Accrual

-Current financial resources

-Non-Current financial resources

-Capital assets, net off depreciation

-Current liabilities

-Long term liabilities

-Contingent liabilities

4<sup>th</sup> Degree: Super-Strong Accrual

- Current financial resources
- Non-Current financial resources
- Capital assets
- Current liabilities
- Long term liabilities
- Contingent liabilities
- Tax collections regarded as liability: no revenue recognized until services are rendered

5<sup>th</sup> Degree: Radical Accrual

- Current financial resources
- Non-Current financial resources
- Capital assets
- Current liabilities
- Long term liabilities
- Contingent liabilities
- Unearned revenue
- Legislative social benefits (entitlements)

### Benefits of Accrual Accounting

The system of Accrual Accounting while retaining the advantages of the Cash Accounting System overcomes its limitations by inclusion of Cash Flow Statement in the Financial Statement of the entity. The major advantages of accrual accounting are as follows:

- It helps in the assessment of financial performance by correctly reflecting surplus/deficit as all expenses whether paid or not and all incomes whether received or not are duly accounted for.

- It provides comprehensive information on expenses, which helps in knowing the cost consequences of policies and enables comparison with alternative policies. Also, information about calculation of subsidy can be extracted from the accounts, which helps in its rationalisation. This ensures the adoption of best policy, which in turn assures optimal use of scarce resources. It also helps in ascertaining the future sustainability of programmes.
- Liquidity position of the Government can be better assessed.
- It gives comprehensive information on the Financial Position i.e. assets and liabilities of government. In this system of accounting the financial decisions are not seen merely from the point of view of cash outgo or inflow but also from their impact on the asset- liability position of the government, future funding requirements of assets enabling planning of their timely maintenance and replacement.
- It gives disclosures on account of contingent assets and contingent liabilities so that risk associated with the guarantees issued and letters of comfort given can be better assessed by the user of the financial statements.
- It bridges the gap leftover by cash accounting by inclusion of accrued expenses and revenues (receivables and payables), physical assets, capital work-in-progress and depreciation, pension liabilities and provisions etc. in the accounting system.
- It discloses the Accounting Policies used in the preparation of Financial Statements for better understanding and appreciation of the Financial Statements.

- The accrual accounting provide scope for addressing the improved disclosure norms for government debts, subsidies, off-budget government borrowings, contingent liabilities and revenue exemptions granted by the government.
- The accrual system of accounting system considered better in terms of transparency and user-friendliness. This will help the management in taking informed decision on allocation of resources and also help curb various malpractices in the garb of accounting.

As far as users are concerned, the information contained in reports prepared on an accrual basis is useful for their decision making. Financial reports prepared on an accrual basis allow the users to;

- Assess the accountability for all resources the entity controls and the deployment of those resources;
- Assess the performance, financial position and cash flows of the entity;
- Make decisions about providing resources to, or doing business with, the entity;
- Evaluate government's ongoing ability to finance its activities and to meet its liabilities and commitments.

Governments need information about expenses in order to assess their revenue requirement, the sustainability of existing programme, and the likely cost of proposed activities and services. Accrual accounting provides governments with information on the full costs of their activities and services provided by the Government, with details on how much of the cost is borne by tax payer and by specific user of the Government's service. so that they can;

- Consider the cost consequences of particular policy objectives and the cost of alternative mechanisms for meeting these objectives;
- Decide whether to fund the production of services within government sub-entities, or whether to purchase goods and services directly from non-government organization;
- Decide whether user fees should cover the costs associated with a service; and
- Allocate responsibility for managing particular costs.

## Rationale for moving from cash basis of accounting to accrual basis of accounting

The need for reforms in accounting originates from the realization of the limitations of the existing system. At the macro fiscal level, the importance of accrual accounting for macro economic policy arises from the fact that it measures assets and liabilities that are relevant to the overall stance of fiscal sustainability, but which are not measured by cash accounting. In particular, whereas cash accounting measures only conventional debt, accrual accounting measures other quasi-debt liabilities such as amount payable for the receipt of goods and services, and employed liabilities.

An accrual accounting framework is essential to systematically determine the full cost of government's activities. Full cost information (including non-cash costs such as depreciation, accrued civil service pensions) is essential for assessing the efficiency of government services and thus is a key element of any public sector performance management framework. More specifically, information about the full costs of government services can be crucial when considering alternative service delivery options including outsourcing and cost recovery, as well as for purpose of international benchmarking (e.g. comparing the costs of health or education services).

Various Finance Commissions have, in the past, concerned themselves with improvements in accounting procedures as a means to ensure a better assessment of

the fiscal position of the Central and State governments. One significant recommendation made earlier relates to the introduction of accrual based accounting system in Government.

## Pre-conditions for Implementation of Accrual Accounting

There are a number of prerequisites to the successful implementation of accounting reforms in a government organization. Careful attention to these factors will help to ensure that any attempts to reform the accounting system meets with success. The main factors can be summarized as follows: -

- ❖ **Consultation and Acceptance:** There is a risk with the introduction of accruals accounting into a Government organization. To be successful, the organization needs to be prepared culturally for its introduction and be willing to respond and accept the benefits that the changes will bring about the costs of implementation in their widest sense. The pre-consultation exercise within government departments and the public consultation exercise are important pre-conditions for success. Acceptance has to go beyond a relatively narrow group of technocrats.
  
- ❖ **Participation of the Accounting Profession:** A complementary precondition is that the accountancy profession is prepared to be interested in and involved with the public sector because not only is the accountancy profession the expert in accounting standards but it has traditionally trained financial managers for the private sector. To be successfully implemented and operated, the reform requires not only an increase in the number of financial managers (who may be qualified accountants) employed by Government but an acceptance of their contribution to the efficient and effective management of the public services.

- ❖ Support of Government Auditor: Successful implementation of accruals accounting does depend heavily upon the understanding of and willingness to support the system by the Government external auditor. As accruals accounting requires not only more complex systems but also a range of new judgments, the responsibilities and expectations of the auditor will change considerably. Therefore the external auditor should be involved in the process from the outset. Auditors will need a thorough understanding of accounting principles and how those principles can be maintained under the pressure of day-to-day administrative decisions.
  
- ❖ Comprehensive Management Training: There exists a need for training of departmental managers to use an accrual accounting system and to achieve the benefits from its operation. There are considerable differences between the information available to managers under cash accounting system and the information available under accrual accounting system. To make proper use of accrual accounting system, managers need not only to understand the differences, but they also need to appreciate how they can use the accrual based information to manage activity more efficiently and effectively.
  
- ❖ A recognition of elapsed time needed: From the outset a willingness to recognize that the introduction of accrual accounting and budgeting will take time usually stretching beyond the lifetime of one Parliament and could therefore stretch beyond the period of control by one political party. The reform therefore needs widespread political support across the political spectrum.
  
- ❖ Application of user-friendly computer technology: This greatly facilitates the introduction of double-entry and accrual reforms, helping to minimize the volume of additional work, including all postings, calculations

and reconciliations. The application of computerized system reduces this burden, freeing clerical staff from many routine accounting applications such as classification of entries under different heads, reconciliation and formation of trial balances and production of final accounts.

- ❖ **Economy:** This entire process of designing an accounting system and implementing it on a manual or computerized basis should be as cost-effective as possible. If such an exercise is designed as a high-cost system it is likely to be opposed at various levels of organization.
  
- ❖ **Budgeting and accounting code structures:** Sound accounting reforms require adoption of a matrix structure for the budget and accounting heads and new accounting should automatically make data available in the correct format, ensuring consistency between all budget and account codes and heads. This may require the adoption of new chart of accounts.
  
- ❖ **Phased implementation:** It is very difficult to introduce all at once sweeping accounting reforms involving an entire organization or departments of Government. A useful sequence for implementation might lead to accounting reforms being carried out first in the Central Accounts Department followed by reform of all peripheral accounting systems and feeder systems. This phased approach can be strengthened through the adoption of fund-based accounting system in place of a single consolidated system. As has been experienced, the preparation for a change to an accrual basis of accounting takes considerable time (several years).



## Measures involved in implementation of Accrual Based Accounting

Adopting an accrual-based double-entry system is an elaborate process that may take several years.

The following measures are required to be taken:

1. Modification of existing laws and rules to introduce double-entry accounting system
2. Appointment of consultants for development of State manual (either based on National Model Accounting Manual or otherwise)
3. Completion and adoption of the manual
4. Personnel Training
5. Business process re-engineering (if required)
6. Valuation of assets and liabilities
7. Production of financial statements (income-expenditure statement and balance sheet)
8. Audit of financial statements

### Move towards Accrual Accounting: Position of India

When we talk about the Government accounts we refer to the Central Government Accounts, State Government Accounts, Accounts of Union Territories and the Local Bodies. Steps that have been taken for accrual accounting reforms in government of India can be traced as under.

#### Reforms in the Central and the State Government

- Government of India set up Government Accounting Standards and Advisory Board (GASAB) in December 2002 for framing the Accounting Standards for the Government. The following is the composition of the GASAB:
  - Deputy Comptroller and Auditor General as Chairperson
  - Controller General of Accounts, Ministry of Finance, Government of India
  - Financial Commissioner, Railways, Ministry of Railways, Government of India
  - Controller General of Defence Accounts, Ministry of Defence, Government of India
  - Additional Secretary (Budget), Ministry of Finance, Government of India
  - Deputy Governor, Reserve Bank of India or his/ her nominee.
  - Director General, National Council of Applied Economic Research (NCAER), New Delhi
  - President, Institute of Chartered Accountants of India (ICAI), or his/her nominee
  - Principal Secretary (Finance)/ Secretary (Finance) of four States by annual rotation and
  - Director General (Accounts)/ Principal Director, Office of the Comptroller and Auditor General of India, as Member Secretary.
  
- A Committee namely, DN Ghosh Committee was also set up by the Comptroller and Auditor General of India for conducting the feasibility study and building up a framework of Government Accounting Reforms in India.

- The Twelfth Finance Commission, recognizing the need for improvements in accounting and financial reporting, recommended a gradual shift to accrual accounting by the Union Government. The Central Government has also accepted the recommendation in principle. Recommendations by Twelfth Finance Commission of India inter alia include to appending the supplementary statements to the present system of cash accounting especially relating to eight areas namely;
  - Statement of explicit and implicit subsidies.
  - A statement containing expenditure on salaries by various departments
  - Detailed information on pensioners and expenditure on Government pensions.
  - Data on committed liabilities in the future.
  - Statement containing information on debt and other liabilities as well as repayment schedule.
  - Accretion or erosion in financial assets held by Government including those arising out of changes in the manner of spending by Government.
  - Implications of major policy decisions taken by Government during the year or new schemes proposed in the budget for future cash flows

- Statement on maintenance expenditure with segregation of salary and non salary portions

This may enable a more complete picture of Government's expenditure on current operations and also on committed liabilities. It may also give more information on financial assets as against presently available in the accounts and facilitate a smooth and efficient transition to accrual accounting system. Out of eight statements mentioned above five statements have been introduced i.e salaries, subsidies, number of pensioners during the year 2005-06, maturity profile of internal debts of Government and loan & advances from Government of India & Change in Financial Assets during 2007-08.

- Government Accounting Standards Advisory Board (GASAB) in its Fifteenth meeting held on 30 July 2008 took a landmark decision to develop Accrual basis Accounting standards for Government. Twenty-one State Governments have expressed their agreement to migrate to Accrual Basis Accounting. The standards will be issued as 'Indian Government Financial Reporting Standards (IGFRS)' and on notification by Government of India will be applicable to Government of India and State Governments in preparation of accounts under Accrual basis accounting. These standards are envisaged to facilitate ongoing pilot studies for migration to Accrual Basis Accounting in Government of India and State Governments. These standards will initially be issued as recommendatory to facilitate transition to Accrual accounting.
- GASAB develops accounting standards under cash basis known as Indian Government Accounting Standards (IGAS) for the existing accounting system and standards for accrual basis under the nomenclature of Indian Government Financial Reporting Standards (IGFRS). The latter is essentially to facilitate pilot studies and the on-going applied research on accrual basis accounting in Government. The Government Accounting Standards Advisory Board has so far developed five IGAS and submitted them to the Government of India for

notification. GASAB has also developed a detailed road map and an operational framework for Government of India and States to migrate to accrual basis accounting. Several other products of GASAB are under various stages of development.

- The Thirteenth Finance Commission has in some ways a unique Terms of Reference when compared to its predecessor Commissions. For the first time, they have been charged with considering amongst other things “the need to improve the quality of public expenditure to improve outputs and outcomes”.

Apart from the Central Government, so far, twenty one (21) State Governments have accepted the idea of accrual accounting in principle. These States include Andhra Pradesh, Assam, Bihar, Chhattishgarh, Goa, Gujarat, Himachal Pradesh, Haryana, Karnataka, Madhya Pradesh, Maharashtra, Manipur, Meghalaya, Rajasthan, Sikkim, Tripura, Uttaranchal, Uttar Pradesh and West Bengal etc. Task Forces are being constituted and pilot studies are also being initiated in many States.

### Reforms in Local Bodies

- The Eleventh Finance Commission in the year 2001 recommended the introduction of Double entry accrual accounting system for the local self Governments.
- Many local bodies have changed over to the accrual system of accounting particularly after the issuance of the National Municipal Accounts Manual (NMAM) by the Ministry of Urban Development, Government of India, supported by the Comptroller & Auditor General of India, National Institute of Urban Affairs and Indo- USAID FIRE-D Project and the inputs provided by the Institute of Chartered Accountants of India. The NMAM provides guidance to ULBs in the

preparation of their accounts on accrual basis. The Ministry of Urban Development, Government of India, has also recently issued the Model National Municipal Asset Valuation Methodology Manual (NMAVMM), as a further step towards implementation of Municipal accounting reforms, for guidance to Urban Local Bodies for valuation of their assets and preparation of general purpose financial statements.

- The Institute of Chartered Accountants of India in the year 2005 constituted a Committee on Accounting Standards for Local Bodies to formulate the Accounting Standards for such bodies. The Committee has been established with the primary responsibility to conceive and suggest areas in which Accounting Standards for Local Bodies (ASLBs) need to be developed, formulate ASLBs, integrate the ASLBs to the extent possible, with the International Public Sector Accounting Standards issued by the International Public Sector Accounting Standards Board, provide implementation guidance on ASLBs, review and revise the ASLBs, assist Local Bodies in adoption of accrual system of accounting, and propagate the ASLBs among the stakeholders in the preparation and presentation of financial statements. So far, the Committee has come out with four accounting standards namely ASLB 3 'Revenue from Exchange Transactions', ASLB 4, 'Borrowing Costs, ASLB 5,' Property, Plant & Equipment' and ASLB 6,' Events After the Reporting Date'. The Committee has also published a Booklet on 'Accrual Accounting for Local Bodies: Elected Representatives & Stakeholders' and organised an Awareness Workshop on 'Implementation of Accounting Reforms in Local Bodies: Current Scenario and a Way Forward' jointly with the Ministry of Urban Development, Government of India in January 2009 at Goa for the benefit of end users.
- The accounting reforms in sixty-three Municipal Corporations in India are progressing successfully under Jawaharlal Nehru National Urban Renewal

Mission and all the mission cities may completely shift to accrual accounting by the next financial year.

- The Ministry of Panchayati Raj has also initiated the process of accounting reforms in Panchayati Raj Institutions and formalize this process in all the States. For Panchayati Raj Institutions, C&AG have suggested an improved budget and accounting system on cash basis with some additional accrual disclosures. Twenty two States have already accepted the formats.
- Another reason for local bodies adopting accrual basis is that these bodies are also approaching capital markets for raising funds.

## Initiatives required to be taken by the Government

Keeping in view the urgency of migration to the accrual accounting reforms, the Central Government should take the initiative in respect of the following aspects for the Government Departments at the Central and the State level.

- Identification of Key Issues in Transition
- Amendments in Rules 1990, accounting codes and provisions of the Constitution of India dealing with the Government accounting
- Migration manual
- Training Manual
- Valuation manual
- Format of Financial Statements
- Re-orientation of existing cash based budgetary process

## Key Issues Involved in Transition

There is also the need to address various issues associated with the move to accrual accounting. These issues comprising of Accounting and implementation issues have been discussed here under:

### Accounting Issues:

**Asset Accounting:** Establishing a system of asset accounting, which is an essential requirement of the new system, is a great challenge. This involves clear identification and comprehensive listing of the physical and financial assets of Governments and also their appropriate classification and valuation. It requires determining the opening balance for proceeding further. Accounting is still in the evolving stage in respect of the following important and major assets of the Government:



Infrastructure Assets: The accounting and valuation issues on these assets with regard to the capitalization, categorization and valuation methodologies are the major concerns and need a special consideration by the Government. For example, the question as to whether the accounting treatment and valuation methodology with respect to land under roads and to those under structures should be different.

Defence Assets: There are divergent views on accounting treatment with respect the military assets in India. One view is that due to strategic reasons these assets should not be shown as fixed assets and expensed in the year of purchase itself. Another view is that these may be capitalized and depreciated as a single group but no details of individual items under this category should be disclosed in the financial statements of the Government. However, if they are to be treated as assets what life should they be given bearing in mind the rate of obsolescence of high technology assets is a crucial question. The development of valuation methodologies for specialized defence assets is a major issue and needs substantial efforts of valuation professionals.

Heritage Assets: There are differing views among the accountants across the globe as to the accounting treatment of heritage assets. Some view that these should be valued at nominal value while others are of the view that the heritage assets should be valued either on historic cost or fair value. Another issue which needs consideration is that of accounting treatment to given to the heritage assets used for operational purposes of the Government. Again, the life of assets needs to be determined if depreciation is to be calculated and charged on those assets which have been capitalized.

Natural resources such as mineral reserves and forests: Whether these assets are be considered for incorporation into the accounts of the Government is an important issue. Accounting practices and valuation principles need to be evolved if these assets are to be reflected in the Government accounts.

Liabilities: Under the existing system the accounting records do not show the complete liability position of the Government or of its various Departments. The information available in the accounting records is not complete and does not include off-budget borrowings. Keeping a track of liabilities is a major challenge.

Pension Liabilities: Pension liabilities with regard to defined benefit plans of the government need more consensus within the Central Government in view of the huge unfunded liability incurred till date by the Government. The financing strategies may have a bearing upon the accounting treatment of pension liability i.e. deferred liability or charged as expense in the year in which employee serves the Government.

Environmental protection: Many activities cause damage to the environment and have the effect of incurring potentially large and long term liabilities. Whether attempt should be made to estimate the cost of restoration of the damage caused to the environment and if so evolve the appropriate accounting norms to account for these costs.

Social policy obligations such as old age pensions and other welfare schemes of the Government: Social obligations at times may trigger liabilities upon Government and for which accounting issues need to be considered whether to bring these obligations into the accounts or ignore on the ground that the legislation affecting them can be changed and therefore the potential liabilities are not capable of measurement.

Reporting entity issues: There may be differing views of the criteria that should apply to determine reporting entity for consolidation purposes. Reporting entities need to be clearly defined which could be the drawing and disbursing office, sub-unit i.e. autonomous body, unit i.e. sub-ordinate office within Department, Department within Ministry, Ministry within Government etc. This issue needs thorough analysis by considering the International Public Sector Accounting Standards and Indian

government specific issues. Some may take the view that the entity decision should be based on the department's/agencies legal responsibilities; others would argue that it should be drawn more widely to reflect say de facto control. Other factors could be budgetary control and/or economic dependency. Determination of the boundary of reporting entity involves the review of existing reporting entities and identification of controlled entities.

Revenue arising from non-exchange transactions: Non exchange transactions are the major constituent of the Government transactions which arise generally from the sovereign power of the Government where Government has no obligation to provide services. The recognition of revenue from non- exchange transactions especially tax revenues i.e., income tax, excise and, sales tax may pose problem with regard to point of time when the Government may treat the tax revenue to have accrued. For example, income tax is deducted at source at the time of payment and advance tax is collected in instalments within the financial year, the return of income is filed by specified date and finalization of assessments span over at least another year. In this scenario, at what point of time, from the tax collection to financial year end to specified date of filing of return of income to finalization of assessment by the income tax department, the revenue to government could be treated to have accrued. Further, what should be the basis of measurement at the time of accrual? How should tax concessions be treated i.e. as a reduction of income or as an expense? What should be the treatment of estimated cost of tax evasion?

Public Private Partnerships: How are the assets, liabilities, income and expenditure arising under these arrangements to be treated? How critical to the decision is the shift of the risk from the public to the private sector and who retains the ultimate control? It is important to ensure that devices are not used to allow commitments to be moved 'off balance sheet' when the ultimate risk and control remains with the Government.

Other Issues:

Chart of Accounts: Another important issue relates to a new Chart of Accounts for the new system. Presently, our system of List of Major and Minor Heads is meant to reflect only cash based transactions. A new Chart of Accounts is needed to meet the requirements of classification of transactions in the new system both in terms of primary allocation like salaries, subsidies, wages, etc. and secondary allocation like Defence, Education, Health, etc.

New Accounting policies, Accounting Standards and principles: The new system would also require devising new accounting principles, policies and standards and formulating new accounting manuals.

Skills and Competence/ Technical Capacity: The new system would require suitably trained and skilled personnel, proper capacity-building and comprehensive training. As change in the basis of accounting requires action both in the Union and in the States, the problems faced in improving skills are complex. Lack of technical resources can be a major impediment to the successful implementation of accrual accounting.

Automated Information system: Although, in theory, cash or accrual accounting can be implemented with either a manual or an electronic system, in practice, it would be inadvisable for Government to attempt full accrual accounting without the aid of modern Government financial management information system (GFMIS) with proven functionality in areas such as general ledger, account payable, purchase asset management etc.

Proper Communication: The New Zealand experience has shown that initial communication with politicians overseeing the implementation of accrual accounting is crucial but it should not end there. Politician would change and new position holders will have to be convinced on an on going basis of the value of use to which accrual

based statements can be put. Thus a strong communication strategy is required initially and on an ongoing basis.

Presentation: Sometimes accrual information can be presented in a way that is difficult for non-accountants to understand. There would be need to focus on the key elements of accrual financial information by the production of summary information to make accrual information more accessible.

Potential Problems: Introduction of a new system of accounting in Government may give rise to the following problems:

- Degree of entrenchment of existing system  
Government systems have an extensive history behind it and these systems have become intrinsic parts of the work culture through institutionalization over generations of Government employees. Therefore, to change these systems will require a comprehensive attitudinal and cultural change which is not only very difficult but will also take a fairly long period to get fully institutionalized.
- Danger of Sacrificing the inherent robustness of the existing system  
The accounting manuals followed in the Government are extremely robust by themselves and internal controls as well as pre-audit, concurrent audit, and post-audit points are very well laid out. As the present system would run concurrently with pilot projects / conversion process, all such issues must be fully and comprehensively addressed.
- Use of the data arising from accrual accounting  
Unlike private sector, where assets and liabilities data are regularly used by financial managers to take decisions, in Government, the whole concept needs to be brought in even at the decision-making levels. This means that the MIS which form the basis of decision support systems, must also comprehensively

change, and the advantage rendered thereby to decision-making clearly brought out.

- Availability of required data / Information

The introduction of accrual accounting would involve gathering of information like details of assets, accruals and prepayments etc. which may not be available easily, as these do not form an important part of cash accounting system.

## Costs of Implementing Accrual Accounting

It is noted that accrual accounting is a tool and not an end in itself [Storm]. It is a tool for decision-makers that can help them to make better decisions and improve the allocation of scarce government resources. However, the benefits of this improved decision-making can be difficult to quantify. Change also involves a human cost. Some people will resist change because it involves an effort and may move them from the familiar to the unfamiliar. The providers of information and the managers and politicians that will use the information need to broaden their thinking if they are to benefit by the move from cash-based system to accrual-based system.

## Time frame and Broad Work Plan

The nature and speed of the transition to accrual accounting can be influenced by various factors like; system of government and the political environment of the country, current basis of accounting used by the country, the capability of existing information systems, the level of political commitment and the capacity and skills of the people and organizations responsible for implementing the change. Further, the period of transition can differ from country to country. It may be short term, medium term and long term. The long term period provide more time for the preparation of detailed implementation plans the developments of accounting policies and implementation and testing of new system and also provide a reasonably long time for the education of groups such as government employees and politicians regarding the change.

Time Frame as Suggested by GASAB\*: New Zealand, which had a unitary system of government, took 7 years for the transition. Since the India has a federal system of governance, it would take a lot of time to integrate different accounting practices of various states and municipalities. Such transition in India can take nearly 10 to 12 years, as recommended by DN Ghosh Committee being studied by the Government Accounting Standard Advisory Board (GASAB), given that different user departments are at different stages of preparedness.

Work Plan by GASAB\*: GASAB suggests that the user departments may like to use the following activities/ items of work, which constitute prerequisites of a road map for transition. These activities/ items of work cover the administrative, technical and capacity- building aspects. Detailed time frame and task schedule will need to be finalised by the user departments:

Setting up Task Force/ Cell: There is need for setting up of a Task Force/ Cell or designating a nodal agency preferably at Ministry of Finance, Govt. of India level for implementation and coordination. It may include representatives of CGA, C&AG, CGDA, Railways, Posts and State Governments. Setting up of such a Task Force will facilitate an integrated approach across Governments. It will provide a forum for evolving accounting policies and experience sharing and facilitating resolution of issues faced by different stakeholders. Since changes in the accounting system would necessarily involve modifications in the existing system of accounting, a Task Force needs to be set up in the concerned ministry/ department headed by the administrative Secretary being the Chief Accounting Authority and the State Governments.

Building adequate database essential for implementation of accrual accounting: This needs to be done by bringing in a broad spectrum of financial information, presently lying outside the reporting framework. These may include required information vis-à-vis data on physical and financial assets; liabilities including accrued liabilities and pension liabilities; information on salaries, subsidies,

---

\* Suggested by GASAB in Road map developed for the accounting reforms

committed and contingent liabilities, etc. A detailed review needs to be carried out to identify whether the data required for accrual accounting exists somewhere. Means need to be devised to bring such data into the reporting framework in a systematic and reliable fashion. For the data that is not held systematically either with the executive or in the present financial reporting system, modalities of its identification, capture and maintenance thereafter need to be worked out also. Building adequate database is a short to medium-term activity; however, some of the actions on this could be taken up straightaway.

Assets identification and creating Assets Registers for physical assets: Information of financial Assets in terms of loans, equity and investments by Governments are available. Information on physical assets and current assets need to be built up by creating an asset register. These involve (i) identification of assets, (ii) grouping them as per accepted classification like property, plant, equipment, infrastructure, block assets etc., (iii) valuation of assets for opening balance, (iv) identification of other financial assets, (v) inventory recording. This will be a short to medium-term activity.

Identification of liabilities: Information relating to long-term debt is available. This will require mapping the types of current liabilities, which persist in Government, and maintenance of Liability Register. Further, to assess pension liabilities actuarial valuation would be required. This should be a medium-term activity.

Pilot Study: Pilot studies would be required covering a few Ministries/ Depts. / State Governments with a view to assess the gaps and the problems in the existing system so that the transitional requirements could be worked out. This will be crucial for process mapping. Ministries which have dedicated accounts services such as Railways, Defence and Posts, may select areas within their jurisdictions for pilot study based on feasibility and their requirements. It is of crucial importance that the Pilot Studies be identified and carried out with the active involvement of the executive branch concerned. Any changes leading to introduction of accrual accounting would have very significant impact on the working of the executive and recording of financial transactions. For the Civil Ministries/ Departments



and the State Governments, it may be possible to select departments with an asset base such as Public Works and Irrigation and social orientation and large expenditure such as Health or Education. It is noted that the Controller General of Accounts and the Ministry of Railways have already taken concrete action in this regard. Conducting pilot study should be a short to medium-term activity.

Process mapping: Detailed process study is required of various activities and accounting practices to know the type and nature of accounting and financial information available and to assess the departure from the existing system in terms of principles and points of recognition, measurement, classification and disclosures. This will also involve listing the agencies and sources of information and mapping their inter-linkages. This should be a medium term activity.

Detailed framework of accounting: While GASAB will suggest a broad operational framework for consideration of the Government, each user department or stakeholder jurisdiction will be required to devise their detailed accounting system taking into account the broad contours of operational framework as accepted by the Government on suggestion of GASAB. While switching over to accrual accounting there may be a need for integrating the requirements of information stipulated in the FRBM rules for respective users. This could be done at the time of devising detailed accounting system by each user department. This should be a medium-term activity.

Laying down accounting policies: There is need to prepare a new Accounting Manual as a new policy document containing accounting policies to be followed in the new system. This could evolve over a period of time. There is also a need to clearly spell out principles and criteria of recognition, measurement and classification applicable in the accrual accounting system in the new Accounting Manual and also policy on depreciation of physical assets. These accounting policies will be based on accrual based public sector accounting standards pending formulation of GASAB's accounting standards. The draft policies should be discussed in the task forces working in the ministries/ departments headed by Chief Accounting Authority of the ministry/ departments and also in the task forces in the states. Preparation of the new Manual and laying down accounting policies could be a medium-term activity.

Preparing Chart of Accounts: The existing List of Major and Minor Heads (LMMHs) needs to be recast as Chart of Accounts, which will need to include Object heads of classification to depict accrual transactions. There is need for rationalization / standardisation of the Object Heads across the States and the Union as also recommended by the TFC. Presently, given the flexibility in the operation of object heads at the States level, there is no standardized list across the Union and the States. In the new system based on accrual concepts, preparation of Income and Expenditure Statement and Statement of Assets and Liabilities would require information on primary allocation basis, i.e., the object heads. It may be noted that Chart of Accounts should be comprehensive as far as possible and should be prepared after wide consultation and with a long-term perspective. It should take into account different dimensions of information vis-à-vis, functional, programme and object heads classification to take care of the desirable requirements of the stakeholders. This is important due to the fact that modifications or changes in the Chart of Accounts may not be feasible frequently. Preparation of the Chart of Accounts could be a medium-term activity.

Devising documentation/ subsidiary ledgers: Necessary documents/ ledgers and other subsidiary books will be required to be in place at the appropriate transaction points such as the PAOs/ Treasury /DDOs /CDOs as applicable, for capturing transactions at their point of origin. This will be a medium term activity.

Organizational arrangements for data / information flow: Making / streamlining arrangements for accounting data flow and defining role and relationships amongst various officials dealing with transactions and accounting will be required. It is also suggested that rationalization of the number of DDOs/ CDOs and limiting their number is an important consideration given the fact that information about payables and receivables (and also asset acquisition and discharges) is to be captured and got reflected in the primary accounting documents which Treasuries/ PAOs forward for further consolidation. This will be medium to long-term activity.

Decision on IT system: There is need to assess adequacy of the existing IT system to meet transition needs. It may be noted that the desired accounting reforms require a robust IT system to be in place. An IT system should be envisaged which enables entry of primary information from the basic accounting records at a single point and maintenance of an integrated database. A desirable IT system should ensure that after the initial entry further human intervention for data entry is not required. This will help maintenance of accurate, reliable, valid and integrated data and generation of accounting and financial information. Assessment of requirements and putting in place the IT system will be a medium-term activity.

Training needs: Assessment of training needs in terms of capacity- building for managing transition, implementation and management of accrual accounting system is required. This will require designing training plans/ programmes, training for implementation of the work plan etc. There may also be requirement of dedicated trained cadre of officials for managing issues of valuation of assets and other balance sheet items. This could be a short to medium term activity.

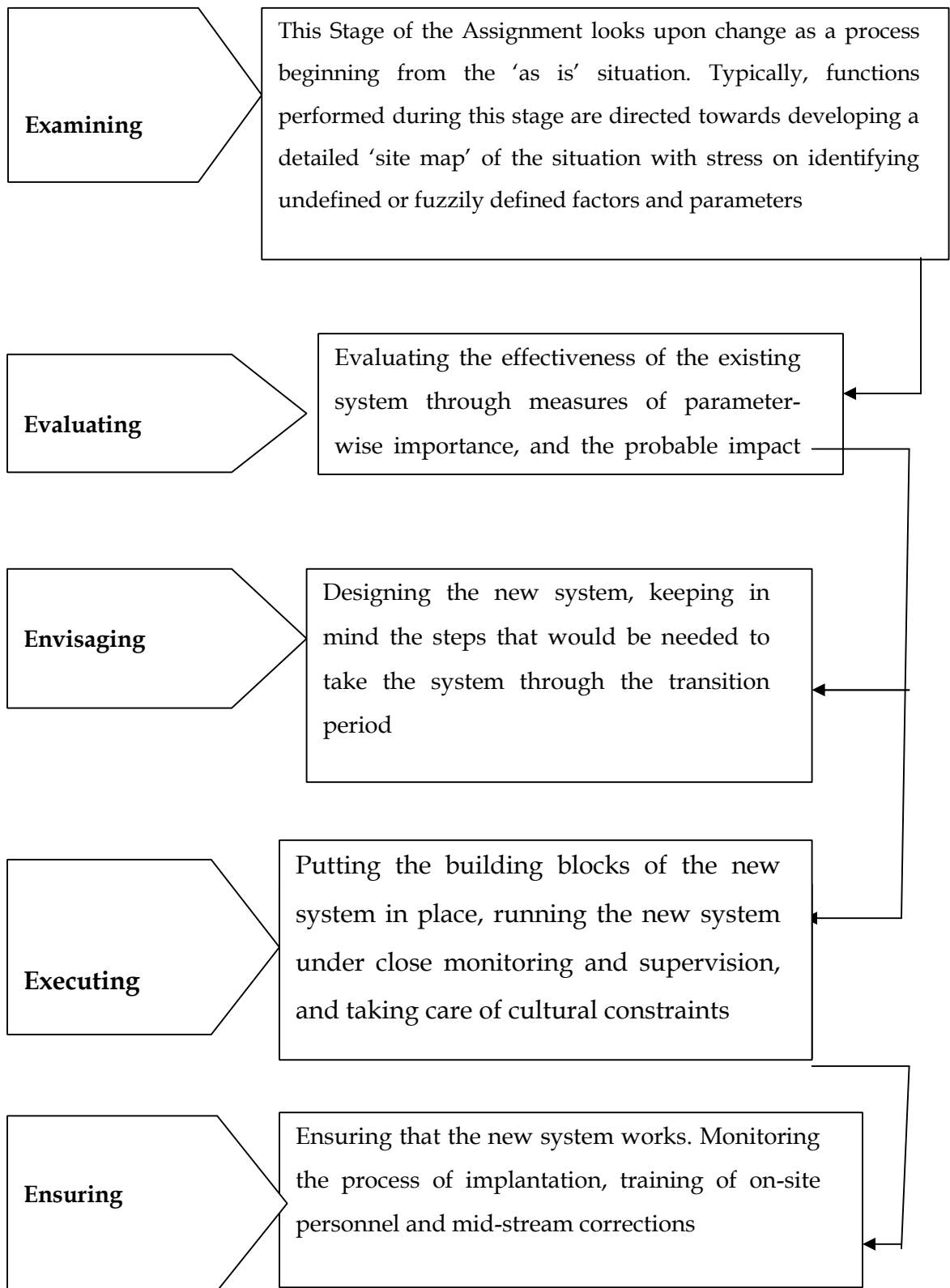
Implementation: Pilot Implementation of a designed system for a few depts. / States are required. This is for testing the system after it has been designed in all its aspects covering accounting framework, Chart of Accounts, asset classification, necessary documentation, etc. Pilot implementation is different from pilot study. While pilot study is for process mapping and knowing the requirements of transition, pilot implementation is for testing the readiness for full implementation. After taking pilot experiences into account and making necessary modifications, as may be required, full implementation in all user departments/ states may be taken up. At this stage, there may be requirement of parallel running of the new system along with the existing system before switchover to accrual accounting completely. This should be a long-term activity.

The total frame and work plan can be divided into various phases as discussed below:

- ✓ First Phase – During this phase, the group of facilitators and the change agents are to be identified, a detailed review of the existing situation, “As is” study is to be conducted, a clear programme of action is to be designed, the change agents implement the first steps connected with the introduction of the Accrual System (which may include introduced under the Accrual System, and assuring continuous assimilation of accurate accounting data within the accounting system. Necessary basic training programme can also be included in this phase.
  
- ✓ Second Phase– This phase concentrated primarily on taking the data from the ledgers to the Trial Balance stage and the understanding of the Government Department staff to basic data entry. This phase also includes re-structuring of Chart of Account, Preparation of Fixed Asset Register, devising new accounting policies and also conducting Training Programme as necessary.
  
- ✓ Third Phase– This phase covers the steps from the Trial Balance to the presentation/finalization of the financial statements and the institution of the necessary procedures and practices. This phase also includes the implementation of the FMIS fully and the development of the necessary guidance documents for the replication of the whole exercise. Training programme as necessary be included.

The following diagram depicts the various phases as discussed above :

## Suggested change-facilitation model



## Accounting Reforms: A Must

Among the numerous changes in Government accounting in recent years, the emergence of International Public Sector Accounting Standards (IPSASs) stands out as the most significant development (see Sutcliffe, 2003).

The initial set of IPSASs, unfortunately, has rather uncritically emulated the business accounting standards set by the International Accounting Standards Board's predecessor (Ghan, 2002). They are detailed technical provisions designed by accountants for accountants, not for public policy-makers whose support is critical for their successful implementation. Even so, IPSASs have some symbolic value. By basing the initial IPSASs on IASG standards, the IPSASs might benefit from the popular notion that business accounting (at least before the 2002 Enron/Arthur Andersen scandal) stood for financial discipline and integrity. Furthermore, the New Public Management literature has raised the expectations about the ability of accounting to make Government more efficient (see Olsen et al, 1998, for a review). IPSASs could raise the prestige of Government accountants, who are often regarded more as bureaucrats than credentialled professionals like certified/chartered accountants. IPSASs might facilitate the entry of private sector accountants and auditors into the public sector. Perhaps IPSASs might serve as a catalyst for including government accounting in the common body of knowledge expected of all accountants. Finally, the financial support of international organizations, such as the World Bank and the IMF, constitutes a favourable assessment of the expected contribution of IPSASs to Government financial accountability. However, it would be naive to exaggerate Governments' propensity to reform their accounting systems on the basis of IPSASs.

Each country's different methodology of adopting Government Accounting Standards will affect their likelihood of using IPSASs. (Countries using independent boards may find it easier to import IPSASs than those that legislate Government Accounting Standards. Unless there are scandals or financial crises linked to bad accounting or

reporting practices, changes would be slow and tardy. As Machiavelli (1513, quoted by Rogers, 1983) counselled his Prince: 'There is nothing more difficult to plan, more doubtful of success, nor more dangerous to manage than the creation of a new order of things'. Liider (1992) emphasized the uncertain prospect of adopting Government Accounting innovations and the necessity of overcoming numerous barriers. The support of the institutions that hold resources of value to Governments— international lenders, donors, bond-rating agencies—may prove to be indispensable.

## Rationale for a system of “Green Accounting” for India

India in the past decade has recorded a dynamic growth that was missing in the earlier quasi-socialist regime. The cumulative impact of the reform process appears to be generating growth. However, it is also desirable to monitor and channel the forces of growth and investment in order to ensure that they truly improve the quality of life for current and future generations. There is an asymmetry between man made and natural capital in that depreciation in the former is reflected in GDP accounts but not the latter. In this context, it should be recognized that GDP growth is too narrow a measure of economic growth and not a measure of national wealth, and this is why we propose a “Green Accounting” framework for the Centre, States, as well as Union Territories.

Key externalities in the form of creation and destruction of Human Capital and Natural Capital both need to be explicitly measured, because they have a significant impact on the long-term sustainability of India's growth.

## Role of ICAI and its members

In order to leverage the accounting reforms process, The Institute of Chartered Accountants of India felt the need to provide a broad framework for reforming the accounting systems so as to provide the guidance for switching to double-entry accrual system in public sector. In this direction, the ICAI in the year 2005 constituted Committee on Accounting Standards for Local Bodies to formulate the accounting standards for local bodies.

In 2008, the ICAI constituted the Committee on Public Finance for the first time to use the professional excellence in the area of Public Finance. The principal objectives of the Committee, inter alia includes to review, analyze, recommend measures and assist the Central and State Governments as also Civic Bodies. Also in the same year, Committee on Government Accounting was constituted with the mission to review, suggest improvements and provide awareness on Government Accounting to the society at large and specifically to the stakeholders.

In 2010 the erstwhile Committee on Public Finance and Committee on Government Accounting were merged to jointly focus on the Accounting Reforms required at all levels of Government machinery.

The pace of accounting reforms has direct impact on the accounting profession and thus the role of chartered accountants in helping the Government in realising many of the objectives which are the need of the hour, prime amongst them being financial discipline, smooth fiscal administration, augmentation of revenue, reduction of potentially litigative situations, establishment of a culture of accountability and ushering in definitive systems of transparency and disclosure about the deficiencies in the existing system of the government accounting is imperative.



The role which the members of ICAI can play in the successful implementation of the Government Accounting Reforms are discussed as under :-

#### Conversion of Accounts to Accrual Based Double Entry Accounting System

- Assessment of existing system and requirements including review of legislative framework with reference to existing laws for smooth transitions into Double Entry Accounting System.
- Review of existing State Accounts Manual.
- Business process re-engineering with reference to Accrual system of Accounting.
- Categorisation, grouping and sub-grouping of assets and liabilities.
- Design of Chart of Accounts with Accounting Codes.
- Determination and valuation of fixed assets including infrastructure assets, current assets, investments, long-term liabilities, current liabilities and net worth as on opening balance sheet date.
- Preparing formats of financial statements and voucher format in the Accrual system.
- Preparation of opening balance sheet.
- Selection of appropriate accounting policies and drafting of disclosures of accounting policies.
- Implementation of Double Entry Accounting System on accrual basis.
- Preparation of financial statements for the transition period.
- Training of finance and accounts personnel and training of trainers.

#### Management Consultancy Services

- Providing assistance as domain expert to the agencies designated by the Government for computerization of records and computerization of Accounting System.

- Consultant in e-governance; implementation of IT based Management Information System and enterprises resource planning style system implementation.
- IT reforms including computerised accounting system introduction and implementation.
- Consultancy in drawing up reforms roadmap, timelines and implementation targets.
- Assisting in change management.
- Design and implementation of Budgetary Control System (Accrual based Budget) in the line with the Accrual Accounting System and linkage among Budgetary System and Financial Management Information System and Decision making system.
- Revenue system assessment and financial analysis of revenue and expenditure exploring potential for raising debt capital for projects, assessing financial viability of investment plans, preparation of financial projections and revenue mobilisation plans, undertaking detailed revenue potential assessments, cost determination, control and reduction analysis, facilitating public private partnership in new the projects and assist in bid process management, negotiations etc.

#### Capacity building to support initiatives for accounting reforms

Chartered Accountants can also support in the capacity building initiatives for accounting reforms by providing formal training which should ideally become an organic part of the whole implementation exercise to strengthen the financial management and control of the organization. Some of the practices which could be followed in this regard are :-

- ❖ Opinion-building exercise: This should be carried out at all levels to create a perceived need for ownership of such reforms

- ❖ SWOT analysis: This is useful starting point for identifying the nature and scope of reforms required within the organization as a whole. A SWOT exercise (identifying strengths, weaknesses, opportunities and threats) should be undertaken for financial and clerical staff in a participative manner before embarking on accounting reforms.
- ❖ Process mapping: Accounting reforms should start with process mapping, followed by the streamlining of the existing accounting system with the present accounting staff. This exercise will assist staff to identify the main weaknesses and limitation with the present system.
- ❖ On-the-job-training: Training programmes should be an integral part of accounting reforms and based on practical issues concerning the design and implementation of the specific system in hand. Care should be taken to avoid general theoretical training removed from the implementation process.

## CONCLUSION

The general conclusion of this paper is that accounting reforms in public sector is must as the need of enforcing transparency and accountability has lead to redefining role of public sector itself. The definition of this role not only involves political and technical dimensions but also draw attention to the varied paths through which these reforms might be revised, tailored to countries' specific institutions and politics. Clearer mandates and policies, organizational strategic orientations, better allocation of resources, more capacity building and data and information on actual performance can alter the climate of technical and political publics and public opinion encouraging institutional changes.

Apart from this the transition to accrual accounting is a major project for most governments that requires careful planning and management.

What is important for the professionals to consider is that there would be numerous challenges in the process of transition which are discussed earlier, inspite of the best planning. To phase these challenges a variety of skills are required to manage and maintain a change to the accrual basis of accounting. Identification of the types of skills required and planning to ensure the availability of those skills is critical to the success of the transition.

Mr. Warren Ruppel, Comptroller of the New York City Government, one of the largest in the world, recommends the following for professionals/accountants:

- Keep methodologies simple-they will need to be done every year.
- Make decisions-avoid paralysis by analysis
- To the extent possible, keep independent auditors informed of what is being done
- Hold weekly status meeting with staff assigned to the implementation effort
- Keep track of every issue that requires follow-up, and resolve them promptly
- Make sure the organization group has a 'can do' attitude

To sum up, institutional reforms are the result of the mobilization of social, political and technical resources. It is not a one shot operation, but a continuous process. The accounting reform in public sector is a strategic target to start processes of institutional reforms which could be achieved firstly through co-herence with the overall institutional framework and the regulators who would bring in and train the existing personnel to face the changes in the present system. Secondly, by leaving behind the old dichotomy between various governments' machineries and making use of the diverse possibilities of joint action, partnerships with the private sector and social organizations is required.

## BIBLIOGRAPHY

- Glautier, M W E and Undertow, B., Accounting Theory and Practice, Prentice Hall (2001).
- Shame, Roger Hussey, "Shame About Standards, "Accountancy International, (August, 1999).
- Chowdhury, A. K. (2000). Compliance with accounting standards in India, why and how? Management accountant, ICWAI, March.
- Hati, W. J. and Rakshit, D. (2002). Integrating accounting standards — A step towards harmonization. Management accountant, ICWAI, May.
- Madan V. (2002). Re-Statement under US GAAP. India Infoline Newsletter, IMT Ghaziabad.
- Memani, R. (2006). Accounting a Milestone for Global Markets. The Financial Express, July 27.
- Reddy, K. R. (2000). Accounting standards and Gaps in Practices in India. Management Accountant, ICWAI, April.
- Samir, M. S. (2003). Harmonisation of Accounting Standards. Chartered Accountant, ICAI, January.
- Allen, R. and Tommasi, D. (2001), Managing Public Expenditure: A Reference Book for Transition Countries, OECD, Paris.
- Bourmistrov, A. and Mellempvik, F. (2000) «Russian Local Government Accounting: New Norms and New Problems», in Caperchione E. and Mussari, R. eds., Comparative Issues in Local Government Accounting, Kluwer Academic Publishers, Boston, pp. 159, 174.
- International Comparative Issues in Government Accounting, Kluwer Academic Publishers, Dordrecht, The Netherlands, pp. 91-122.
- Chan, J.L., Jones, R.H. and Lüder, K.G. (1996), «Modeling Government Innovations: An Assessment and Future Research Directions», Research in Governmental and Nonprofit Accounting, Vol. 9, pp. 1-19.

- Chan, J.L. (2000), «A Sino-American Comparison of Budget and Accounting Coverage», in Caperchione, E. and Mussari, R., eds., *Comparative Issues in Local Government Accounting*, Kluwer Academic Publishers, Boston, pp. 11-34.
- Chan, J.L., Cong, S.H. and Zhao, J.Y. (2001), «The Effects of Reform on China's Public budgeting and Accounting System», in Bac, A., ed. *International Comparative Issues in Government Accounting*, Kluwer Academic Publishers, Dordrecht, The Netherlands, pp. 297-314.
- Chu, K-Y, and Hemming, R. (1991), «Public Expenditure Handbook: A Guide to Public Policy Issues in Developing Countries», International Monetary Fund, Washington, D.C.
- Coombs, Hugh M. and Mohamad Tayib, (2000), «Financial Reporting Practice: A Comparative Study of Local Authority Financial Reports Between the UK and Malaysia», in Caperchione, E. and Mussari, M. eds., *Comparative Issues in Local Government Accounting*, Kluwer Academic Publishers, Boston,, pp. 53-68. Schiavo-Campo, S. and Tommasi, D. (1999), *Managing Government Expenditure*, Asian Development Bank, Manila.
- Simon, H.A. (1954), *Centralization vs. Decentralization in Organizing the Controller's Department*, Controllership Foundation, New York.
- Sutcliffe, P. (2003), «The Standards Programme of IFAC's Public Sector Committee,» *Public Money and Management*, January, pp. 11-12.
- World Bank (1998), *Public Expenditure Management Handbook*, World Bank, Washington, D.C.
- American Institute of Certified Public Accountants, *Statement on Auditing Standards No. 78, Consideration of Internal Control in a Financial Statement Audit: An Amendment to Statement on Auditing Standards No. 55.*
- Association of School Business Officials International, *GASB Statement No. 34: Implementation Recommendations for School Districts*. Reston, VA: Association of School Business Officials International (2000).

- Deloitte and Touche (2001). Twelve White Papers on Issues in Education Finance. Unpublished manuscript.
- Everett, R.E., Lows, R.L., and Johnson, D.R. (1996). Financial and Managerial Accounting for School Administrators. Reston, VA: Association of School Business Officials International.
- Gauthier, Stephen J. (2001). Governmental Accounting, Authority and Financial Reporting. Government Finance Officers Association, ISBN 0-89125-219-3.
- Deutsch, K.W. (1966), The Nerves of Government: Models of Political Communication and Control, The Free Press, New York.
- Godfrey, A.D., Devlin, P.J. and Merrouche, C., (1996), «Governmental Accounting in Kenya, Tanzania and Uganda» in Chan, J.L., ed., Research in Governmental and Nonprofit Accounting, Vol. 9, JAI Press, Greenwich, Connecticut, pp. 193-208.
- Godfrey, A.D., Merrouche, C. and Devlin, P.J. (1999), «A Comparative Analysis of the Evolution of Local Governmental Accounting in Algeria and Morocco,» in Copley,
- P.A. and Sanders, G.D., eds. Research in Governmental and Nonprofit Accounting, Vol. 10, JAI Press, Greenwich, Connecticut, pp. 201-234.
- Grindle, Merilee S. (2000), «Ready or Not: The Developing World and Globalization,» in Nye, J.S. and Donahue, J.D., eds. Governance in a Globalizing World, Brookings Institution Press, Washington, D.C., pp. 178-207.
- Hopwood, A. and Miller, P., eds. (1994), Accounting as a Social and Organizational Practice, Cambridge University Press, Cambridge.
- International Federation of Accountants (IFAC) (1996), «Responding to an Increasing Demand for Accountability in the Public Sector,» IFAC Quarterly, October.
- IFAC (2003), Handbook on International Public Sector Accounting Standards. IFAC, New York.

- IFAC, International Public Sector Accounting Standards Board (2005), Exposure Draft 24, Financial Reporting Under the Cash Basis of Accounting - Disclosure Requirements for Recipients of External Assistance, IFAC, New York.
- IFAC, International Public Sector Accounting Standards Board (2005), «Background and Update,» unpublished paper, March.
- IFAC, Public Sector Committee (2000), Study 11, Government Financial Reporting: Accounting Issues and Practices. IFAC, New York, May.
- Jaruga, A. (1988), «Governmental Accounting, Auditing and Financial Reporting in East European Countries,» in Chan, J.L. and Jones, R.H. eds., Governmental Accounting and Auditing: International Comparisons, Routledge, London, pp. 105-121.
- Keefer, P. and Khemani, S. (2004), «Democracy, Public Expenditure and the Poor,» World Bank Research Observer. World Bank, Washington, D.C.
- Nowak, W.A. and Bakalarska, B. (2001), «Polish Public Sector Accounting in Transition: The Landscape after 1999 Step in the State Redefining,» in Bac, A. ed., International Comparative Issues in Government Accounting, Kluwer Academic Publishers, Dordrecht, The Netherlands, pp. 265-278.
- Ouda, Hassan A.G. (2001), «Central Governmental Accounting of Egypt and the Netherlands: Similarities and Differences,» in Bac, A. ed., International Comparative Issues in Government Accounting, Kluwer Academic Publishers, Dordrecht, The Netherlands, pp. 71-90.
- Rose-Ackerman, S. (1999), Corruption and Government: Causes, Consequences and Reform, Cambridge University Press, Cambridge. Reuters (2003), «World Bank urges crackdown on government corruption», December 10. Sachs, J.D. (2005), The End of Poverty: Economic Possibilities for Our Time, Penguin Books, New York.
- Governmental Accounting Standards Board. (2002). Codification of Governmental Accounting and Financial Reporting Standards (Statement 34 Edition), as of June 30, 2002. Norwalk, CT.



- Governmental Accounting Standards Board. (2001). Guide to Implementation of GASB Statement 34 and Related Pronouncements: Questions and Answers. Norwalk, CT.
- Governmental Accounting Standards Board. (2000). Guide to Implementation of GASB Statement 34 on Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments: Questions and Answers. Norwalk, CT.
- Governmental Accounting Standards Board. (1999). Statement No. 34, Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments. Norwalk, CT.
- Miller, L. and McClure, M. (Year unknown). "Reliable School Budget Forecasts: Seven Tools That Work." School Business Affairs, (Vol. and No. unknown).
- Osborne, D., and Gaebler, T. (1993). Reinventing Government. How the Entrepreneurial Spirit Is Transforming the Public Sector. New York: Plume.
- Renzulli, J.S. and Reis, S.M. (1997). The Schoolwide Enrichment Model (2nd ed.). Mansfield Center, CT: Creative Learning Press.
- Reschovsky, A. and Imazeki, J. (1997). "The Development of School Finance Formulas to Guarantee the Provision of Adequate Education to Low-Income Students." In W.J. Fowler, Jr. (Ed.), Developments in School Finance, 1997 (NCES 98-212). U.S. Department of Education, National Center for Education Statistics. Washington, DC: U.S. Government Printing Office.
- U.S. Department of Education, Institute of Education Sciences. (1990). Financial Accounting for Local and State School Systems. Washington, DC: National Center for Education Statistics.

## THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

The Institute of Chartered Accountants of India (ICAI) is a statutory body established by the Chartered Accountants Act, 1949 for the regulation of the profession of Chartered Accountants in India. During its more than six decades of existence, ICAI has achieved recognition as a premier accounting body not only in the country but also globally, for maintaining highest standards in technical , ethical areas and for sustaining stringent examination and education standards . ICAI is now the second largest accounting body in the world.

ICAI has its Headquarters at New Delhi with 5 Regional Offices at Mumbai, Chennai, Kanpur, Kolkata, New Delhi .It presently has 125 branches spread all over the country. In addition, it has also set up 21 chapters outside India and an overseas office in Dubai.

Currently, over 6, 50,000 students are pursuing the Chartered Accountancy course and the total membership of ICAI is about 1, 61,000. Out of the total members, nearly 55% are in Practice and the rest are in employment. Among the members in Government, Judiciary, industry, banks, financial institutions, private enterprises etc, a significant number of members had occupied/occupy eminent positions in their respective organizations such as Chairperson of regulatory body, Chairperson of banks and insurance companies, Chairperson & Managing Directors of reputed enterprises, Executive Directors of various enterprises/organizations. Chartered Accountants are also serving as Vice-Presidents and Members of Income Tax Appellate Tribunals besides being in IAS, IPS and IRS cadres. The members of ICAI are getting recognition in foreign countries as well. It is evident from the positions they are occupying in all big companies across the World. Presently, there are about 12,000 members working abroad and occupying key positions.

ICAI is working on emerging paradigm and imperatives of a New Trade Order. Besides working in the core domain of Financial Reporting, Accounting, Standard Setting, Auditing, Corporate Governance, Fiscal Policies and alike; it is also focusing on Public

Finance, Government Accounting, Accounting Standards for Local Bodies and thus striving to create resources/outcomes of utility to society at large.

ICAI is one of the unique organizations with its activities encompassing education, training, examination, disciplinary mechanism, peer review, continuing professional development, government accounting, standard setting and alike. Its contribution to the work programmes of Government and other regulators has seen it being an important constituent of their select Committees. ICAI is truly a partner in Nation Building.

## ICAI-PARTNER IN NATION BUILDING

ICAI, as a part of its role in aiding pro-active process towards better governance is called upon to interact with various regulatory/statutory authorities in India on issues of interest touching upon the profession and otherwise.

The Institute, on its part, is putting the vast experience of its structure and its members at the disposal of those entrusted with governance. In this process, the Institute, at regular intervals, provides technical advise and necessary inputs to:

- Comptroller and Auditor General of India- Technical advise in response to references received including maintenance of audit panels, issues arising out of audit and accounts of government companies and public sector undertakings. Besides, ICAI contributes by being part of C&AG initiative to bring reforms in Government Accounting.
- Ministry of Corporate Affairs- Inputs in regard to matters relating to corporate laws and responds to technical issues, by way of offering comments/views/suggestions etc., on receipt of relevant references. ICAI is actively contributing in Company Law Reforms, Limited Liability Partnership legislation and e-governance initiative MCA 21.
- Reserve Bank of India- Technical advice and maintains constant touch in regard to matters pertaining to bank audits and audit of non-banking financial companies etc.
- Securities and Exchange Board of India- Maintaining constant touch and offers views/suggestions and also hold discussions in all matters touching upon the profession of Chartered Accountants. ICAI has been bringing out publications on Capital Market Regulations and Clause 49 of Listing Agreement.
- Central Board of Direct Taxes- Actively associating in the process of formulation of budget by offering pre-budget and post-budget suggestions/comments. Actively involved in offering suggestions to simplify

tax laws and their administration for the purpose of making it more responsive to tax payers.

- Insurance Regulatory & Development Authority- Helping the authority in redesigning the format of accounts of insurance companies both in the life and non-life sectors and provides necessary inputs in response to references received.

Following the initiative taken by the Institute, more departments of the Central and State Governments of the country are approaching ICAI for utilizing the services of Chartered Accountants for advice on economy in expenditure, development of control mechanism over public funds etc.

In addition, ICAI also provides necessary inputs, from time to time, to the Trade Policy Division, Ministry of Commerce, Govt. of India so as to enable the Indian Government to take part in a more effective manner in negotiations under GATS/WTO.

## Committee on Public Finance & Government Accounting:

### WE CARE FOR THE FISCAL HEALTH OF THE NATION!

In terms of authority given to the President by the Council at its 293rd Meeting held on 12th February 2010, the President has constituted a new Committee in the name of Committee on Public Finance and Government Accounting for the year 2010-11 by merging previously formed Committee on Public Finance and Committee on Government Accounting.

The principal objectives of the Committee on Public Finance and Government Accounting are:

- To review, analyze, recommend and suggest measures to the Local, State & Central Government, PSUs and other organizations in Policy assessment, planning and execution in public finance, Reforms in Government accounting system and Maximizing public fund's utility to augment and vitalize economic growth for end beneficiaries.
- To provide training within the Government bodies, to evolve methods which would enable in use of present day Information technology in assisting the accounting reform process, Collaboration and coordination with Comptroller & Auditor General of India (CAG) and Controller General of Accounts (CGA) to bring improvements in the framework of Government Accounting System.
- To suggest to the Central and State Government the means and ways which would assist in widening the tax base & in better administration of the revenue collection, improve MIS, budgetary control mechanisms, and enhance accountability and transparency.
- Committee also strives to undertake capacity building measures for the profession to enable the profession to assist the Government in the process of implementation of Government Accounting and Public Finance reforms.

The Institute of Chartered Accountants of India  
(Set up by an Act of Parliament)  
New Delhi

**Committee on Public Finance & Government Accounting**

ICAI Bhawan, A-29, Sector 62, Administrative Wing (III Floor), Noida-201309

[www.icai.org](http://www.icai.org)