A Compilation and Certification Program for Developing Countries

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The International Consortium on Governmental Financial Management (ICGFM) has introduced a Compilation and Certification Program for Developing Countries that are in the process of implementing the International Public Sector Accounting Standards (IPSAS). This Program is comprised of the following components:

1. IPSAS Compilation Guide for Developing Countries
2. Roadmap to Implement the IPSAS Compilation Guide
3. Certificate of Conformance for Implementing Pertinent Stages of the Compilation Guide

Each of these components will be explained in this article. This Program is presently being field tested in select countries. The draft documents being field tested are available at the ICGFM website (www.icgfm.org). If your country would like to participate in this field test, please send an email to the ICGFM website.

IPSAS COMPILATION GUIDE FOR DEVELOPING COUNTRIES

The Compilation Guide (the "Guide") supplements the International Public Sector Accounting Standards to assist developing countries in their implementation of IPSAS. Consequently, some IPSAS requirements (e.g., reporting fixed assets) are not included in the earlier stages of implementation. On the other hand, some financial information (e.g., attaching the auditor's opinion to the financial statements) is recommended even though an IPSAS has not yet been issued to address this area of concern.

This development program acknowledges that different jurisdictions may have different starting points and each country's program should be tailored to jurisdictional circumstances. In some cases the General Government Sector (GGS) and some controlled entities that are included in the GGS are already adopting a modified accrual basis (albeit modifications may vary from jurisdiction to jurisdiction). Some Government Business Enterprises (GBEs) and certain statutory authorities are already adopting an accrual basis. While a series of steps with particular time frames are presented in the Guide, this is a generalised first principles model that identifies key components. The application of this program needs to be assessed by reference to (and may need to be amended to respond to) the circumstances of each jurisdiction. Such matters as the entry point to the program, time for each stage, and sequence of some items may vary depending on those jurisdictional circumstances.

Introduction

Accounting Standards for Developing Countries

Timely, clear and open annual financial statements play a significant role in the accountability of governments to their citizens and their elected representatives. These financial statements are prepared on a cash basis or some variation of an accrual basis of accounting. However, most of these financial statements are not prepared on a consistent or comparable basis in developing countries. The benefits of achieving consistent and comparable financial information across

[2] Anthony Bennett, Michael Parry, and Andy Wynne assisted in the development of this program.

jurisdictions are very important and a set of IPSAS[3] have been established by the IPSAS Board (IPSASB) to assist in that endeavour. The IPSASB has also provided Study 14 to assist in the transition to the accrual basis of accounting.[4] Yet many developing countries have had difficulties in fully realizing these benefits due to lack of capacity, inadequate accounting procedures, or weak accounting systems. Many articles have been published in the International Journal on Government Financial Management (IJGFM)[5] to assist these countries as they attempt to implement the IPSAS. It is hoped the Guide will serve as another avenue to enable realization of these benefits.

The adoption of the Guide by developing governments will improve both the quality and comparability of financial information reported by their government entities for external users. For fiscal management, good cash accounting and forecasting procedures are essential. Initially, there are two basic elements of information that are needed for any governmental entity to manage effectively and efficiently in the short term:

(a) Is there enough cash to pay the bills when they come due?
(b) Is the budget properly prepared in order to maintain fiscal discipline within the governmental entity?

Over time, the need to expand the accounting systems beyond the two basic elements of information is recognized so that fiscal sustainability is maintained and fiscal crises are avoided. To achieve this objective, full accrual accounting is needed to identify the full costs of services provided. **Thus, taxpayers are able to pay for the services they receive at the time of their receipt rather than passing those costs on to future generations.** Accrual accounting provides a comprehensive and integrated accounting system that enables transparent reporting and enhanced fiduciary risk management. Governments and national standard setters have the right to establish guidelines and accounting standards for financial reporting to provide the information needed to make financial decisions necessary to maintain fiscal sustainability.

The Guide is based on the move toward good practices in public financial management (PFM) among developing countries around the world. The Guide builds on the structure of the current Cash Basis IPSAS[6] that was initially published in 2003. It is hoped that the Guide will be used to influence accepted good practices across the globe and act as a stepping stone for the possible implementation of the accrual IPSAS. Thus, adoption of the Guide will be an important step forward to improve the consistency and comparability of financial reporting by governments throughout the world.

Public Sector Accountability and the Role of Financial Statements

Along with the auditor's report, a government's annual financial statements provide the essential financial data necessary for accountability purposes and enable citizens and their representatives to make informed decisions about their government. In a parliamentary democracy, the legislative body sets the annual budget and so authorises the government to set

[3] In addition to the accrual IPSASs, a Cash Basis IPSAS has been issued to assist those countries not yet ready to implement the accrual IPSAS. The IPSAS can be downloaded free at www.ipsas.org.

[4] Study 14, *Transition to the Accrual Basis of Accounting: Guide for Governments and Government Entities*, International Federation of Accountants (New York).

[5] In particular, note articles by Hughes, Ouda, Parry, Sutcliffe and Wynne in the International Journal of Government Financial Management (or the Public Fund Digest that preceded the IJGFM) at www.icgfm.org.

[6] *Financial Reporting Under the Cash Basis of Accounting*, International Federation of Accountants (IFAC), New York, 2008.

tax rates, to borrow, and to spend money as indicated. For governments, a budget takes on a special legal significance. Governmental budgets are expressions of public policy priorities and legally authorise the purposes for which public resources may be raised and spent. The publication of government budgets and then the reporting of actual results in annual financial statements and other formats are the primary methods by which citizens and their elected representatives hold governments to account for their financial management. The annual financial statements are the key way in which the government accounts to the legislative body and its citizens for the taxes raised, loans contracted, grants received and money spent on the provision of public services.

A government's financial statements (and associated report of the Supreme Audit Institution) indicate how its management of financial resources complied with the annual budget authorised by the legislative body and with relevant laws and financial regulations. Citizens and their elected representatives have the right to know whether the government actually used funds and resources in accordance with the approved budget and relevant financial regulations. Demonstrating accountability for compliance with budgetary authority is a distinguishing objective of governmental financial reporting. The aim is to facilitate control by the legislative body to ensure that all public expenditure is within the limits set by the legislative body.

For governments that are dependent on donors for a significant proportion of their revenue, their annual financial statements are also a key document to enable the donor community to monitor adherence to agreed policies. These may include, for example, poverty reduction strategies as well as the proportion of government funds to be allocated and actually spent on defined pro-poor activities (for example, primary healthcare and education spending).

Because revenues raised through governments' power to tax are expected to be used to advance the public interest, the public is entitled to hold governments to a standard of financial accountability that is wider in scope than for private sector companies. Accountability to the legislative body is the cornerstone of all financial reporting in a representative democracy. Government accountability is based on the belief that citizens and their legislative body have a "right to know" which leads to a right to openly receive financial information that may lead to public debate by the citizens and their elected representatives.

Many of the key users of government financial statements (citizens and their political representatives) do not have a strong foundation in reading financial statements and so extra effort is needed to make sure the financial statements are accessible, clear and understandable.

Current Good Practices

A variety of approaches are currently used by governments and these approaches have yet to be comprehensively documented with the good practices identified. In 2006, the East and Southern African Association of Accountants General (ESAAG) supported a study resulting in a *Financial Reporting Survey and Database*.[7] This was based on broad assessments against the following indicative criteria:

- stakeholder support
- legislative framework underpinning financial reporting
- financial reporting
- credibility of financial statements.

[7] Anthony M Hegarty. *A Review of Existing Government Accounting Standards and Practices in the East and Southern African Region for the East and Southern African Association of Accountants General (ESAAG)*: Final Report. (Botswana, December 1996).

The Guide complements the above ESAAG study and builds on the seminal work performed by Andy Wynne.[8] It also builds on a research report by the African Capacity Building Foundation. The research included a review of the annual financial statements of a dozen sub-Saharan African governments and collated existing good practice. These countries included eight ESAAG member countries (Botswana, Kenya**,** Mauritius, Namibia, Rwanda, South Africa, Tanzania and Uganda) and four other sub-Saharan African countries (Burkina Faso, Ghana, Nigeria and Sierra Leone).[9] Another report to assist various countries in their transition from cash to accrual accounting has been published by The Chartered Institute of Public Finance & Accountancy (CIPFA).[10]

Qualitative Characteristics of Financial Reporting[11]

The following key qualitative characteristics of public sector financial reporting have been identified by the IPSASB:

- **understandability** – are the financial statements clear and are the key aspects and terms explained?
- **relevance** – can the information be used to assist in evaluating past, present or current events? In order to be relevant, information must also be timely.
- **reliability** – is the information free from material error and bias?
- **comparability –** can the information be used to identify similarities and differences between that information and information in other reports?

The Guide identifies good practices in terms of achieving each of these four qualitative characteristics of public sector financial reporting.

Benefits

The Guide should improve the capacity of governments to provide the legislative bodies, citizens, media and other stakeholders with understandable, relevant, reliable, and comparable financial statements. This will improve the quality of financial accountability and governance in the countries adopting the Guide. As a result, public spending should be more effective and focused on key areas of poverty reduction, democracy and development. Up-front development of the harmonised accounting policy is a key step in strengthening the budget execution process and improving the quality of financial reporting.

The Guide outlines the form and content of comprehensive and clear financial statements. It incorporates the cash information provided by the Treasury Single Account and is based on good practices being developed in some countries, especially in the areas of cash and debt management; it is to be practical and attainable. In addition, this approach should encourage peer review, learning and co-operation as the relevant professionals mutually learn, share and build on each other's good practice.

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[8] Andy Wynne, *Guide on Government Annual Financial Reporting on the Modified accrual Basis for Countries of sub-Saharan Africa, (*www.scribd.com/doc/94001463*).*

[9] Stephen Emau, Mercy Nyangulu and Andy Wynne, *Annual Financial Reporting by Governments – existing and practices in sub-Saharan Africa,* African Capacity Building Foundation. (Harare, 2012) www.scribd.com/doc/111894079.

[10] CIPFA, *stepping stones on the transition from cash to accrual accounting*, (London, March 2011).

[11] *Appendix B, IPSAS 1, Presentation of Financial Statements*, International Public Sector Accounting Standards Board (New York, December 2006).

The Guide, when adopted by governments, will increase the level of accountability of these governments to their citizens. It will also increase the level of comparability of financial statements between governments and so facilitate international comparisons.

Developing the Accounting System

"The government's accounting system lies at the foundation of a FMIS and should meet certain recognized standards. While it is important that the system should be able to record more than just cash transactions, this does not imply a move to a full accrual basis of accounting, which involves considerable costs in its introduction and maintenance. Rather, the output of the accounting system should match the information requirements demanded by the PFM system's stage of development. Accordingly, a development path for the accounting system can be described as a progressive movement to full accruals: first getting cash accounting to work well; progressively integrating operating accounts and financial asset and liability accounts (to move to modified accruals); introducing more elements of accrual recording; and finally recognizing nonfinancial assets (final stage for accrual accounting). A further stage of development, to move to accrual accounting and budgeting (currently attempted by only a very few countries), is perhaps best pursued after operating full accrual accounting for a period of time. The intermediate accrual stage (modified accruals) should be regarded as a reasonable target for low income countries, and would allow them to satisfy international reporting requirements. In this regard, IPSAS Cash and GFSM 2001 standards, met at least at the central government level, are the most relevant. The production of financial reports compliant with these international standards should be considered a benchmark output for a successfully functioning FMIS and a requirement for moving to further reforms beyond the "core".[12]

Government Finance Statistics

In order to collect comparable government finance statistics, the International Monetary Fund (IMF) issued the Government Finance Statistics Manual (GFSM 2001) to implement the System of National Accounts promulgated by the United Nations in 1993. "Although the GFS system is described in standard accounting terms, it is important to remember that it is a statistical reporting system that might differ in important ways from the underlying financial accounting system from which most of the GFS will be derived."[13] The GFSM requires the data to be collected on the accrual basis of accounting and to be reported in the following financial statements:

- Balance Sheet
- Statement of Government Operations
- Statement of Sources and Uses of Cash
- Statement of Other Economic Flows

Since many countries were not on the accrual basis of accounting, IMF issued a compilation guide for developing countries to assist these countries in transitioning from the prior requirement for cash reporting[14] to the current requirement to report on the accrual basis of

[12] Jack Diamond, *Good Practice Note on Sequencing PFM Reforms, page 20 (January 2013).*

[13] *Footnote 5, Government Finance Statistics Manual 2001* (p. 5). This GFSM is being updated and is due to be released in 2013.

[14] *Government Finance Statistics Manual* (1986).

accounting.[15] The Guide recommended that the GFSM 2001 methodology be implemented in the following four main stages (the time estimated to complete each stage is shown in parenthesis):[16]

1. Introducing the presentation, i.e., summary statements and detail tables, and classifications of the GFSM 2001 only for existing budget execution data, commonly referred to as adoption of the GFSM 2001 format (about one year);
2. Expanding the institutional and transactional coverage of GFS to include all general government/public units on a cash basis (2-4 years);
3. Expanding the coverage of GFS to include selected noncash items, commonly referred to as compiling GFS, on a modified accrual basis (3-5 years); and,
4. Expanding the coverage of GFS to cover all flows and stocks associated with general government/public units, i.e., compilation of GFS on both a cash basis and an accrual basis for the whole general government/public sector and its sub-sectors (10 years or more).

In Chapter 2 of the IMF Guide referenced above, the IMF further recommends[17] that consolidated financial statements for each of the following controlled entities be included in the financial statements of the controlling entity, as appropriate:

1. General Government Sector (GGS)—encompasses the central operations of government and typically includes all those resident non-market, non-profit entities that have their operations funded primarily by the government and government entities. Includes the following:
   a) Central Government—the political authority of a country's central government extends over the entire territory of the country. The central government can impose taxes on all resident institutional units and on non-resident units engaged in economic activities within the country. It also includes those expenses incurred for the provision of services, primarily for the benefit of individual households (e.g., education and health).
   b) State Government
   c) Local Government
   d) Social Security

(b) Public Financial Corporation Sector (PFC)—comprises resident government controlled financial corporations, quasi-corporations and non-profit institutions that primarily engage in financial intermediation and the provision of financial services for the market. Includes the following:
   a) Monetary (e.g., Central Bank)
   b) Non-monetary

(c) Public Non-Financial Corporation Sector (PNFC)—comprises resident government controlled non-financial corporations, quasi-corporations and non-profit institutions that

[15] *Government Finance Statistics Manual: Compilation Guide for Developing Countries*, September 2011.

[16] Ibid., pp. 186-188.

[17] Ibid., Chapter 2, Coverage of the GFS System, pp. 5-14. This Chapter provides an excellent guide on the appropriate classification for each controlled entity.

produce goods or non-financial services for the market. Included within the sector are entities such as publicly owned utilities and other government owned entities that trade in goods and services.

The public sector is defined further by the IMF in Chapter 2 of their Compilation Guide. This Chapter also includes guidance in assigning each controlled entity to each sector identified above.

The Accounting System

The IPSAS identify which accounting elements are to be recognized and how these elements will be measured. The chart of accounts used in the accounting system will need to be robust enough to meet the needs of management as well as provide the data required for government finance statistics identified above. It is not necessary that the chart of accounts use the same coding as identified in the GFSM 2001 since the data for those codes can be derived electronically from the accounting system through the use of bridging tables. However, in those instances where there are differences in the way the accounting elements are measured (i.e., historical cost in the IPSAS and current market prices in the GFSM), the data extracted from the accounting system will need to be adjusted for reporting in the statistical reporting system.[18] The financial statements required to be prepared from the accounting system are as follows:

Cash IPSAS

Statement of Cash Receipts and Payments (with a separate column for budgetary comparisons or a separate Comparative Statement of Budget and Actual Amounts)

Accrual IPSAS

Comparative Statement of Budget and Actual Amounts

Statement of Cash Flows

Statement of Financial Position

Statement of Financial Performance

Statement of Changes in Equity/Net Assets

The accrual IPSAS are based on the International Accounting Standards/International Financial Reporting Standards (IAS/IFRS) published by the International Accounting Standards Board and applicable to the private sector. The IAS/IFRS have been modified by the IPSAS Board, where appropriate, to adapt them to the public sector. If there are no applicable IAS/IFRS, separate IPSAS have been established. However, the Government Business Enterprises (GBEs) should adhere to the IAS/IFRS in a manner similar to that applied in the private sector. These are referred to as Public Corporations (financial and non-financial) in the GFSM.

Since most countries around the world currently report on the cash or modified accrual basis, developing countries intending to migrate to the accrual basis of accounting will generally accomplish this in stages for each of the government controlled entities identified in the GFSM 2001. Sequence and timing are only indicative and some countries or some elements within the

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[18] For a matrix identifying the differences, see research report *IPSAS and Statistical Basis of Financial Reporting: An Analysis of Differences and Recommendations for Convergence* (January 2005). A consultative paper *IPSAS and Government Finance Statistics Reporting Guidelines* (October 17, 2012) has been issued to converge these differences as much as possible. These documents are available in the Public Sector section of the IFAC website.

country may follow a different sequence or proceed at a different pace. For purposes of the Guide, six main stages are identified (the time estimated to complete each stage is shown in parenthesis):

1. Preparing a Statement of Cash Position, as well as a Comparative Statement of Budget to Actual Amounts, for select entities within the **central government** (about 1 year).
2. Expanding the coverage to include a Statement of Cash Receipts and Payments, as well as a Comparative Statement of Budget to Actual Amounts, as prescribed in Part 1 of the Cash Basis IPSAS[19] for the **central government**. However, it is not expected that consolidated statements would be prepared at this stage. This is generally referred to as the Cash Basis (about 3 years). Preparation of financial statements for the other controlled entities within the GGS, as well as the public corporations, is delayed until later stages;
3. Expanding the coverage to include **financial assets and liabilities** for **central government** in the format required for the statements prescribed by the accrual IPSAS above. Part 2 of the Cash Basis IPSAS[20] can assist in this effort. This is generally referred to as the Modified Cash or Modified Accrual Basis; for ease in presentation, this will be referred to as the Modified Accrual Basis in the Guide (3-5 years);
4. Expanding the coverage to include **all assets and liabilities** for the **GBEs (public corporations in the GFSM literature)**. This is referred to as the full accrual basis of accounting in the format required for the statements prescribed by the IAS/IFRS[21] (3-5 years).
5. Expanding the coverage in Stage 3 to include **all assets and liabilities** for **general government** in the format required for the statements prescribed by the accrual IPSAS above. This is generally referred to as the full accrual basis of accounting. Some developing countries may prefer to break Stage 5 into two sub-stages: 5a—simple accrual, basically tangible, non-heritage assets without anything complicated and 5b—all the IPSAS (which may not be achievable in the near term for many developing countries). (5-8 years); and
6. Expanding the coverage to include **all assets and liabilities** for **all general government controlled entities and GBEs** in the format required for the statements prescribed by the accrual IPSAS above. This is generally referred to as the full accrual basis of accounting (10 or more years).

The transition from one stage to another stage is illustrated below and is discussed in more detail in the Guide. In any event, the intent is to simplify the preparation of the financial statements and provide the basic information needed for decision making. Thus single statements for each stage should be prepared to the maximum extent possible. Preparation of consolidated statements is not required in the early stages unless the preparer can easily identify the intra-entity transactions to eliminate on consolidation.

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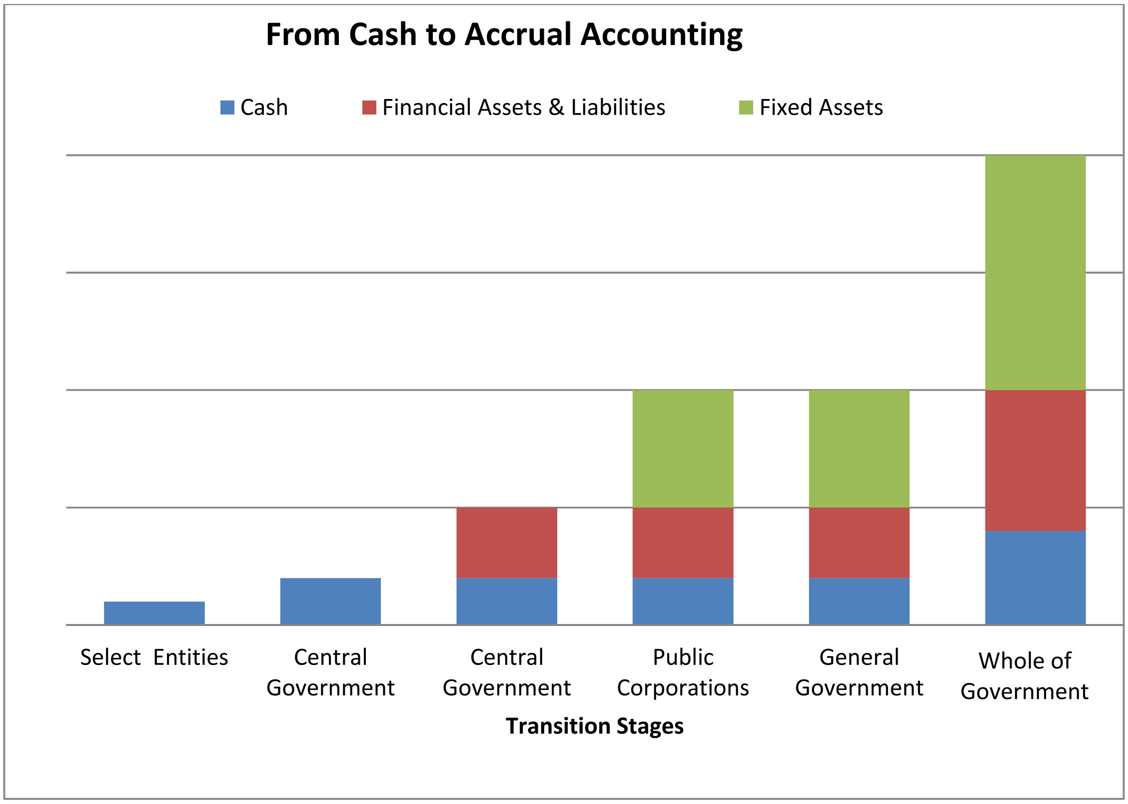
[19] Part 1, Requirements, *Financial Reporting Under the Cash Basis of Accounting*, IFAC, New York, 2008.

[20] Ibid. Part 2, Encouraged Additional Disclosures.

[21] *International Financial Reporting Standards,* International Accounting Standards Board (London).



As each stage is completed, the published financial statements should clearly identify the stage under which they are reporting. If difficulties (e.g., systems, capacity, etc.) are encountered in movement from one stage to another, these difficulties should be explained in the Financial Statement Discussion and Analysis narrative at the beginning of the report. Thus go or no-go decisions can be made until those difficulties are rectified.

It is recognized that the above trajectory is indicative, and the sequence or timing may vary for individual countries. For example, many countries will have a different starting point. Also the stage at which accrual accounting is implemented for GBEs may depend on factors outside the above sequence, and can be treated as an independent decision.

Most countries will implement the Guide by the adoption of national public sector accounting standards that progressively adopt the requirements of the IPSAS (first cash, then modified accrual, and finally full accrual). For this reason the requirements in the Guide are referenced to the relevant IPSAS to facilitate such a process.

Overview

Objective of the Guide

The purpose of the Guide is to describe the manner in which the annual general purpose financial statements for governments in developing countries should be presented to the legislative bodies and citizens. The Guide explains the six stages that governments in developing countries will generally go through as they implement the Cash Basis IPSAS en route to implementing the accrual IPSAS. The Guide is not intended to replace or supplant the IPSAS. The purpose of the Guide is to provide guidance on the implementation of IPSAS as a country moves through the six stages of cash to full accrual.

a. The Guide has the objective of providing best practice guidance consistent with existing IPSAS requirements for countries applying a more sophisticated version of cash basis reporting.
b. The Guide incorporates appropriate elements of the accrual IPSAS, e.g., incorporating financial assets and liabilities in a set of financial statements, reporting contingent liabilities, rules for converting foreign currency, etc.
c. The Guide is linked to IPSAS requirements (cash and accrual) and allows progressive adoption.
d. The Guide indicates elements of the Cash Basis IPSAS not feasible for early implementation and which could be deferred, e.g., GBE consolidation. Instead, it introduces the more sensible ideas such as consolidation phased by sector.
e. The Guide incorporates some ideas which are not IPSAS requirements (e.g., remuneration of public officials) but these are indicated as being additional non-IPSAS requirements.
f. The Guide could form the basis for National Public Sector Accounting Standards to be adopted by individual countries.
g. Individual countries could issue public sector financial statements in compliance with the national standards. Separately, countries could indicate and report the extent to which their national standards followed the Guide and IPSAS.

Some governments in developing countries have a common fund (sometimes called the Consolidated Revenue Fund or General Fund) into which all government income is paid. In these countries, transfers are made from this common fund, with the authority of the annual budget approved by the legislative body and warrants from the Minister of Finance to ministries, departments and agencies, which enable them to provide the agreed public services. Governments should be accountable to the legislative body for the funds raised and the payments made directly from the common fund. They are also accountable for the financial management and accounts of individual ministries, departments and agencies that are funded from the government's annual budget. Designated officials (called Accounting Officers in the Guide for ease in discussions) are assigned the above responsibilities. Such officials are personally responsible to the legislative body and may be called to account for the financial management of their entity to a legislative committee. The responsible officials present annual financial statements to their entity's legislative body. The Supreme Audit Institution provides independent assurance to the legislative body that the resources utilised by each entity have been mobilised and utilised in line with the annual budget and the relevant laws and financial regulations. Where necessary the annual report of the Supreme Audit Institution will also highlight irregularities that have been identified and make recommendations for their prevention and correction.

Compliance with the requirements of the Guide will enhance comprehensive and transparent financial reporting by government entities in developing countries. It will also enhance comparability with the entity's own financial statements of previous periods and with the financial statements of other entities which adopt the Guide.

Scope of the Guide

Government entities in developing countries that prepare and present annual financial statements to account for the monies raised or spent under the authority of its government's annual budget agreed by the legislative body, should apply the requirements of the Guide in the adoption of IPSAS and presentation of their general purpose annual financial statements. To meet this requirement, most developing countries will initially assure compliance with Part 1 of the Cash Basis IPSAS before they attempt to comply with the accrual IPSAS.

The Guide is not a universal prescription; every country is different and the national authorities will consider what is possible within what time, in conjunction with existing and planned reforms, and lead the reform process itself. In most Anglo-Saxon countries, general purpose financial statements and the associated reports of the Supreme Audit Institution are the core ways in which budget funded ministries, departments and agencies account to the legislative body for the money they have raised and spent during the relevant financial year. General purpose financial statements include those financial statements that are presented separately or within another public document such as an annual report. Francophone, Soviet, and some home grown systems may differ in these policies, but the basic concepts are the same or similar.

The Guide applies to both the financial statements of an individual budget funded entity (ministry, department or agency) and to the financial statements of the common fund from which transfers are made to the individual ministries, departments and agencies.

Accountability is achieved by the appointment of an accounting officer who is personally responsible to the legislative body for the budget (or votes) for their organisation. The Accountant General is the accounting officer for the common fund and so is responsible for providing the legislative body with the financial statements for the Fund. Accounting officers are similarly responsible for providing the legislative body with annual financial statements for the ministry, department or agency for which they are responsible.

Other funds may be established under the legislative authority (i.e., a Capital, Development, or Road Fund). In each case, arrangements should be made to appoint an accounting officer for each of the funds who will be personally responsible to the legislative body for the financial management of the fund and for presenting annual financial statements for the fund to the legislative body. The Guide also applies to the financial statements of such funds.

An entity whose financial statements comply with the key aspects of one of the stages described in the Guide should disclose the stage with which they have complied. In addition, the financial statements should indicate any key aspects of the relevant IPSAS (whether cash or accrual) with which they have not complied and explain the reason(s) for any such non-compliance.

The key aspects of the Guide are set in bold italic font. Entities whose financial statements comply with these key aspects should disclose their compliance with the Guide. Where an entity is not able to comply with any particular key aspect of the Guide, this should be disclosed in the notes to their financial statements with a brief explanation of the reasons for the non-compliance and, where appropriate, future plans to ensure compliance.

With the exception of stage 4 (which pertains to Government Business Enterprises or GBEs), the Guide applies to all government entities in developing countries. In addition, stage 6 includes the presentation of financial information pertaining to GBEs along with the financial information for the rest of the government controlled entities.

The *Preface to International Financial Reporting Standards* issued by the International Accounting Standards Board (IASB) explains that International Financial Reporting Standards (IFRSs) and International Accounting Standards (IASs) are designed to apply to the general purpose financial statements of all profit-oriented entities, which would include GBEs (referred to as public corporations by the IMF in the *Government Finance Statistics Manual*).

The Glossary to the IPSAS provides the definitions used in the Guide. The definitions of other terms used in the Guide are as follows:

<u>Accountability</u> – the obligation to demonstrate that work has been conducted in compliance with agreed rules and standards or to report fairly and accurately on performance results against mandated roles and plans.

<u>Accounting Officer</u> – public official with ultimate responsibility and personal accountability to the legislative body for the control of a vote (section of the annual budget) and the financial management of the related government entity in the developing country; May be appointed by the Treasury/Permanent Secretary in the Ministry of Finance (most senior public official) or the President of the entity.

Financial statements result from processing large quantities of transactions that are aggregated into groups according to their nature or function. The final stage in the process of aggregation and classification is the presentation of condensed and classified data that form line items either on the face of the financial statements or in the notes. If a line item is not individually material, it is aggregated with other items either on the face of the financial statements or in the notes. An item that is not sufficiently material to warrant separate presentation on the face of the financial statements may nevertheless be sufficiently material that it should be presented separately in the notes.

The principle of materiality provides that the disclosure requirements need not be met if the resulting information is not material. Materiality covers both the financial significance of transactions and the level of political interest in the subject.

Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. For an investment to qualify as a cash equivalent, it must be readily convertible to a known amount of cash and be subject to an insignificant risk of change in value. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity date of, for example, three months or less from the date of acquisition. Equity investments, for example, shares in public or private companies, are excluded from cash equivalents.

Bank borrowings are generally considered to give rise to cash inflows. However, in some jurisdictions, bank overdrafts, which are repayable on demand, form an integral part of an entity's cash management. In these circumstances, bank overdrafts are included as a component of cash. A characteristic of such banking arrangements is that the bank balance often fluctuates from being positive to overdrawn. In such cases, any bank overdrafts are netted against other bank balances and cash holdings. Thus, a liability is not reflected in the financial statements.

Cash flows exclude movements between items that constitute cash because these components are part of the cash management of an entity rather than increases or decreases in the cash the entity controls. Cash management includes the investment of excess cash on hand in cash equivalents.

ROADMAP TO IMPLEMENT IPSAS COMPILATION GUIDE

In many developing countries, the capacity among the accounting staff is not sufficient to fully implement the IPSAS, the data collection procedures are not adequately identified to collect the necessary data, or the software is not sophisticated enough to handle the various financial transactions. Consequently, as explained earlier, an IPSAS Compilation Guide has identified six stages to assist these developing countries in their efforts to better manage their financial resources. The Roadmap identifies the tasks to be performed in each of these stages in order for the government to be more transparent in its efforts to establish the accounting system necessary for full disclosure of its financial transactions.

The Roadmap is not a universal prescription; every country is different and the national authorities will consider what is possible within what time, in conjunction with existing and planned reforms, and lead the reform process itself. Technical assistance is, of course, readily available, but the change management of major reforms needs to be planned and carried through by the political directorate. To control the process, it is recommended that beginning and ending dates be identified for each task in each stage along with the name of the individual responsible for completing the task.

CERTIFICATE OF CONFORMANCE FOR IMPLEMENTING PERTINENT STAGES OF THE COMPILATION GUIDE

The Certificate of Conformance Program for Annual Financial Reports (Certificate of Conformance Program) is designed to help developing countries improve the quality and consistency of their financial reports. For practical considerations due to a lack of capacity or computer support, many of these developing countries have not prepared financial statements in conformity with generally accepted accounting principles (GAAP). Consequently, a Compilation Guide has been prepared to:

1. Provide guidelines to help standardize the format and content of annual financial reports prepared on a cash, modified accrual, or accrual basis;
2. Encourage governments to follow those guidelines by offering public recognition to those that successfully do so; and
3. Assist governments to implement the guidelines by providing technical materials and training.

The Certificate of Conformance Program is designed to encourage *compliance* with basic norms of sound financial reporting in situations where GAAP financial reporting is not practical. For some governments, participation in the Certificate of Conformance Program may be a first step toward GAAP financial reporting by implementing the accrual IPSAS. Any government, regardless of type, is eligible to participate in the Certificate of Conformance Program.   The Certificate of Conformance Program prescribes a cash, modified accrual, or full accrual basis financial reporting framework consistent with the provisions of the *IPSAS Compilation Guide for Developing Countries*.

For those developing countries that adhere to the *IPSAS Compilation Guide for Developing Countries,* separate certificates would be granted to those developing countries that have met the requirements for each of the following stages:

Stage 2: Central Government—cash reporting;
Stage 3: Central Government—modified accrual reporting; Stage 4: Government Business Enterprises—full accrual reporting;
Stage 5: General Government—full accrual reporting;
Stage 6: Whole of Government—full accrual reporting.

Note: A Certificate of Conformance will not be granted for Stage 1 since there are no general specifications against which to measure progress.

As noted in the Compilation Guide, this development program acknowledges that different jurisdictions may have different starting points and each country's program should be tailored to jurisdictional circumstances. In some cases, the GGS and controlled entities that are included in the GGS are already adopting a modified accrual basis (albeit modifications may vary from jurisdiction to jurisdiction). Some GBEs and certain statutory authorities are already adopting an accrual basis. While a series of steps with particular time frames are presented, this is a generalised, first principles model that identifies key components. The application of this program needs to be assessed by reference to (and may need to be amended to respond to) the circumstances of each jurisdiction. Such matters as the entry point to the program, time for each stage, and sequence of some items may vary depending on those jurisdictional circumstances. Consequently, a Certificate of Conformance may be issued to a country that has prepared a set of consolidated statements on the full accrual basis of accounting for their GBEs (Stage 4). A separate Certificate of Conformance may be issued to the same country if they have prepared a set of interim financial statements on the modified accrual basis of accounting for the Central Government (Stage 3).

For purposes of the Certificate of Conformance Program, **Local, State, or Central Governments** preparing financial statements on a "modified accrual basis" must meet all of the following criteria:

(a) The report must comply, in substance, with the basic requirements of GAAP for financial statement presentation, but applied in a manner consistent with a modified accrual basis. For example, a Central Government would need to present a combination of controlled entity financial statements (i.e., *compliance, in substance, with the basic requirements of GAAP*), but would use the same modified accrual basis for presenting data in all (i.e., *applied in a manner consistent with a modified accrual basis*);

(b) Only cash (and cash equivalents) as well as financial assets and liabilities that involve the receipt or disbursement of cash (or cash equivalents) during the period should be recognized, except as follows:

(1) *Interfund receivables and payables* that arise from transactions and events involving cash or cash equivalents must be recognized;

(2) *Assets that normally convert to cash or cash equivalents* (e.g., certificates of deposit, marketable investments, and receivables resulting from loans) that arise from transactions and events involving cash or cash equivalents must be recognized;

(3) *Liabilities for cash (or cash equivalents) held on behalf of others*, *held in escrow, or received in advance of being earned or meeting eligibility requirements* must be recognized;

(c) Note disclosures similar to those required by GAAP must be made if they are relevant to any of the items listed in (b); and

(d) Other note disclosures related to matters not presented on the face of the financial statements should be provided, as considered necessary.

Conversely, an Intermediate Statement of Financial Position prepared by controlled entities in **Local, State, or Central Government** using the modified accrual basis of accounting would *not* report: (a) capital assets or long-term debt that arise from transactions or events involving the receipt or disbursement of cash or cash equivalents; (b) deferred outflows of resources or deferred inflows of resources; (c) prepaid items; (d) supplies inventories; (e) accrued assets and accrued liabilities; or (f) other assets or liabilities that do not arise in connection with transactions or events involving the receipt or disbursement of cash or cash equivalents.

For those **GBEs** that have implemented the full accrual basis of accounting, a Certificate of Conformance will be granted if the controlled entities adhere to the IAS/IFRS. In like manner, a Certificate of Conformance will be granted to those **General Governments** that have implemented the full accrual basis of accounting if the controlled entities adhere to the accrual IPSAS.