

The Experience and Issues of IPSAS Implementation in Ukraine in the Context of Cooperation with the United Nations

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Abstract

The authors analyzed the main directions of reforming the preparation of accounting information by public sector entities: introduction of the national provisions (standards) of accounting in the public sector, the training for preparers of financial statements, the oversight on efficiency of implementation of innovations.

The role of international organizations in implementation of the reform in accounting and reporting is defined. Authors provided the survey in chronological order on certain aspects of cooperation between Ukraine and the United Nations (Conference on Trade and Development), in particular, the creation and improvement of the Guidance in the field of monitoring of compliance and enforcement for high-quality corporate reporting (MC & E).

The necessity of monitoring of the implementation and compliance with international accounting standards in the public sector, the development and consolidation of its basic principles at the international level and appropriate methodological support for its implementation are substantiated. Recommendations regarding the scope of the MC&E are presented.

Key words: the UN, Conference on Trade and Development, reform in the field of accounting in Ukraine, the International Public Sector Accounting Standards (IPSAS), the International Financial Reporting Standards (IFRS), Monitoring of compliance and enforcement.

Introduction

Since 1945 Ukraine has been one of the founding members of the United Nations. This obliges us to actively support the actions for implementation of the tasks set up by the UN Sustainable Development Goals (2015) and other solutions (The United Nations, 2015).

Cooperation with intergovernmental and international professional organizations in the field of developing the strategy and tactics of reforms is crucial.

The Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting of the United Nations Conference on Trade and Development (ISAR-UNCTAD) (Geneva, Switzerland) is one of the most authoritative international organizations.

Given the importance of reforming the national accounting and reporting systems based on international standards to attract investments and provide the development of the national economy, Ukraine participates in the activities of ISAR-UNCTAD UN.

Active cooperation with ISAR-UNCTAD started with the discussion in 2006 about the ways for implementation of international financial reporting standards (IFRS). Significant changes in the field of financial reporting in Ukraine were the result of the execution of the Cabinet of

Ministers Resolution “On Approval of the Strategy of application of International Financial Reporting Standards in Ukraine” (Strategy) (Cabinet of Ministers of Ukraine, 2007). The strategy was the result of Ukrainian cooperation with UNCTAD. In 2007 it was presented and approved at the 24th session of ISAR-UNCTAD.

In Ukraine the transition to the direct application of IFRS was held according to the Strategy on 1 January 2012. As of today The Strategy is almost accomplished.

The next step of cooperation with ISAR-UNCTAD was the capacity assessment for high-quality corporate reporting in Ukraine (from April to October, 2013) in accordance with UNCTAD-ISAR methodology, Accounting Development Tool (ADT). The assessment was carried out by the Ministry of Finance of Ukraine (the MOF). The obtained results of capacity assessment helped to determine actions for further development strategy.

In general, the following three strategic directions have been defined. The first is the development of the accounting system, the second is the development of independent audit and audit services market, and the third is training accountants, auditors, heads of departments of state authorities and other experts. In the context of development the accounting system it is necessary to admit the reforming in the public sector. It should be noted that great preparatory work is under way, providing major changes in the Governmental Financial Management. The integrated informational system of the Governmental Financial Management is being developed. Against this background, since 1st January 2015, public sector entities have been in transition to national provisions (standards) of accounting in the public sector (NP(S)APS), based on international accounting standards in the public sector (IPSAS).

Currently, 19 NP(S)APS and a new chart of accounts in the public sector were approved and designed in accordance with the requirements of IPSAS. However, the ideology of accrual basis of accounting (put into the new chart of accounts) is new to our system. Thus, the transition to it is accompanied by a number of methodological and technical complexities. To overcome them it is necessary to take some measures, in particular:

1) to design the methodological framework for the application of national standards:

- methodology for the application of NP(S)APS;
- order on how to fill in forms of financial reporting in the public sector;
- improvement of the methods of preparing and consolidating financial reporting;
- harmonization of chart of accounts with budget classification;

2) to develop new software. It should be introduced firstly in the treasury system, and then in budget entities system. Currently, the experts are working on the realization of this task;

3) to provide staff training:

- organizing of training for specialists of the MOF, the Treasury, high and low level administrators of budgeted funds (or spending units);
- holding seminars, conferences, consultations for employees of financial and accounting services of budget entities and funds of obligatory state social and pension insurance;
- training workforce for public sector entities that provide public services (especially for experts in the field of finance and accounting of budget entities);
- providing recommendations for improving the system of training, retraining and upgrading of experts in the field of finance and accounting.

The expected results of the reform:

- adaptation of Ukrainian legislation in the field of accounting and reporting to international standards (IPSAS);
- improvement of public financial management system;
- transparency of financial reporting data in the public sector and its comparability with the similar data of other countries;
- modernization of information and communication technologies;
- improvement in training and retraining of personnel in the field of accounting in the public sector.

Thus, in the field of accounting there are active reform processes. The considerable results have been achieved. However, there will be a lot of further work and it is necessary to provide constant monitoring of these processes in order to find out weaknesses.

At the same time, accounting reforming in the public sector can be considered as a "shock therapy." In order to smooth this transition it is necessary to provide serious consultative support and explanatory work.

Any reforming and administration will not give the desired effect without control and monitoring of the process. Therefore it is necessary to strengthen the control of the State Treasury Service in compliance with the common rules of accounting and preparation of reporting by spending units and other public sector entities.

At the same time we made some suggestions for further improvement of ADT questionnaires and the report layout as an evaluation tool. Overall scoring elements should be restructured with the inclusion of the Public Sector as a separate Pillar, not only as an addendum.

After reviewing the summary report and questionnaire, the summary report was updated in accordance with the changes that occurred in legislation on accounting, reporting and auditing, and new trends of reforming (on 1 January, 2016).

A new stage of cooperation between Ukraine and UNCTAD-ISAR started with the participation of Ukrainian experts in the development of the draft Guidance «Monitoring of compliance and enforcement for high-quality corporate reporting: guidance on good practices» (MC&E).

IFRS summarizes the world's best accounting practices. At the same time, as rightly mentioned in the Introduction to Guidance developed by UNCTAD, the benefits of their application cannot be realized unless the standards are properly implemented in a specific national environment. Therefore, monitoring of compliance with standards and their enforcement in corporate reporting are crucial for the achievement of economic and social effects from their implementation.

The MCE system is especially important for emerging market economies entering the global economy as new, independent countries. Ukraine is one of them. Reviewing the draft Guidance showed that it contains information on key elements of monitoring and control. The objective of the document is to provide relevant policy makers and other stakeholders in the area of accounting and reporting of a specific country with a reliable guidance on creating an effective national system of monitoring of compliance and enforcement and on identifying major changes to be addressed in establishing such a system.

As stated in the Draft Guidance, to build an efficient MCE system, it is important to define its scope and objective, design a set of MCE-related benchmarks, activities and methodologies for

both the prevention of bad practices and correction of errors, if necessary. In defining the scope of an MCE system, a decision should be made as to whom MCE-related actions will apply and what kind of information will be assessed.

Good practices of Monitoring compliance & enforcement in the Guidance are shown in the example of countries, which can be classified according to the UN into three groups:

- countries with developed economies (16 countries);
- countries with economies in transition (1 country);
- countries with developing economies (7 countries) (The United Nations, 2014).

Among mentioned 24 countries, most examples demonstrate practices of countries with developed economies. This is reasonable because the Guidance provides the best practices of monitoring of compliance & enforcement system (table 1).

Table 1: Countries with developed economies mentioned in the Guidance

Europe			Other countries	Major developed economies (G7)
European Union	New EU member	Other Europe		
Austria	Bulgaria	Iceland	Australia	Canada
Belgium	Croatia	Norway	Canada	Japan
Denmark	Cyprus	Switzerland	Japan	France
Finland	Czech Republic		New Zealand	Germany
France	Estonia		United States	Italy
Germany	Hungary			United Kingdom
Greece	Latvia			United States
Ireland	Lithuania			
Italy	Malta			
Luxembourg	Poland			
Netherlands	Romania			
Portugal	Slovakia			
Spain	Slovenia			
Sweden				
United Kingdom				

Source: The United Nations, 2014

However, sometimes it is impossible to apply best practices of developed countries in countries with economies in transition or developing countries due to lack of appropriate institutional and legal settings for such implementation.

This is stated in the Guidance, but recommendations are not specified according to the stage of development of the country. The Guidance indicates that effects of recommended procedures of Monitoring of compliance & enforcement can vary depending on the type of the country and such effects can be different for countries with economies in transition and countries with developing economies.

For example, it is noted that "...developing countries (where the credibility of new laws may need to be demonstrated through enforcement) show measurable improvements in market outcomes after enforcement cases, while this effect is harder to observe in developed countries that already have a credible regime", different stages of development (countries with economies in transition and countries with developing economies). Since there are no conditions for the implementation of Monitoring of compliance & enforcement system elements in such countries, which is necessary according to the Guidance, direct implementation of good practices of developed countries can bring the opposite effect or be ineffective.

It is appropriate to supplement the Guidance regarding countries with economies in transition and countries with developing economies, in particular:

- specification of recommendations contained in the Guidelines by examples of different options for countries with economies in transition and countries with developing economies;
- best practices and examples of Monitoring of compliance & enforcement system elements in countries with economies in transition and countries with developing economies.

A separate issue is the scope of MCE application, i.e. which elements within a reporting chain should fall under the scope of an MCE system. We share the point of view, reflected in the Guidance, that the following attributes of institutional functions are essential for promoting a higher quality of financial reporting: rule of law; regulatory quality; control of corruption; government effectiveness; political stability; voice and accountability.

The experience of post-Soviet countries suggests that these factors can be assessed and included in the scope of the MCE system. Political instability, violation of law, corruption and governmental non-transparent activities could be an obstacle for the development of national economies. The implementation of IFRS and International Standards on Auditing will significantly disrupt these negative factors. That is especially applicable to the public sector of the economy. In managing this sector, special consideration should be given to the strengthening of accountability, transparency and performance risk assessment. Therefore, we propose to include the public sector into the scope of the MCE system: the central and local government budgets (treasury system), high and low level of budgeted funds administrators (or spending units). The following arguments can be given in favor of this proposal.

First, the public sector has a significant share in the institutional structure of economy in general and Ukraine in particular. This is demonstrated by figures that describe the share of the Gross National Disposable Income (GNDI) of the state governance sector in Gross Domestic Product (Lovins`ka, L. H. & D`yachenko, Ya. Ya., 2016, Lovins`ka, L. H. & Yastrems`ky`j, O. I., 2016)

Second, the shadow economy is one of the manifestations of corruption in the country. Corruption and the shadow economy are two interconnected phenomena that take place in almost all countries. The “shadow” economy, meaning economic activities not included in statistics and not reported in accounting, exists everywhere. In developed countries, the size of the shadow economy ranges from 8 to 28% of the official GDP, in economies in transition – from 10 to 45%, in developing countries – from 60 to 75% (Schneider, F., 2015, Ministry of Economic Development and Trade of Ukraine, 2016).

Obviously, the problem of the shadow economy is very pressing for Ukraine in the transition period. Without its resolution, it is impossible to achieve the economic growth, realize a broad external and internal investment potential, and stabilize the financial and economic system. Therefore, monitoring of compliance and enforcement of accounting and audit standards and requirements in the public sector is a protective device against corruption and the shadow economy.

The third argument in favor of including the public sector in the MCE scope is the existence of high risks for the development of national economies in the area of public sector governance. This is especially relevant to economies in transition.

The public sector governance in these countries increasingly faces uncertainty as a result of transition to market relations and their further development. The crisis situation of the last decade exacerbates the general instability of the economy, the widening of gaps between the growth of financial deficit, and public expectations concerning the public sector performance.

The government's room for maneuver is becoming increasingly limited amid accelerated growth of government expenditures compared to increased GDP indicators. Under these conditions, it is even more difficult to forecast and understand what actions should be taken into consideration in making management decisions in the public finance management system. When making reasonable management decisions, it is necessary to consider the complication of cause-and-effect, or functional relations between the elements of a modern market mechanism. This factor causes difficulties in estimates and projections, in the understanding of relations between actions and their result, and in ensuring the reliability of accounting records and financial statements.

The public finance management sector has a number of risk factors, such as inefficient, irrational use of budgeted funds as a result of abuse of office or commitment of any other violations or corruption actions. Therefore, the risk to be considered in exercising control and verifying the reliability and fairness of reporting information is a risk contingent upon the probability of making inefficient management decisions and irrational use of budgeted funds. This risk causes an increase in the state budget deficit and a failure of the public sector to perform its core functions, such as a social function. For society, the social function of the State is essential, since it aims to ensure social security of citizens, create an environment conducive for the full exercise of their constitutional rights and freedoms, and maintain adequate living standards.

External risks are generally uncontrolled forces outside the public sector that have a significant impact on the informational support of the public finance management system (in particular, through state regulation and requirements for the accountability system; organizational and institutional circumstances and conditions of the preparation of financial statements). These risks include fiscal risks related to ensuring inflows to the state and local budgets and servicing them. Internal risks arise within the framework of budget-funded entities and institutions of the treasury system. These risks are mainly associated with an imperfect management system and weak internal control system. These risks constitute a significant part of the informational risk – one of the most serious and pressing issues of current management in the Public Finance System.

A number of risks have a significant impact on the informational support to the state governance sector. That is why it is necessary to modify key elements and MCE benchmarks of the Guidance document to create efficient national MCE mechanisms for public sector entities and professional accountants and auditors who work in this sector, and, by their actions, contribute to the development and enforcement of requirements for financial reporting.

To implement such an initiative, we have offered a number of additions to the text of the Draft Guidance in almost all of its sections. Additional factors that improve the quality of financial reporting and create a favorable investment and business climate, as stated in the Guidance, include: audit quality, corporate governance level, institutional supervision systems, public disclosure, and participation of the public in MCE.

Going forward, the work related to changes proposed by us to the Draft Guidance should cover the following issues:

1) coordination of the work on issues of strengthening corporate and public transparency and accounting. The Framework for building the MCE system should describe the issues of ensuring:

- quality of accounting records and financial statements in the public sector in defining the scope of the MCE system;
- monitoring of compliance of public sector entities with reporting standards;

2) coordination of the work on monitoring of compliance and enforcement of requirements for corporate reporting. Expand the Scope and Objectives Section of MCE to cover public sector entities: general government, government-owned corporations, and budget-funded entities;

3) coordination of the work on monitoring of compliance and enforcement of requirements for audit and quality assurance:

- expand the Scope and Objectives Section by specifying the Oversight Bodies that supervise and control compliance with accounting standards by public sector entities;
- to disclose institutional mechanisms of internal monitoring, it is necessary to consider the appointment of internal auditors in the public sector, their organizational and financial independence, official subordination and accountability, professional and social protection, etc.;
- in the context of improving procedures and methodology, it is advisable to disclose the criteria applied by national regulators to reforms of national accounting and audit systems, in particular, the best global and EU standards;
- in order to add new institutional mechanisms, it is necessary to state the need for post-audit support services – auditors should present their auditor’s report at the meetings of audit committees, supervisory boards and similar corporate governing bodies and provide relevant recommendations as well as initiate the inclusion of a separate item on the increasing the responsibility of the management of a government-owned corporation for the use of the auditor’s report and implementation of recommendations made by the auditor;

4) coordination of work on monitoring of compliance and enforcement of requirements for professional accountants. A potential area of human resources supervision is the training of workforce for public sector entities that provide public services. The issues related to such training should be added to the MCE Guidance. These issues include: replacing/training the personnel, tender-based selection of a professional accountant/state auditor on a new basis (requirements for the competence and qualification of candidates), mandatory professional certification of those responsible for financial statements/auditor’s report. The scope of the impact assessment should be changed to include requirements for public disclosure in the area of disciplinary proceedings and implementing differentiated (violation-based) sanctions against auditors, audit companies and professional accountants.

The revised text of the draft Guidance MC&E was considered at the 33rd session of UNCTAD-ISAR. This document is relevant for economies at different stages of development; however. It is necessary to emphasize that in transition economies, such as Ukraine, the implementation of provisions of this document is especially important. First, to pursue European integration, we are committed to achieving the UN Sustainable Development Goals adapted to the national environment. The reform processes require the implementation of the state-of-art governance technologies, including monitoring. It is also important in the context of the tasks announced by the G20 leaders at the Hangzhou Summit in September 2016 (China). In particular, building the stable and resilient international financial architecture under the conditions of global economic recovery and the emergence of new sources for growth that carry downside risks (G20, 2016).

Second, considering the high vulnerability of transition economies to external risks inherent to the global economic environment, it is necessary to perform the continuous monitoring to check the advisability of goals set and, where appropriate, correct the tactics of reform. It is important to focus on the result, which requires the Government to monitor the implementation of tasks, to assess the current status of reform, in order to identify problems and aspects that need improvement.

Despite an unprecedented burden on the Ukrainian budget because of foreign aggression, our economy shows the signs of stabilization and economic recovery. In particular, there is growth in investment activity – in the first half of this year, gross fixed capital accumulation increased by 11.7% compared to the same period of last year and the growth of foreign investment in Ukraine reached 154%. The rate of real GDP in the 2nd quarter of 2016 compared to the relevant quarter of the previous year was 1.4% (in the first half - an increase of 0.8%) (Official website of State Statistics Service of Ukraine, 2016).

This economic growth is primarily associated with the factors of recovery in domestic investment and consumer demand. Under these conditions it is critical to perform continuous monitoring. Joint efforts of our country, international organizations and the European Union to improve transparency, together with other factors, contribute to the gradual improvement of the investment and business climate.

Conclusion

For such countries as Ukraine, it is vital to implement the international best practices presented in the Guidance, but the implementation of these practices should be adapted to the actual economic conditions.

International organizations involved in issues relating to monitoring play an important role in this process, and cooperation of transition economies with such organizations makes reforms more efficient.

A prerequisite for any reform is the gathering of relevant and complete information about the best current practices, for instance, it is necessary to form a clear view of all the MCE elements and their interaction in order to establish the MCE system. These facts led to changes in the structure of the MCE Guidance. The approaches to introduction of the information about the three basic elements of the MCE system (corporate reporting, audit, requirements for professional accountants) were unified and brought into line with the structure of the MCE conceptual framework (definitions, objective and scope, institutional arrangements, activities and methodologies, monitoring arrangements and impact assessment mechanisms).

Also, it should be noted that the changes in the terminology used in the MCE Guidance, in particular, the transition from the “oversight” of auditing to “monitoring”.

In September, we made a number of proposals to further improve the perception of the Guidance and classification of information in light of the above; it was proposed to expand information about the regulation and presentation of reports on payments to governments and the MCE best practices for such reports.

The information indicated above proves the advisability of the proposal on presenting the data about the best practices not only by the MCE element, but also by the country. It will be useful to present the information about the best practices in the developed countries in annexes to the Guidance. This will allow countries that are embarking on the task of implementing such models to choose the most suitable MCE model for the size and structure of their economies.

There is a clear need to unify the requirements for classification of different groups of undertakings in order to enforce the transparency, market efficiency, and comparability of financial and non-financial information. It is critical because the requirements for classification may vary at both national and regional levels. In implementing MCE, the methodology for assessing the initial conditions and capacity of the country in the field of accounting and audit is the Accounting Development Tool designed by UNCTAD-ISAR.

A survey by this method allows for the detection of gaps in corporate reporting and aspects of oversight that need improvement.

The assessments of various elements of accounting, corporate reporting and auditing can be tracked in dynamics, which is important for determining the success of reform.

Therefore, we proposed to carry out such assessments of accounting and auditing, as well as the effectiveness of the MCE system in countries that pursue corporate reporting reform by using ADT on an annual basis.

The results of this annual monitoring will contribute to the development of the MCE system in countries conducting such assessments. Regular meetings for the discussion of these results will be the foundation for improving the theoretical and methodological pillars of the MCE system and the relevant amendments to the Guidance.

The proposed recommendations will help promote the best practices of monitoring of compliance and enforcement for high-quality corporate reporting, especially for the transition economies that face the abovementioned risks and problems. In Ukraine, with the full support and assistance of the IMF (International Monetary Fund), we are trying to overcome the crisis and carry out reforms designed to ensure financial stability in the country. Corporate reporting reform also takes place in our country as in other countries and our participation in the UNCTAD-ISAR Intergovernmental Working Group is of great importance in this process.

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