

## ***Form And Content Of Accounts–Moving Towards International Accounting Standards***

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*Mr. Iftikbar Ahmed Khan*, CGA (Pakistan), chaired the session. The other panellists were *Mr. B.S. Thapliyal*, Addl. CGA (India); *Mr. Abdullab-AlMamun*, CGA (Bangladesh); and *Mr. Ian Mackintosh*, Consultant, World Bank.

Initiating the discussion, the Chairman *Iftikbar Ahmed Khan* highlighted the need to ponder over what should be the road map for the Government Accounts in the South Asia region. He indicated that after the separation of accounts from the Audit in Pakistan in 2001, there is an ongoing project in Pakistan for introducing a new Accounting model on modified cash basis and a new Chart of Accounts giving more financial information. The project has reached a critical stage and after it comes through, there will be tremendous change in the Form and Content of Accounts as well as Financial Reporting.

*B.S. Thapliyal*, Addl. CGA made a detailed presentation on the Form and Content of Accounts followed in the Union and State Governments in India. Mr. Thapliyal stated that according to Article 150 of the Constitution of India, the form in which the accounts of the Union and of the States shall be kept is prescribed by the President on the advice of the Comptroller and Auditor General of India. This function is exercised by the Controller General of Accounts (CGA), Ministry of Finance (Department of Expenditure) on behalf of the President of India.

The accounts in the Govt. of India and the State Governments are maintained on cash basis i.e. recording transactions resulting only from cash flows.

### **Structure and Content of Accounts**

In India, the Government Accounts comprise:

- ❖ **Consolidated Fund** – this reflects the Government's fiscal operations. All revenues and receipts of the Government are credited to Consolidated Fund and the expenditures out of it are subject to the approval of Central/State legislature
- ❖ **Contingency Fund** – this is a revolving corpus of fund to meet any unforeseen expenses or an emergency. Monies taken out of this fund are recouped from Consolidated Fund, and
- ❖ **Public Account** – this deals with all the monies kept with and managed by the Government as a Trustee. It includes small savings, Provident Fund etc., Reserve Funds, Deposits and Advances, Suspense and Miscellaneous Remittances, Inter-Government adjustments and the Cash Balance of the Government. In this section, the “principle of lapse” does not apply.

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## Classification in Government Accounts

The classification system in India has evolved over the years with modifications being carried out over the years. Since 1<sup>st</sup> April, 1987, programmes are listed at the minor head level so that expenditure on programmes can be extracted directly from the Accounts. The code numbers allotted to major heads have also been changed from 3 digits to 4 digits to provide room for accommodating new functions, as and when they are evolved. All heads of accounts have been given numeric codes to facilitate the computer-based Financial Information System. The treatment given to various receipts and expenditures under the Consolidated Fund and the Public Account is as below.

### Consolidated Fund

#### Level-1: Sections

The Consolidated Fund is divided into the following sections:

Revenue	Receipt Head [Revenue Account]
	Expenditure Head [Revenue Account]
Capital	Capital Head [Receipts]
	Capital Head [Expenditure]
	Capital Head [Public Debt, Loans etc.]

The coding scheme in the Chart of accounts also follows a logical relationship pattern. Of the four digits allotted to a major head, the first digit of the 4-digit code of a major head signifies the characteristics of the transaction as follows:

0 or 1	Revenue Receipt
2 or 3	Revenue Expenditure
4 or 5	Capital Expenditure
6 or 7	Public Debt/Loans and Advances
8	Public Accounts

There is a simple linking between the Revenue, Capital and Loan heads. To give an example, 0401 represents Revenue receipts from Crop Husbandry, 2401 – Revenue Expenditure from Crop Husbandry, 4401 – Capital Outlay for Crop Husbandry and 6401 stands for Loans for Crop Husbandry.

#### Level-2: Sectors/Sub-sectors

The Consolidated Fund is further divided into Sectors and Sub-sectors as follows:

- ❖ General Services
- ❖ Social and Community Services
- ❖ Economic Services
- ❖ Grants-in-aid and Contributions – to accommodate transfer of resources in the form of grants-in-aid, share of duties etc.
- ❖ Public Debt, Loans and Advances, Inter-State Settlements, Transfer to Contingency Fund etc.

## **Public Account**

The Public Account is divided into Sectors and Sub-Sectors as follows:

- ❖ Small savings, Provident Fund
- ❖ Reserve Funds
- ❖ Deposits and Advances
- ❖ Suspense and Miscellaneous
- ❖ Remittances
- ❖ Cash Balance

## **Six Tiers Accounting Classification**

Following the Section and Sector/Sub-Sector levels as the case may be, the government transactions are classified under a six-tier system as discussed below.

**1<sup>st</sup> Tier – Major Head** – This is a 4 digit code which indicates the functions of the Government such as agriculture, education, health etc.

**2<sup>nd</sup> Tier – Sub-Major Head** - Sometimes a Sub-Major Head with a 2 digit code representing a sub-function is also opened when a major head is sub-divided depending upon functions and needs.

**3<sup>rd</sup> Tier – Minor Head** – This is a 3 digit code denoting the various plan and non-plan programmes undertaken by various departments of Government to achieve the objectives of the function represented by the major head. The expenditure on a programme is classified under the minor head relevant to the programme below the concerned functional major head irrespective of the department incurring the expenditure.

**4<sup>th</sup> Tier – Sub-Head** – Being a 2 digit code, this reflects and identifies the schemes undertaken in pursuance of the programme such as organisation.

**5<sup>th</sup> Tier – Detailed Head** – This 2 digit code represents organisations at the various subordinate administrative levels and also sub-schemes.

**6<sup>th</sup> Tier – Object Head** – This is meant for itemised control over expenditure and indicates the object or nature of expenditure in terms of inputs such as salaries, travel expenses, investment, loan etc. otherwise known as objects of expenditure. This corresponds to units of appropriation.

## **Periodicity of Reporting/Preparation of Accounts**

The fiscal year begins on 1<sup>st</sup> April and ends on 31<sup>st</sup> March. No adjustments are required to convert the data to a cash basis as none of the data are on accrual basis. The accounts data are recorded on a gross basis. Revenue and expenditure refunds are treated as corrective transactions and are netted out from the respective revenue or expenditure category, as appropriate. The data dissemination standards for Central Government operations and debt conform to the IMF's SDDS.

The final accounts, which are prepared on a yearly basis, are duly audited by the C & AG of India before they are presented to the Parliament. The Public Accounts Committee scrutinises these

accounts along with the Audit Reports. The Annual Finance Accounts give complete picture of Receipts and Disbursements pertaining to the Consolidated Fund, Contingency Fund and Public Account of the Government.

### **Weaknesses of Present Accounting System**

*B.S. Thapliyal* highlighted a few weaknesses in the present accounting system and expressed the view that the introduction of the Fiscal Responsibility Bill by the Government of India is a step in the right direction.

- ❖ The existing Accounting System on cash basis is unable to produce adequate data since it does not record or report state owned assets, specifically the tangible fixed assets.
- ❖ The accounts data is not yet comprehensive enough to provide useful information particularly at the micro level for taking timely corrective measures.
- ❖ There is no mechanism to record the commitments entered into, expenditure arrears or the outstanding liabilities of the government and no provision is made in the following year's budget on this account.
- ❖ Data is not compiled and presented w.r.t. the Receivables, Payables and various Liabilities particularly the contingent liabilities of the Union or State Governments.
- ❖ Accounts do not throw adequate light on Subsidies and Grants-in-aid given to various organisations/agencies.
- ❖ Since the budget is formulated on yearly basis, there is lack of continuity in handling the budget activities/applications beyond the financial year. The need to move to Medium Term Expenditure Framework – a multi-year budgeting system is imperative.

### **Move towards new Accounting Standards**

*B.S. Thapliyal* mentioned that Government of India has been considering a possible shift from a cash-based to an accrual based Accounting System. A Committee was set up by the Controller General of Accounts to examine the issue of specifying Accounting Standards for Government Accounting. The Committee submitted its report in August, 2002 and recommended the establishment of a Government Accounting Standards Board of India (GASBI), which could be vested with the responsibility of laying down Accounting Standards in the Public Financial System. However, the C & AG of India in the meantime has set up Government Accounting Standards Advisory Board (GASAB) with all heads of Accounting Services as its members.

### **Need for a Cautious Approach for Developing/Underdeveloped Countries**

*B.S. Thapliyal* observed that whereas the GFS 2001 and all International Bodies are advocating changing over to Accrual System of Accounting, a cautious approach needs to be taken in the case of developing and under-developed countries. The pitfalls in such countries to suppose

revenues on accrual basis of accounts are obvious and dangerous. On the converse, in the absence of a proper Commitment Control System, accrued expenditure may be swept below the carpet, which would not give true and fair picture of the government's financial health.

*Abdullah-Al-Mamun* made a brief presentation on the usefulness of the financial information in the public sector and the various elements of the general purpose financial statements. He also dealt with the problems and prospects concerning the form and contents as well as the related organizational and classification issues. He stated that usefulness of financial information in the public sector context lies in the way the information is provided to the users (the form) and the data that are contained in the financial statements (the contents). The International Public Sector Accounting Standards (IPSASs) recognize two bases for financial reporting: Cash based reporting and Accrual based reporting. The International Federation of Accountants (IFAC)– Public Sector Committee (PSC) provides a road map by incorporating various transition provisions within certain IPSASs for systematic progression from cash based reporting to accrual based reporting.

#### **Forms and Contents – Purposes**

Speaking about the purposes, *Abdullah-Al-Mamun* mentioned that the public sector financial statements are issued in two forms: general purpose form and special purpose form. The general purpose financial statements are issued for users that are unable to demand financial information to meet their specific information needs - citizens, voters, their representatives and other members of the public. The special purpose financial statements are prepared for other parties such as governing bodies, the legislature and for parties who perform an oversight function and can demand financial statements tailored to meet their specific information needs.

#### **Forms and Contents- Elements**

The elements of general purpose financial statements vary depending on the bases of reporting used. When the accrual basis reporting system is followed, the financial statements will include the Statement of financial position, the Statement of Financial Performance, the Cash Flow Statement and the Statement of Changes in net asset/equity. When the cash basis reporting system is followed, the primary financial statement is the cash flow statement.

#### **Forms and Contents- Problems and Prospects**

*Abdullah-Al-Mamun* observed that most of the countries of the South Asian region are currently under the regime of cash basis reporting. Steps should be taken initially to standardize the reporting system to move towards adoption of cash basis IPSAS - a short-term to medium-term objective. The adoption of accrual basis IPSASs can be considered as a long-term objective. The adoption of accrual basis IPSASs will require appropriate resources both in terms of physical and

human resources which most of the countries of the region can not instantly afford to provide. The accrual basis reporting system should also require massive changes in the public sector ethos and culture. Changes are also required in the parliamentary system of voting funds for the public sector entities, which are not easy to achieve overnight.

So, the countries of the region should join together and take pragmatic steps in a concerted manner by sharing the experiences and resources for establishing a system by remaining within the cash basis reporting system for the time being to build a transparent and accountable environment in the region. The initiatives should be directed towards ensuring that the financial reporting system should meet four principal qualitative characteristics viz. *understandability, relevance, reliability* and *comparability* as envisaged by the IFAC: PSC.

### **Organisational Issues**

Dealing with the organisational issues, *Abdullah-Al-Mamun* mentioned that few countries still have in some form or the other combined audit and accounts structure where Supreme Audit Institution (SAI) has a major role in financial reporting. Some have opted for separation of audit and accounts and are half way in the reform process. The different areas of public sector financial management such as treasury management, fund (budget) management, financial reporting, internal control, internal audit, statutory audit are not being operated in a transparent and accountable manner. The institutional separations are often unclear, ambiguous and there is lack of clear procedure in each area of financial management.

Then he spoke about the organizational issues concerning Bangladesh. The Constitution of Bangladesh provides that the 'forms and manner' in which the government accounts should be kept would be decided by the Comptroller & Auditor General with the approval of the President. Until recently, by virtue of the power vested on him through an Act of Parliament, the Comptroller & Auditor General was also responsible for keeping the Government Accounts. But to avoid conflict of interest the Comptroller & Auditor General, from July 2002, has been relieved of the responsibility of accounts keeping.

### **Classification Issues**

*Abdullah-Al-Mamun* observed that the lack of clear institutional separation and procedure have made it difficult to identify the various level of reporting entities such as Economic Entity, Controlling Entity, Controlled Entity etc. The classification of transactions under various groups of classification is not an issue that should be overlooked when we talk about standardisation of financial reporting. It is widely expected that the classification of transactions should meet the needs not only of the users of general purpose financial statements but also it should be amenable to fine tuning to fulfil the requirement of special purpose uses such as for National Income Accounting, Government Finance Statistics (GFS).

It has been the experience of many countries of the region that instead of creating a neutral platform for classification of transactions that can serve the divergent users' need and at the same time maintain the integrity of the system, the classification system were made biased and tilted towards fulfilment of the requirement of particular user or users thereby weakening the integrity of the system and depriving other users from getting appropriate benefit from the system.

*Abdullah-Al-Mamun* was of the view that even the adoption of cash basis IPSAS, let alone the accrual basis IPSASs by the countries of the region, requires a thoughtful road map in terms of changes in the institutional arrangement, unambiguous and transparent procedure of reporting and change in the culture and ethos of public sector.

The requirements for professional development of human resources involved in the process through training are also major factors that needed to be considered simultaneously.

Moreover, bearing in mind the long-term objectives for adoption of accrual basis IPSASs in public sector financial reporting, the additional accounting policies and disclosures as envisaged in the IPSAS should be reported. This would pave the way for smooth transition towards adoption of accrual basis IPSASs in the future.

Finally, he suggested that the countries of the region should join their hands together and form a committee consisting of experts drawn from each country of the region to identify the problem areas and come up with a recommendation for a uniform system of reporting that comply with the requirements of IPSAS and at the same time sharing the information for mutual benefits. Since we belong to and share the same historical linkage and heritage and since existing problems and prospects are almost similar in nature, he was of the view that even a minimum effort in this regard will certainly yield maximum benefit.

*Ian Mackintosh* mentioned that he is impressed with the organization of the conference, the quality of cases being presented and the ideas being put about. He then made a presentation giving an overview of the various International Accounting Standards including the International Public Sector Accounting Standards (IPSASs) evolved by the Public Sector Committee of the IFAC. He indicated that many countries, across all continents, have moved, or are moving, to accrual system. He explained the transitional steps to accrual accounting but stressed that a strong cash system is a necessary basic for any move to accrual accounting.

### **International Accounting/Statistical Standards**

*Ian Mackintosh* described the various International Standards followed for Accounting and Statistics purposes as under:

- ❖ International financial reporting standards (IASB),
- ❖ International public sector accounting standards (PSC)
- ❖ Government Finance Statistics (IMF)
- ❖ European system of accounts 1995 (Eurostat)

### **International Financial Reporting Standards**

These are promulgated by International Accounting Standards Board which is a full-time adequately resourced board. It has as an imperative to have an improved and increased set of standards by 2005. These standards are used as a basis for IPSASs. Harmonization of IFRS and IPSASs is of prime importance.

### **International Public Sector Accounting Standards (IPSASs)**

These are set by the Public Sector Committee (PSC) which is a committee of IFAC and funded by ADB, IFAC, IMF, UNDP and WB. The standards program was started in 1996 and the Standards are based on IASs.

### **PSC Output To Date**

The PSC has done a study on governmental financial reporting. It has come out with 20 accrual accounting standards, a standard on cash based accounting and guidance on transition to accrual based accounting. There have also been occasional papers on governments' financial reporting (including NZ, France, UK and Argentina) and Governance in the public sector.

### **Government Finance Statistics (GFS):**

These are promulgated by the IMF-latest manual issued in 2001 and are accrual based, using same concepts as IPSASs. Within the over-arching System of National Accounts, these are used to measure movements in a national economy and concentrate on General Government Sector but encourage consolidation of the whole of government. There are differences vis-a-vis IPSASs.

### **European System of Accounts 1995**

These standards are promulgated by Eurostat, a part of the EU. It is the requirement for members of the EU. Both GFS and ESA95 are consistent with 1993 System of National Accounts as regards definitions, accounting rules and classifications. ESA95 differs from GFS in the presentation of its publication, and its concepts are more specific and precise. ESA95 is more rules based than 1993 SNA. The 2002 GFS yearbook maps the ESA95 results to GFS.

### **Government Financial Reporting**

*Mackintosh* stated that majority of governments maintain cash account for the general government sector. However, many, across all continents, have moved, or are moving, to accrual based accounting. Some are reporting on the whole of government. It seems far from satisfactory to financially manage only some of the government's resources and liabilities and some of the government's entities. Sri Lanka and South Africa are good examples.

## **IPSASs Financial Reporting Under The Cash Basis Of Accounting**

It has a mandatory part and a non-mandatory part. The Mandatory part consists of a statement of cash receipts & payments including all cash receipts, cash payments and cash balances *controlled*, payments made by third parties, accounting policies and notes, appropriate classifications, restricted and unavailable cash balances, undrawn borrowing facilities, comparative information and consolidated financial statements with eliminations. The Non-Mandatory part consists of -

1. extraordinary items,
2. administered items,
3. major classes of cash flows,
4. related party disclosures,
5. assets, liabilities and budget comparisons, and
6. cash flow format.

The IPSAS cash reporting framework is auditable.

### **Transitional Steps To Accrual Accounting:**

An example of steps involved are to Establish standards and policies, Define the reporting entities, Improve cash accounting, Liabilities, contingencies and commitments, Financial assets, Non-financial assets and Budgeting. One could use IPSAS accrual accounting standards as a basis.

### **National Standard Setting Bodies And Charts Of Accounts**

*Ian Mackintosh* observed that the emergence of strong international standard setting bodies in both the private and public sectors changes the role of national standard setters. National public sector standard setters' roles could include: adopting the international standards, deciding when the various government sectors should move to accrual system, responding to international exposure drafts and being part of the international process, amending international standards for local conditions *in extremely rare circumstances*, supplementing international standards where there are gaps and educating the nation on standards.

He also felt that the National Standard Setting Bodies should not reinvent the wheel as only in extremely rare circumstances the need for amending international standards for local conditions will arise. There is probably a greater need for this body or bodies to set accounting policies under the standards.

While giving a brief outline of the Form and Content of Accounts in respect of the Cash Accounting Standard and the Accrual Accounting Standard, he also mentioned the basic qualitative characteristics of the Accounts, which are understandability, relevance, reliability, completeness, comparability and timeliness. The qualitative characteristics are even more pervasive in accrual accounting.

He also supported the idea that the countries of this region should get together and move towards a public sector committee and cash accounting standards. He also mentioned that there is a precedent for this and there has been a similar attempt down in Africa, where African

countries are getting together, to work together, to apply the IPSASs cash process accounting and there is a lot of synergies to be doing it together.

#### **Summing up by the Chairman:**

While concluding the session, the Chairman mentioned that the overall pattern of the Form and Content of Accounts is more or less the same throughout the region. We have moved from the old type of classifications to one, which of course facilitates computerization with numerical chart of classification. The weaknesses of the existing system and their form and contents were highlighted by various panellists in that it does not give adequate information to the policy makers and a very important point was touched upon by the Addl. Controller General of Accounts, India concerning the commitment control part. Incidentally the project that the Government of Pakistan is implementing is based on modified cash basis and does include the commitment part of accounting. Now as far as moving towards the accrual system is concerned, various speakers have highlighted the relevant issues and have advocated a cautious and calibrated approach. In our context, the important issue is of Capacity Building to achieve this end. The movement towards Accrual system should be from a strong and sound Cash-based one and on a step-by-step basis.

So these were the issues that were raised in this very important session on form and contents of Accounts, what ideal pattern should be followed in future and how one should move from one to the other and form a consensus on accounting as a tool for producing results.

#### **Conclusions and Recommendations:**

- ❖ Governments should aim to create a common platform for classification of transactions that can serve the divergent users' needs while maintaining the integrity of the system.
- ❖ The move towards rationalisation of the form and contents of accounts should be strengthened. The chart of accounts should be revised, if necessary, to reflect meaningful financial information keeping in view user-needs.
- ❖ Accounts should reflect future liabilities that exist on account of commitments entered into during the current and previous years. Contingent liabilities, subsidies and grants in-aid should also be spelt out clearly.
- ❖ To begin with, steps should be taken to standardize the reporting system to International Public Sector Accounting Standards (IPSAS) developed by the International Federation of Accountants (IFAC). This will inter-alia facilitate subsequent adoption of accrual based IPSAS.
- ❖ National standard setting bodies should adopt international standards, amending these standards should happen in rare cases. Accounting policies must unambiguously reflect these standards.

- ❖ Expert committees should be constituted, comprising professionals from various countries, to study common issues and recommend pragmatic solutions that could be uniformly adopted by countries in the region. The sharing of information in these committees would also be mutually beneficial.
- ❖ Countries in the region should get together and move towards establishing an institutional structure to oversee the modernization of government accounting in the region.