

# The International Journal on Governmental Financial Management

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International Consortium on Government Financial Management

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*“Working globally with governments, organizations, and individuals, the International Consortium on Governmental Financial Management is dedicated to improving financial management so that governments may better serve their citizens”*

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# International Consortium on Governmental Financial Management

## General Information

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Our mission includes three key elements. First, it highlights that, within the international community, the International Consortium on Governmental Financial Management (ICGFM or the “Consortium”) is unique - it serves as an “umbrella” bringing together diverse governmental entities, organizations (including universities, firms, and other professional associations), and individuals. At the same time, it welcomes a broad array of financial management practitioners (accountants, auditors, comptrollers, information technology specialists, treasurers, and others) working in all levels of government (local/municipal, and national). Additionally, the mission statement emphasizes the organization’s commitment to improving government infrastructure so that needs of the people are better met. Our programs provide activities and products to advance governmental financial management principles and standards and promote their implementation and application.

Internationally, the Consortium: (1) sponsors meetings, conferences, and training that bring together financial managers from around the world to share information about and experiences in governmental financial management; and (2) promotes best practices and professional standards in governmental financial management and disseminates information about best practices and professional standards to our members and the public. ICGFM provides three options for membership:

**1. Sustaining Members:** organizations promoting professional development, training, research or technical assistance in financial management; willing to assume responsibility for and to actively participate in the affairs of the Consortium. Each Sustaining Member has a seat on the ICGFM Board of Directors. (Dues: \$1,500)

**2. Organization Members:** government entities with financial management responsibilities, educational institutions, firms, regional and governmental organizations, and other professional associations. Six organization members serve on the ICGFM Board of Directors. (Dues: \$250/\$150<sup>1\*</sup>)

**3. Individual Members:** persons interested in or dedicated to activities directly related to financial management and who wish to be members in their own right. Six members of the ICGFM Board of Directors will be selected from among all individual members. (Dues: \$100/\$50\*)

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## Foreword

While the implementation of accrual accounting in the public sector started three decades ago, the current public sector literature is still interested in studying in detail the experiences of different countries and the further required reforms in this field. The adoption of accrual accounting in the public sector was introduced under the umbrella of the New Public Management (NPM) and New Public Financial Management (NPFM.). Therefore, the current issue focuses mainly on the public financial management reform (including the adoption of accrual accounting).

The first article of this issue deals with public financial governance, government fiscal reporting and financial performance: the Nigerian case. In this article, Christopher Alozie and his colleagues have attempted to appraise public corporate financial governance or impact of the quality of public financial management institutions on financial performance in the Nigerian federal treasury (Federal Ministry of Finance) from 1999 and 2014. The overall result produced a fair but below average performance rating. This shows corporate financial governance imposes significant adverse influence on financial accountability and financial performance in Nigeria's which can easily lead to financial distress.

The second article tackles some issues related to the implementation of accrual accounting in Ukraine. In this article, Tetiana Lefymenko has tackled the following issues of implementation of accruals-based accounting in public sector of Ukraine such as: the absence of proper measurement and recognition in accounting and reporting of all assets and liabilities of state (including all rights owned by the state, all natural resources that make a state asset and property, pension liabilities of state, etc.); uncertainty about the moment of recognition and measurement of revenue from payed taxes.

In the third article, Jesse Hughes and Michael Parry have attempted to discuss the conflict between the political issues and logical financial recommendations made by the accountants. They present some of the actions that are taken in the USA since publication by the IPSAS Board of the USA case in 2006.

Fourth article deals with an appropriate financial reporting framework for the public sector in East and Southern Africa. Herein, Amino Dhliwayo seeks to identify the perspectives of experts and senior officials that prepare financial reports in the Office of the Accountants-General in the public sector of the ESAAG region on the attributes that define the appropriate financial reporting framework for the public sector.

The fifth article focuses on the local government accounting: Hodgepodge or harmony. Nagalingam Nagendrakumer attempts to explain why Local Governments stick to Wickramanayake's Accounting System and castoff the Sri Lanka Public Sector Accounting Standards. The study adopted the qualitative methodology and case study strategy. Data for this study were gathered through semi-structured interviews in the selected cases. The study found that the continuation of Wickramanayake's Accounting System and rejection of Sri Lanka Public Sector Accounting Standards respectively are due to the existence and nonexistence of coercive pressure.

In the sixth contribution, Michael Parry and other members of Ad Hoc Committee on International Accounting Standards –ICGFM presents the response to Consultation Paper on: Exposure Draft 62 "Financial Instruments" Issued August 2017, Exposure Draft 63 "Social Benefits" Issued October 2017, and Accounting for Revenue and Non-Exchange Transactions August 2017.

We hope the articles in this issue will stimulate discussion on contemporary problems of public organizations. If you would like to participate in such discussions, please contribute to the next

issue of this Journal and/or attend future ICGFM events. We would also be pleased to receive reviews and suggestions for future issues. Send them to [icgfm@icgfm.org](mailto:icgfm@icgfm.org).

We look forward to hearing from you!

Prof. Dr. Hassan Ouda  
*Editor*

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*Vice President of  
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*President*

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# Corporate Financial Governance, Government Fiscal Reporting and Financial Performance: The Nigerian Case

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## Abstract

This paper appraises public corporate financial governance or impact of the quality of public financial management institutions on financial performance in the Nigerian federal treasury (Federal Ministry of Finance) from 1999 and 2014. Ex-post 'facto' empirical analysis approach using document content study and archival retrieval system as research instrument for data collection is the research design followed in this study. Secondary data extracted from Nigeria's Federal Government (FGN) fiscal budgets, financial statements, statutory audit reports and public finance statistics were utilized in analysis. Tools of data analyses employed include; numerical analysis, descriptive statistics governance performance indicators, (or non-financial performance indicators), financial performance indexing (FPI) variant of a modified Z-score were employed. Overall result indicates that the FGN's financial reporting practices is sub-optimal and in-effective in driving sound and reliable corporate financial reporting in the federal treasury; which contribute sub-optimal financial performance and the below-average macroeconomic performance too (citizenship distress). Of the five governance performance criteria, it was only auditors' un-qualified certificate in proxy for audit quality assurance that recorded significant positive performance on financial accountability. The remaining four criteria yield either negative or insignificant performance indicators, implying that they induce negative impact on public financial performance. The overall result produced a fair but below average performance rating. This shows corporate financial governance imposes significant adverse influence on financial accountability and financial performance in Nigeria's which can easily lead to financial distress.

**Keywords:** Corporate Financial governance, Fiscal Institutional Quality, Financial Reporting, Transparency, Financial Performance.

## 1 Introduction

### 1.1 Introduction

Financial governance in government entities or public finance management institutions comprise policies, rules, legislation, procedures of public revenue and expenditure management processes and fund dispositions that translated to surplus budget or budget deficit that culminate to fiscal discipline or otherwise (Hameed, 2005). Government accounting, financial controls, government financial reporting as well as transparency in public sector's financial reporting demonstrated by timely issuance of the audited accounts (Hameed, 2005; Alt & Lassen, 2006; Weber, 2012), Financial accountability and transparency in fiscal reporting open access and availability in public domain are considered as part of important commitment of the fiscal institutions to sound treasury management and good governance (Aruna, (2003) Hameed,



(2005); Alt & Lassen (2006); Weber, (2012)). Public financial governance is also inter-linked with function of the public finance management institutions and reflection of fiscal institutional quality, the political organizational structure, political systems (Weber, 2012). These also include the size of government and managerial behaviour of both the authorities of government, political office holders and management of public service. This study focuses on impact of non-financial performance of public finance management institutions (corporate financial governance) on sovereign treasury management and Nigeria's public financial performance (financial health).

The elements of public sector's financial governance interface with the public treasury and public financial management through fiscal budgeting, passage of annual appropriations bill, budget implementation performance and the timing lags. Statutory audit services including the routine internal auditing; audit reporting, oversight supervisory function of the public account committee of the legislature; and down to the approval, assent and publication of annual financial statement of government entity is another core component of fiscal governance. Other governance issues that act as veritable drivers of public financial performance rather remotely including certification of government annual accounts and reports by the government independent auditor and the head, national audit office; government accounting system and financial reporting practices, the availability, openness and accessibility of members of the public to government financial statements -. These demonstrate public financial accountability and transparency in handling of government's business transactions and financial affairs.

The qualitative characteristics of public finance management institutions (institutional factors) or financial governance often include: time-lag in fiscal budgeting, passage and implementation performance (budget management); time-lag in preparation of financial statements, statutory auditing and publication of annual financial statements; quality assurance in statutory audit reporting using clean or qualified opinion as proxy; government-wide accounting financial reporting practices and transparency (represented by open access and availability of financial reports) as the last one. Thus, the paper utilizes qualitative governance variables obtained from content study and the archival information retrieval approach with application of modified Altman & Hotchkiss (2010)'s Z-score financial distress index to measure the effect of financial performance in the Nigerian treasury. Gollwitzer (2012 or 2013) noted that since the seminar paper by von Hagen (1993), a rapidly increasing empirical literature has concentrated on the functions of fiscal institutions, effectiveness of their financial control efforts in enhancing public revenues, expenditures and overall fiscal discipline and by extension, macroeconomic performance.

Following a growing concerns on the quality and reliability of public sector's corporate financial reporting especially with the aftermath of the immediate past global financial crisis, governments, citizens, stakeholders and international agencies have shown greater interest in financial accountability and fiscal transparency. The International Monetary Fund (IMF's study (2007) revealed that about ten countries that experienced the largest unexpected increases in general government gross debt as a share of GDP between 2007 and 2010. The IMF's report identified that lack of incomplete information about government's underlying fiscal position; rendition of untimely and unreliable data about sovereign governments' deficit and debt contributed a collapse in market confidence some countries (Greece, Ireland and Portugal).

In related development the World Bank (1998) report evaluated government financial performance, public treasury management and the quality of fiscal institutions—that is-corporate financial governance in Lagos State, of Nigeria which encouraged the latter to extend huge credit facility to the State government. Dabbla-Norris and other (2010), Gollwitzer (2011) alongside few others authors have evaluated the impact of fiscal institutions on public financial performance in selected African countries. The research findings from these countries were

mixed but those studies revealed that those developing countries that have adhered to good accounting practices, proper accountability and transparency in financial reporting recorded better fiscal discipline and lower public debt position (Hamed (2005); Alt & Lassen, 2006).

Gleich (2003), Hallerberg and von Hagen (2005) have also made significant contribution to the quality of literature and development in practice of public financial management and government performance. Furthermore, Ncube and Vacu (2014), Casal, Gomez and Liste (2014) assessed financial distress in South African local governments and impact of political parties and political ideologies on financial performance in local governments in Spain respectively. However, the authors are not aware or accessed any empirical papers that duly evaluated the impact of public finance management institutions on sovereign treasury management and financial performance presently. Apparently, there is paucity of empirical studies on non-financial performance evaluation and measures of public financial performance in Nigeria. The aim of this paper is to assess the impact of public finance management institutions on government financial performance in the Nigerian government sector.

The study employed governance performance indicators, (non-financial performance indicators), financial performance indexing (FPI) variant of a modified Z-score in its performance measurement. The result indicates that the FGN's financial reporting practices is sub-optimal and in-effective in driving sound and reliable corporate financial reporting in the federal treasury; which contribute sub-optimal financial performance and the below-average macroeconomic performance too (citizenship distress). Of the five governance performance criteria, it was only auditors' un-qualified certificate in proxy for audit quality assurance that recorded significant positive performance on financial accountability. The remaining four criteria yield either negative or insignificant performance indicators, implying that they induce negative impact on public financial performance. The overall results yields a fair but below average performance rating grade 'D'. This shows corporate financial governance imposes significant negative effect on public financial performance and on public financial accountability in Nigeria which can translate financial distress.

## 1.2 Background Information to the Study Introduction

An assessment of the impact of corporate financial governance of a government entity as critical component of public treasury, financial performance and measure of financial health of government is necessary due to paradigm shift in management philosophy in the public sector. Thus, the paper focused on the effect of managerial behaviour of the public service management, managerial efficiency, inefficiency; effectiveness or ineffectiveness in public financial management which in turn translate into good public governance and macro-economy performances. von Hagen (1993, 2005), Gleich (2003); Gollwizer (2013) and several others have contributed to a rapidly increasing literature on public financial management that focused on appropriate design of budget institutions, on budget management and their roles in enhancing fiscal discipline. Whilst most of the empirical literature concentrated on budget institutions, practices and fiscal performance; little has been research and reported on public sector's corporate financial governance on government financial performance particularly Nigeria, even though the country has remained cynosure of massive revenue leakages, financial corruption and mismanagement of resources in the past years.

The adoption of qualitative (non-financial) governance variables in performance management system becomes necessary due to the influence of managerial behaviour, efficiency or inefficiency and general attitude of public functionaries and those of management of public service in handling public funds and service delivery (Kattelus, 2013, Hoffman and Clarkson, 2005). Qualitative governance indicators in performance measurement system in evaluation of public financial performance represents one the latest approach and international best practices

adopted in assessing good public governance and macroeconomic performance in the contemporary period (Carmeli, 2008, Casal, Gomez and Liste, 2014).

The incidence of the last global financial crisis inadvertently revealed shortcomings in many governments' understanding of their underlying financial position and potential shocks to that position. The IMF's (2007) report identified among other issues that lack of incomplete information about government's underlying fiscal position; rendition of untimely and unreliable data about sovereign governments' deficit and debt contributed a collapse in market confidence some countries. The report of the study finds also that hidden or implicit obligations to public corporations and public-private partnerships (PPPs) outside the general government perimeter rebounded on the government finances when the crisis struck in Greece, Germany, Iceland, Portugal, and the US (Weber, 2012). In Greece, Portugal, and Spain, governments cash-based budgeting, accounting, and reporting systems failed to capture and control expenditure commitments, resulting in an accumulation of payment arrears before and during the crisis. Second, that percent of the increase was due to an underestimation of the likelihood and scale of shocks to the government's fiscal position. In particular, the fiscal impact of the unexpected fall in output was an important factor in all countries and the principal reason for the unexpected surge in government liabilities in five. Weber (2012) identifies poor fiscal transparency as a key predictor of statistical discrepancies in published fiscal data as measured by stock-flow adjustments between general government net lending/borrowing and the change in net debt. Gelos and Wei (2005) cited in Alt and Lassen (2006) find that fiscally more transparent countries tend to attract more foreign equity investment and are less vulnerable to withdrawals during times of stress. During the last decade and a half substantial efforts have been made to improve fiscal transparency across advanced, emerging, and developing economies (Gelos and Wei, 2005) cited in Alt and Lassen, (2006). The Asian crisis of the late 1990s highlighted shortcomings in financial reporting in both public and private sectors and regarding the linkages between the two (Lane and others, 1999; cited in Alt & Lassen, 2006) Empirical evidence has shown that gradual improvements have been achieved in fiscal transparency reporting across countries (Alt & Lassen, 2006).

From Nigerian perspective, the narrow base of the taxation and non-oil fiscal revenue generating capacity couple with recent decrease in crude-oil price and dwindling revenue accretion to the Federation Account caused treasury liquidity and solvency problems in public finances of different layers of government entities in Nigeria. Under the prevailing financial situation, the Nigerian governments at different levels are facing difficulties in meeting financial commitments. This fiscal situation has manifested in service-level distress and lack of fiscal solvency which arises partly as due to tremendous increase in demand for public goods / services in line with population growth (Ritonga, 2014). Consequently, the constituents require greater financial accountability and transparency particularly in general government sector and Nigerian public service (Ncube & Vacu, 2014).

Governments as an economic, political and sovereign entity are required by its own laws, regulations and ethics of good governance to prepare, present and gazette their annual audited accounts and reports commonly referred as financial report for each year on regular basis (World Bank, 2010, International Organization of Supreme Audit Institutions (INTOSAL), 2006, FGN, 1999). This reporting responsibility is equated to and or related legal and corporate governance requirements to registered companies and enterprises in the private sector which compels the management to prepare and publish their audited reports and annual financial statements to its members, relevant government agencies, and other stakeholders in the affairs of a company including the public in some cases. The main objective of financial reporting in public sector and private enterprises is to provide accurate and reliable financial information concerning economic entities, primarily financial in nature, and useful for economic decision

making (International Federation of Accountants (IFAC) 2013) Kattelus, (2013) stated that the existence of an efficient financial reporting systems and practices enhance credibility, integrity, public confidence, and the information value of government finances, and contribute to more effective management of resources.

Preparation, issuance of comprehensive and provision of reliable government-wide financial statements as core components of government finance statistics vis-à-vis other annual corporate reports constitute essential pieces of public information from government sector (Aruwa, 2004, Padovanni, 2016). It depicts the level financial stewardship and accountability by the state actors to the constituents (Ncube & Vacu et al), other stakeholders and the society at large. These user groups supports government through taxes, grant of short and long term credit facilities, variety of financial aids and technical assistance from the development partners (Kattelus, 2013).

However, it has been observed that the annual statutory auditing, government financial statements and the overall government fiscal reporting leaves much to be desired. For instance, the Nigerian public finance laws stipulated that the annual appropriation bill takes effect from the first day of each new fiscal year but in practice, the federal budget laws are passed by the end of first quarter and or in the second quarter of current periods. Second, the Nigerian (1999) Constitution requires that the FGN's annual audit report and accounts should be issued and published within nine months after the end of each financial year but this rule is not fully complied with. Therefore, effective financial reporting practices, commencing from budgeting, financial accounting, management accounting, auditing services and publication of government financial reporting are critical to government performance (public service) in order to be in better position to formulate fiscal policies, and economic decision and deliver the required services to the population.

Aruwa (2004) have argued that public accountability is an obligation on the part of the government to render proper record of public resources for responsibility entrusted to the public office holders. It is also a relationship based on the obligation to demonstrate and to be responsible for performance in light of agreed expectations. Fiscal accountability in its broad context is a duty of stewardship or every public central treasury as well as the public functionaries particularly those entrusted with the management of public finance owe the population especially the tax payers, stakeholders and the general public without boundaries (Kattelus, et al). Kinua (2013) stresses that accountability is the regime's duty to provide the citizenry with the facts, figure and good reasons for public revenue generated and feedback communication on the utilization. It is a common phenomenon that the published annual financial statements of the Nigerian governments are rarely found, accessed and read in the public places and libraries and unavailable in the internet financial reporting, presently. Whilst the published financial reports of the Nigerian governments and their public sector organization are not readily available in the public domain, the governments have been engrossed with several reported cases of missing public funds, leakages in public revenues and mismanagement of financial resources in the treasury. These incidents constitute sufficient background for discerning researchers, stakeholders in fiscal affairs of the Nigerian state and authorities of the governments in Nigeria to carry out in-depth research inquiry into the public corporate financial governance and public financial performance which is non-existent and the over-riding gap this paper is bridging here.

### **1.3 Problem Statement**

Financial governance in government entities which includes transparency in fiscal reporting plays an important part in the evaluation and management of fiscal risks. Fiscal risks are factors that give rise to differences between a government's forecast and actual fiscal position (Aruwa,

(2003), Weber (2012); Alt & Lassen (2006); International Monetary Fund (IMF), 2007).). These differences according to Babatunde (2013), Weber (2012); Alt & Lassen (2006) can be the result of (i) an incomplete understanding of the government's underlying fiscal position; (ii) exogenous shocks to the public finances; or (iii) endogenous changes in fiscal policy settings. While improvements in fiscal transparency cannot eliminate these risks, they can help policymakers and the public to understand and respond to them. For example, first, there remain significant gaps and inconsistencies in financial transparency standards in areas such as the coverage of public institutions, treatment of assets and liabilities, reporting of transactions and other economic flows, and the comparability between forecast and actual data. These problems are inherent in annual financial reports and fiscal reporting (government finance statistics) in different countries, especially in developing economies.

Public budgeting system and processes in the Nigerian government constituted only of the toughest challenges of public treasury and public financial management over the years. For instance, Nigeria's federal annual budget appropriation bills has been consistently passed and implemented around the second quarter of each current fiscal year for the past decade (Omolehinwa, 2014) which in effect affect effective budget implementation. Several previous studies that have investigated the impact of fiscal institutions (which includes fiscal governance), public budgeting on government financial management in different countries by Hameed (2005), Dabla-Norris and others (2010) established that developing countries with greater transparency in budgeting and fiscal reporting recorded better fiscal discipline and credit rating. This is supported by Alt and Lassen (2006) which found that a greater transparency in government financial reporting is associated with lower annual budget deficits and public debts. Moreover, monitoring of fiscal transparency by other institutions has not been sufficient to prevent the substantial underreported deficits and debt in some advanced economies (by citizens, residents, stakeholders, trading partners and various user groups (IMF, 2010b). This has reflected a combination of falling demand and a reduction in public financial resources devoted to this area.

In related development, theoretical and empirical literature have provided evidence that excessive delays in execution of statutory auditing and belated rendition / publication of the audited annual financial statements erode public confidence in financial reporting (Aruwa, (2003 or 2005); Kittnonen, (2013); Weber (2012); Alt & Lassen (2006); International Monetary Fund (IMF), 2007). The extant legislations guiding government accounting and financial reporting for Nigeria stipulate that government annual accounts must be audited, approved and published within nine months after the end of financial year. However, in practice, Nigeria's government audited accounts and reports have been approved and published in about thirty months after the completion of several fiscal years. This trend in corporate financial or fiscal reporting renders the information utility of such financial statements obsolete for decision-making and at the same token enhance information asymmetry and also encourage mismanagement of public funds and assets. We are not aware of any published empirical study that adopted the elements of financial governance to assess public financial performance presently. Given the role of public functionaries and political office holders in fiscal policy decisions and the avalanche of reports of mismanagement of public funds in the federal treasury, non-inclusion of fiscal institution in the analysis and measurement of fiscal condition in government entities it is expedient to examined the effect of financial governance on government performance in Nigeria.

From the Nigerian perspective, Federal Government of Nigeria (FGN) approved the adoption of the IPSASs accounting and financial reporting system 2010 and proposed that the new accounting regime takes effect in 2014 but this is yet to be fully implemented (as at the 2016 year-end). This is an indication that the accounting systems and financial reporting used in

preparation of the FGN's financial reporting could have been sub-optimal and lacking transparency over time. Babatunde (2013) confirmed that Nigeria has not implemented accrual method in its fiscal budgeting and government accounting and argued that the implementation of accrual accounting will enhance transparency. Apparently, governments' implementation of international accounting and statistical reporting standards has lagged behind the development of the standards themselves. Hameed (2005), Alt and Lassen (2006), Weber (2012) observed that implementation of international accounting and statistical standards help in detection of the deficiencies in the public sector entities' accounting and can highlight otherwise hidden costs or obligations and encourage governments to budget and reflect such events in the accounts.

Effectiveness in the publication of audit reports and financial reporting of government entities in accordance with internationally accepted standards can highlight weaknesses in government financial control or accounting practices and prompt governments to remedy the issues identified. In buttressing this view-point, the World Bank (2010) study reports that more frequent and timely public reporting of fiscal developments can help ensure that fiscal forecasts are based on the most up-to-date understanding of the current fiscal position and facilitate rapid policy responses to shocks. Surprisingly, in the Nigerian model of government accounting and financial reporting, printed (hard) copies of the annual audit reports and financial statements of government entities of the three tiers are rarely in circulation and thus, they remain inaccessible to the citizenry and other members of the public. Federal Government of Nigeria hardly publishes its annual financial statements in her official web-set – that is, internet financial reporting and likewise the state governments. In the light of lack of internet financial reporting, transparency in fiscal reporting is presumed to constitute a major factor that facilitates corrupt practices, mismanagement and lack of proper functioning of the economy. The degree of fiscal transparency has been shown to be an important predictor of a country's fiscal credibility and performance. A growing body of empirical research has highlighted the positive relationship between the degree of fiscal transparency and measures of fiscal sustainability (such as government deficits and debts), with a stronger correlation among low and middle income countries than among high income countries. Empirical evidence also points to a positive relationship between the degree of fiscal transparency and market perceptions of fiscal solvency.

The main objective of the paper is to assess the impact of financial governance on government financial performance in Nigeria's federal treasury. The specific objectives are:

- (1) Examine the impact of budget passage vis-à-vis implementation timing-lag on public financial performance in the Nigerian treasury.
- (2) Appraise impact of statutory auditing alongside financial reporting timing-lag in gazette of government's (FGN) annual financial statements and financial performance;
- (3) Determine the direction to which un-qualified audit reporting of the Nigerian government's financial reporting (unqualified reports) in attestation of audit assurance influence on financial performance;
- (4) Ascertain the direction to which the quality of government accounting practices alongside financial reporting influence financial performance in Nigeria's federal treasury;
- (5) Determine the extent transparency in government financial reporting (distribution, availability and open access in public domain including internet reporting) affect public financial performance in federal treasury.

The pertinent research questions that guided the investigation on the impact of financial governance and government financial performance in Nigeria are the following:

- (1) In what direction does the timing-lag in federal budget passage-implementation as a criterion of fiscal governance affect government financial performance in Nigeria's sovereign treasury?
- (2) In which direction does statutory audit, financial reporting vis-à-vis gazette of government (FGN) financial statements timing-lag affect the utility of accounting in decision making in the Nigerian federal treasury?
- (3) To what extent does the un-qualified audit opinion certification as evidence of audit quality assurance of government financial statements sustain public confidence in government's financial reporting add value to the management of treasury in Nigeria?
- (4) Which direction does government accounting systems including financial reporting practices affect government financial performance (financial health) in federal treasury?
- (5) Which direction does the prevailing trend pattern in the distribution or circularization of the Nigerian government's financial statements affect financial performance in the federal treasury?

The hypotheses of the research are:

- (1) Budget passage along with implementation timing-lag does not impose adverse impact on Nigeria's federal treasury's financial performance.
- (2) Timing-lag in statutory audit execution, presentation of government annual financial reports and the issuance (gazette) of audited financial statements does not induce poor financial performance (impairment in information utility fiscal policy-making in Nigeria's federal treasury).
- (3) Unqualified audit opinion as certificate of quality assurance of assurance to government annual auditing services and rendition of financial statements does not sustain public confidence in accounting information utility including soundness financial performance in Nigeria's federal treasury.
- (4) Government-wide accounting systems combined with financial reporting practices in Nigeria's federal treasury do not yield positive impact on financial performance in the federal treasury.
- (5) Transparency in government's published financial statements does not confer positive influence on information utility of the corporate financial reporting as well as financial performance of the Nigerian federal treasury.

The paper is significant in public treasury management and financial performance management because useful insights of the impact, contribution and consequences of institutional quality and or fiscal governance factors on sound, efficient and effective public financial management in a government treasury and macro-economy. Human side of the public financial administration within the realm of new public management as a critical factor which can enhance or undermine good public governance and proper functioning of the economy, especially under resource constraints.

Through adoption of qualitative governance variables which capture managerial behaviours of the public service, managerial efficiency or inefficiency, incompatible incentives of public functionaries to utilize public resources for personal interest, budgeting systems, fiscal management, financial practices, statutory auditing and transparency in financial reporting; all configured into performance measurement metrics of financial performance, this research

established that fiscal governance exert enormous influence on management of public resources. Furthermore, performance management system developed and adopted in this study exposes the nature, relevance and implication of public finance management institutions quality, and by extension, managerial efficiency and or inefficiency of the public functionaries on public financial performance and political economy (Casal, Gomez & Liste, 2014). Empirical evidence in Casal et al identified managerial behaviour of the executing agencies in the public sector to exert influence on public resources management, financial accountability and sound or weak public financial management including losses or wastage of funds.

The scope of study is assessment of impact of the public financial management institutions' quality (fiscal governance quality) on financial management performance in federal treasury. The paper covers a total period of 16 fiscal years, from year 1999 to 2014 financial years, both years inclusive. Budget passage / implementation timing-lag, statutory auditing / financial reporting timing lag, audit certification attesting audit quality assurance, accounting systems, financial reporting architecture vis-à-vis quality of financial reporting, and transparency in publication of financial statements as proxy for and public accountability are the fiscal governance variables of interest in the paper.

## 2 Review of Related Literature

### 2.1 Conceptual Literature

Public finance governance or simply fiscal institutions quality in the context of public treasury and public finance management in a government entity refers to the collection or amalgamation procedures, rules, legislations, controls systems, organization structures adopted in the public service that guide management of resources and good governance. Kopits and Craig (1998) defined fiscal (financial) transparency in a government entity as “openness toward the public at large about government structure and functions, fiscal policy intentions, public sector accounts, and projections. The ministries, departments and agencies of government, public functionaries and all employees in the government sectors follow these procedures in all their functions in handling of public financial resources. Public financial management institutions include also all committees of the legislative arm of government (under a democracy) vested with responsibilities and oversight functions on budgeting, revenue, public finance and public accounts. Casal, Gomez and Liste (2014), Dabbla-Norris, and others (2010); Gollwizter (2012) stated that the quality of public finance management institutions or fiscal institution exerts strong influence (positive and or adverse) on financial management system, financial performance in government treasury and macroeconomic performance of a country.

Government accounting refers to the concepts, standards, rules, and systems used to generate the financial information used in fiscal reporting (IMF, 2007). Weber (2012), Alt and Lassen (2006) defined fiscal transparency as the clarity, reliability, frequency, timeliness, and relevance of public fiscal reporting and the openness to the public of the government's fiscal policy-making process—is a critical element of effective fiscal management. Fiscal transparency helps ensure that governments' economic decisions are informed by a shared and accurate assessment of the current fiscal position, the costs and benefits of any policy changes, and the potential risks to the fiscal outlook. Fiscal transparency also provides legislatures, markets, and citizens with the information they need to make efficient financial decisions and to hold governments to account for their fiscal performance and their utilization of public resources. Finally, fiscal transparency facilitates international surveillance of fiscal developments and helps mitigate the transmission of fiscal spillovers between countries. Padovanni, 2016 argued that fiscal institutional quality represent a qualitative governance indicators approach to the evaluation of public financial performance and performance management of public treasury in an entity. Padovanni, 2016 explains further that measures of financial performance and financial health of



an entity assesses its ability to meet its existing financial obligations both in respect to service commitments, creditors, employees and other stakeholders. Carmeli (2008), Padovanni (2016) stressed that financial condition (health) is a broad, complex concept with both short and long-term implication that describes the financial health in a government entity in the context of its overall economic and financial environment.

## 2.2 Relationship Between Corporate Finance Governance and Public Financial Performance

The association between public finance governance factors has been considered in measuring public financial performance by many scholars including Casal, Gomez and Liste (2014). Public financial management institution or fiscal institutions and political economy links public resources with government financial management performance and how the political and fiscal institutions affect the macro-economy is an essential component of performance evaluation framework. Weber (2012) argued that the degree of fiscal transparency has been shown to be an important predictor of a country's fiscal credibility and performance. A growing body of empirical research has highlighted the positive relationship between the degree of fiscal transparency and measures of fiscal sustainability (such as government deficits and debts), with a stronger correlation among low and middle income countries than among high income countries. Empirical evidence also points to a positive relationship between the degree of fiscal transparency and market perceptions of fiscal solvency (such as credit default swap spreads on sovereign debt, credit ratings, and foreign equity investment), this time with a stronger correlation among high-income than middle-income countries. The impact of these institutions on public resources are multi-faceted and may arise through incompatible incentive of public functionary to hold on to power, budgetary allocation and compensation for patronage or support, deliberate mismanagement of resources, quality of accounting and audit institutions and provision of asymmetric financial information.

Furthermore, Alt and Lassen (2006), Hameed (2005) and Weber (2012) considered transparency in government financial reporting refers to the clarity, reliability, frequency, timeliness, and relevance of public fiscal reporting and the openness to the public of the government's fiscal policy-making process. Within this, clarity refers to the ease with which these reports can be understood by users (Weber, 2012). Alt and Lassen (2006) opined that reliability refers to the extent to which these reports reflect the government's true financial position, frequency (or periodicity) refers to the regularity with which reports are published, timeliness refers to the time lag involved in the dissemination of these reports, relevance refers to the extent to which these reports provide users with the information they need to make effective decisions, and openness refers to the ease with which the public can understand, influence, and hold governments to account for their fiscal policy decisions.

Kattelus (2013) argued that the financial factors include revenue generating capacity, aggregate public expenditure, size of government fiscal operating balances; debt portfolio, unfunded liabilities and state of public infrastructure affect public financial performance. However, organizational factors encompass fiscal institutions; legislative policies, management practices, behaviour of public functionaries and of government employees. Also included under organizational factor are mismanagement, quality of public financial management institution, other political factors, transparency, and union power in public administration. Due to the above factor, the present study specifically considers impact of public financial management institutions, predicated purely on governance performance ratios to measure the soundness or weakness in public financial management and financial health of the Nigerian federal treasury. It is established that strong links exist between public financial management agencies, notably: fiscal institutions, that is, the public accounts committee of the legislature (FGN, 1999). Compliance to rules and external audit performance are some of the specific public finance

governance issues that affect financial performance / distress in public treasury in a democracy (FGN, Casal, et al.; Dabla-Norris et al).

Furthermore, the relationship between transparency in government corporate financial reporting, treasury management and good public governance has been well defined in 1998 by Kopits and Craig which argue financial transparency in a government entity presuppose “openness toward the public at large about government structure and functions, fiscal policy intentions, public sector accounts, and projections. This viewpoint is corroborated by Alt and Lassen (2006) which found that a greater transparency in government financial reporting is associated with lower annual budget deficits and public debts. Moreover, monitoring of fiscal transparency by other institutions has not been sufficient to prevent the substantial underreported deficits and debt in some advanced economies (by citizens, residents, stakeholders, trading partners and various user groups (IMF, 2010).

In essence, efficient and effective public fiscal management institutions influence sound public financial performance (INTOSAI, 2006). Effective financial accountability and transparency in fiscal reporting also provides legislatures, markets, and citizens with the information they need to make efficient financial decisions and to hold governments to account for their fiscal performance and their utilization of public resources. Finally, fiscal transparency facilitates international surveillance of fiscal developments and helps mitigate the transmission of fiscal spillovers between countries. On the contrary, inefficiency in public finance institutions encourage mismanagement of resources, poor financial performance and often cause public financial distress. Thus, the quality, characteristics and managerial behaviour of the public functionaries and management of government services as well as quality of the performance of the Supreme Audit Institution (SAI) in a sovereign entity impact either positively or adversely on the utilization of resources in public treasury (INTOSAI), public financial performance and ultimately, financial health. Thus, managerial inefficiency, ineffectiveness and or gross mismanagement of public financial resources can lead deterioration in fiscal capacity, formulation of unsuitable fiscal policies and financial decision whereby influence financial distress.

Public financial management institution is the dependent variable while dimensions of government financial performance are independent variables. Thus, to capture the effect of managerial efficiency and effectiveness of public financial management institutions in government performance and financial distress model in the five criteria, the following qualitative variables are attributes of management and governance related issues variables frequently used include: budget planning, approval and implementation timing lag; statutory audit-cum- government financial reporting timing lag; audit certification -external audit performance quality on reliability of financial reporting; quality of accounting services and the financial systems architecture; transparency in government financial reporting (openness, availability in the public domain, and accessibility).

### **2.3 Public Finance Management Institutions, Fiscal Governance and Performance Theory**

Some eclectic of theories corporate management underpinning impact of corporate financial governance, financial control system in public sector and managerial controls or organizational theory in performance measurement and management in government entities exist in literature. These include: the Code of good public governance, system theory and public auditing theory. These were drawn from the International Monetary Fund (IMF)'s 'Code of Good Practices and Fiscal Transparency' (2007); the World Bank's (2010) Principles of good public governance; Institute of Internal Auditors (IIA)'s Public sector governance (2011), International Federation of Accountants (IFAC)'s Good Public Governance (2013, 2015); System Approach Theory

(Dixit, 2012) cited in Kinua (2015). Kinua (2015) posits that the broad scope of accounting services alongside corporate financial reporting can be more sufficiently and appropriately utilized to formulate fiscal and macroeconomic policies in government entities.

Kittonen (2013) invoked pertinent theories of statutory auditing, notably: monitoring hypothesis, lending credibility hypothesis, inspired confidence hypothesis, agency hypothesis and information hypothesis) in situating the roles and importance of auditing service in corporate finance. Kittonen (2013) explains that public financial accountability is enhanced through statutory auditing and audit implementation in a government entity. Also, in the organizational theory of the new public management (NPM) recognizes that inefficient management of resources by managers is facilitated through rendition of asymmetric financial information (Jensen & Meckling, 1976). Drawing from rules-and-principles based accounting practices and corporate financial reporting in public sector, compliance to rules hypothesis has been added to theoretical framework of auditing in government entities. This brings number of core variants of eclectic theories of auditing applicable to government sector in existing literature to five.

Public corporate financial governance or public finance management institutional quality (PFMIQ) utilize the statutory external audit functions and the execution of routine internal audit and external auditing services in providing strong moderating influence or interface between audit assurance, financial accountability and stewardship financial reporting, transparency in government financial performance and financial distress (Kittonen, 2013). This is, in the sense that effective accountability supports fiscal governance principles, good public governance, prudence, financial information symmetry, and optimal resource utilization. According to Aruwa (2005) this performance measures links audit assurance, financial accountability and stewardship financial reporting, transparency in government financial performance. It also lends credence to the effectiveness of financial accountability and assesses the level of compliance of the federal MDAs extant public laws, fiscal governance rules, good public governance principles, and optimal resource utilization.

Statutory auditing services provided by independent external auditor to the sovereign governments. For example, the Comptroller / Head, the National Audit Office in the United Kingdom have provided effective interface that linked government-wide accounting services, financial reporting, sound public financial management performance with good governance (Bourns, 2012). In Nigeria, the office of the Auditor-General of the Federation (OAuGF) in collaboration with the National Assembly and Public Accounts Committee (PAC) administer the statutory audit functions and services for the federal treasury (Federal Government of Nigeria, (FGN), 2014). Similarly, in the jurisdictions that already adopted actionable governance metric, optimal resource utilization and remarkable reduction in poor financial accountability, in slack of audit independence, low external audit system in government sector, lack of credibility in financial reporting, and published annual financial statements (World Bank, 2010). However, there exist several factors that have encouraged financial information asymmetry and poor financial performance of government entities, efficiency in treasury management and macroeconomic performance (example growth with development) is the lack of transparency in financial reporting and non-compliance to fiscal responsibility reporting (IIA, 2011).

Managerial activities of the PFMI's encompass fiscal policy formulation, preparation of fiscal budgets, negotiation, adoption and implementation on one hand. Both the operating and strategic management of government finances are handled by public functionaries including bureaucracy, type and quality of accounting practices, financial reporting architecture, auditing and corporate financial reporting. Statutory auditing and external audit reporting is the final step in public finance management cycle and reporting chain. To conclude, the adverse information asymmetry theory propounded in Jensen and Meckling (1976), the incompatible

incentive of public office-holders hypothesis (using public resources for private gains) and erected in Altman and Hotchkiss (2010)'s modified Z-score represent the suitable framework for empirical model to measure impact of qualitative financial governance and financial performance in Nigeria's public treasury in this paper.

## 2.4 Review of Empirical Studies

Aikins (2012) research considered the impact of government's auditing processes on audit client management's adoption of audit report findings. Result showed that client management's adoption of audit recommendations is a function of auditors' professional designation, due diligence, client relations, and the agreed post-audit implementation plan. Results further indicated that clients management's adoption of audit reports is strongly influenced by professional due diligence as the auditors assessment of risks inherent in clients operation to determine the appropriate tests. Aikins (2012) confirmed that government auditors generally maintained independent reporting structure and exercise quality control over their work.

Wong (2012)'s thesis assessed the role and performance of audit committee in providing assurance and governance (public accountability) in the Victorian state's public sector in Australia. Results of the research indicated that the oversight functions and performance in the public sector of the Victorian State ensured compliance with the extant legislations on public financial management and audit; and the set of rules for the treasury. Kinua (2013)'s dissertation assessed the effect of "financial reporting practices" on quality of annual accounts in Kenya's government sector. Results established that fiscal budgeting as singular independent variable whose performance had significant consequence on quality of Kenya's government annual accounts. The results further revealed that expenditure appropriations alongside budget implementation performance, financial statements preparation and external auditing variables were not significant in influence quality of annual accounts. This empirical study demonstrated that there are direct linkages between institutional quality, budgeting, treasury management, financial reporting practices, preparation of annual accounts, annual external auditing, and compliance to public finance rules, governance and effective public financial management system.

Dabbla-Norris et al, (2010)'s paper establish the linkages between budget implementation performance, financial management and economic growth. Research result of findings, based on the constructed multi-dimensional indices provides preliminary empirical support that strong political and institutions with due compliance to rules accelerated economic growth. Bartlett (2016) dissertation evaluated the impact of "Government financial disclosures on the timeliness of the comprehensive annual financial reports (CAFR) in the USA states from 2005 to 2014. Results of model variables tested found that debt capacity, total revenues, population, credit worthiness rating, and statutory deadline for the states' financial reporting all had significant effect on when financial statements (CAFR) is issued.

Alt and Lassen (2006) which found that a greater transparency in government financial reporting is associated with lower annual budget deficits and public debts. This empirical finding is in tandem with the outcome of the IMF's report of monitoring of fiscal transparency and by other institutions has not been sufficient to prevent the substantial underreported deficits and debt in some advanced economies (by citizens, residents, stakeholders, trading partners and various user groups (IMF, 2010b).

Oghuma (2009) examined Nigeria's federal budgets, and the economic implication of misuse of unspent budgetary funds and its impact on effective implementation of government's annual budgets on fiscal planning. The paper finds that in some cases un-utilized budget funds – mostly for capital development programmes were misappropriated and shared by some government officers. This human behaviour hindered proper execution of capital project and plans and also

imposed serious constraints to the leadership of the executive arm of government from attainment of fiscal goals. These are some of the notable case of financial practices perpetrated in fiscal operations but uncovered by both routine audits and external audit services. Oghuma (2009) counselled that public officers to consider overall interest of the nation above individual interest; therefore enjoined public servants to ensure that budget disbursed for capital projects are effectively utilized. The author recommended that Nigeria's federal budget appropriation bills should be passed, adopted and implemented before the end of January every year; and that budget process adhered to by all state actors without inducements to towards personal benefits. The papers also recommended that project implementation monitoring units should henceforth be established to supervise execution of capital projects in the federal agencies.

Wynne (2016) examined the impact of government-wide financial reporting practices in the national treasury of eight countries in Sub-Saharan Africa (SSA). Result of the showed that out of the five indicative criteria of good financial accounting / reporting practices in the analysis, only timeliness was rated satisfactory while understandability, openness and consistency were unsatisfactory. Wynne's results further showed that out of the five indicative criteria of good financial accounting / reporting practices, only timeliness was rated satisfactory.

## **2.5 Limitations of the Reviewed Empirical Studies**

Most of the reviewed empirical studies did not include fiscal institutions or public financial management institutions and statutory external performance as governance performance criteria in their measures of financial performance and financial distress in sub-section 2.4. However, Alt and Lassen (2006) provided confirmation that fiscal institutions or institutional capacity, external audit quality assurance, compliance to legal regulation and transparency in government financial reporting exert strong influence on sound public financial management practice and good public governance. The omission governance variables in measures of financial performance might have contributed to some of the limitations observable in the results of prior public financial performances and financial distress studies in many climes.

## **2.6 Value Addition of the Study to Knowledge**

The paper adopts financial governance which most of the previous empirical studies consulted on public financial performance omitted fiscal governance variables in the model. Second, there is paucity of existing empirical study on Nigeria's public financial performance that adopted PFMI's quality as key governance indicators in the models. This is a major milestone and significant contribution to knowledge and public finance literature to be emulated by other researchers.

Furthermore, through inclusion of non-financial qualitative variables in evaluation of government financial performance omitted in prior studies create awareness of the leadership of authority of governments, public managers and external user groups' on deficiency in government-wide accounting, corporate financial reporting and financial management practices and in performance evaluation. An evaluation of government external auditing, assessment audit quality assurance as a measurement of stakeholders' confidence on public financial accountability, verification of the level of transparency in government financial reporting as non-financial qualitative variables to be built into public financial performance indexing is a veritable factor in gauging good public governance and prudence in treasury resource management in developing countries including Nigeria.

## **3 Research Methodology**

The research design and method used in development data adopted in the models, data collection, population, survey sample; in fiscal performance analysis, measurement and test of

hypotheses and other important information relating to the methodology of the research are presented in this section.

### **3.1 Research Design**

The paper adopted ex-post ‘facto’ empirical financial analysis and quantitative methods to utilize fiscal governance variables extracted from the Federal Government’s financial statements as metric in evaluation of the impact of corporate financial governance (mechanisms) on government financial performance of the federal treasury. Similar research design and methods were adopted in Kinua (2014) for Kenya; Casal, Gomez and Liste, 2014 in Spain; Carmeli, 2008) for Israel. The research instrument adopted in the process of data generating and collection is facilitated through content study of the FGN financial statements, domestic audit reports, budget documents and other pertinent information on compliance with legal regulations aspect of public financial management; external audit performance and audit reporting; audit reporting lags, effectiveness of public institutions to the management of Nigeria’s federal treasury. Usman and Anao (2015) posited that the longitudinal data survey method deals with data relating to different periods. Asika (1991) cited in Usman and Anao (2015) posits that despite the fact that time exists as variable, it should not be measured, but should rather be accepted as a factor responsible for variations in independent variables. Document content study with that archival data retrieval collection system are data collection procedure followed in extraction of relevant data sets utilized to derive fiscal aggregates of model.

### **3.2 Data Sources, Population, Sample Size and Method of Collection**

#### **3.2.1 Data Sources and Method of Collection**

The necessary annual time series were obtained from secondary data sources, exclusively from the FGN published official documents particularly Nigeria’s government annual financial statements, the approved annual appropriation bills, annual budget speeches delivered by the President, budgetary accounting and performance reports, and the Auditor-General of the Federation (OAuGF)’s domestic audit report and audited financial statements. In effect, the pertinent non-financial and governance variables were extracted from the Federal Government of Nigeria’s corporate financial reports for the relevant years covered in the study from the year 1999 to 2014 (both years inclusive) were used.

#### **3.2.2 Focal Institution, Population and Sample**

Nigeria is the focal institution in this study, which makes it a country specific analytical and evaluation study on corporate financial governance as drivers of government financial performance in a developing country. The research concentrated on Nigeria’s Federal Ministry of Finance and its financial management agencies since this federal ministry is statutory responsible for management of the sovereign treasury and government’s corporate financial reporting. Flowing from this perspective, with Nigeria as the sole unit of research, the population and sample of the study covered 16 consecutive financial years, representing 100 percent sample size in terms of the time frame with the Federal Government of Nigeria (FGN) the unit of research. Population of the research is guided by data availability on all the variables (fiscal aggregates) of the study.

#### **3.2.3 Data gathering and Method of Collection**

These include the pair-wise non-financial and corporate finance governance variables such as actual time spent on annual budget execution compared the number of normal standard days in fiscal year (365 days); actual time spent on statutory audit performance including preparation, approval and gazette of governments annual financial statements against the minimum statutorily permitted period (expressed in days or months). Another set of pair-wise variables is drawn from the actual number of clean audit opinion certificates or qualified audit opinion

issued for the total number of the evaluated financial years in comparison with the total years involved. Then, qualitative indices for the actual government-wide accounting practices alongside those of the financial reporting architecture and presentation pattern in comparison with the expected normal standard systems. The implementation of the international public sector accounting standards (IPSASs); accounting for fixed capital assets, current assets, current liabilities and public debt funds as well as faithful representation of such balance sheet items in the audited financial statements are used (IFAC, 2014). The pair-wise variable relating to transparency in government-wide financial reporting was premised on actual number of annual financial statements published in Nigeria's official web-site; and availability of the printed copies of such annual accounts in the print media, new-stands, and public libraries.

Data gathering for the study was facilitated through the document content study and archival data retrieval collection system which involved extraction of the necessary secondary data from official documents required in deriving the governance variables we adopted the analyses. The procedure was facilitated through the use of simple numerical ratios and derivation of the raw key non-financial performance indicators (KPI) which we used in the construction of financial performance index (FPI) in the models of the study. It is pertinent to state (here) that document content study / archival data retrieval method is the equivalence or the alternative approach to questionnaires as research instrument in primary data collection. This method is often adopted by researchers / analysts when data sets are obtained from published reports.

### 3.3 Model Specification and Development on Public Corporate Financial Governance

Corporate financial governance or public finance management institutions' (PFMIs) quality is dependent variable while government financial performance variables drawn from five sub-systems of managerial activities of the public financial management institutions constitute the independent variables. To analyze and realize the goals of the research objective, the qualitative governance variables incorporated in the models include; timing-lag in federal budget passage / implementation; timing-lag in statutory audit execution with issuance of government annual financial statements; statutory audit reporting quality assurance; government-wide accounting system with the financial reporting practices (Frap) and transparency in the rendition, distribution and availability of government financial reports in the public domain. These are the representatives of the independent variables (Xs) or the intervening control variables. Raw non-financial governance performance indicator derivable from these pair-wise government variables are utilized as predictors of financial performance index of this model (FPI). Predictor values of the financial prediction index FPI {(Y) (Z)} ranges from 0.01 to 0.99 or from one (1) percent to 99 percent is the financial parameter for measuring financial distress in this model of the study. Descriptions of model variables are provided in table 3.1.

The financial governance-oriented performance measurement empirical model in this paper is supported by the frameworks established by the International Internal Auditors (IIA)'s Guideline on Good Governance, (2012); International Monetary Fund's (IMF) (2007)'s Code of Good Governance and Kittenon (2013)'s 'Statutory Auditing Theory". Following a modified Altman's (1968); Altman and Hotchkiss (2010)'s modified Z-Score for developing countries and emerging markets; the CRAs (Fitch, 2014; Moody, 2014) financial performance index (FPI) rating score system now blended into a hybrid FPI model score-rating can be expressed as: is:

$$FPI = Z\text{-Score (Z)} = 0.5X1 + 0.50X2 + 0.50X3 + 0.05X4 + 0.50 X5 \quad (3.1)$$

Values of the predictor variables and financial performance indicators were converted to natural numerals using data transformation procedures such that the values ranges from 0 (zero) and 1.00 then, plugged in the developed financial distress index where the sum total is restricted and becomes one (FPI) or Z-Score = 1.

Composition and description of the qualitative governance variables used in model development are given as follows:

Models : Prefix of Variables, Symbols and Descriptions

Prefix	Code	Description of the performance indicators (ratios)
BPIT	X1	Budget Planning, Passage-cum-Implementation Timing-Lag
SART	X2	Statutory Auditing-with-Government Financial Reporting Timing-lag
SUAS	X3	External Audit Quality Assurance (Clean Audit/Total Reports)
FRAP	X4	Financial Reporting Accounting Practices (IPSAS as proxy)
TGFR	X5	Transparency in Government Financial Statements Reporting

Thus, the arrangement of the model equation function commences with econometric method, and subsequently, the multiple discriminant analysis (MDA) approach for the construction of the financial distress index (FDI) of the five model in the study is given as:

Econometric model development of qualitative governance of financial performance indices is

$$FPI = (Z) = a + B_0 + B_{pit} X_1 + S_{art} X_2 + A_{uas} X_3 + F_{rap} X_4 + T_{gis} X_5 + d + E \quad (3.2)$$

$$Financial\ Performance\ Index\ FPI = (Z) = W_1 * X_1 + W_2 * X_2 + \dots + W_n * X_n / n \quad (3.3)$$

Where: FPI or (Z) is a composite financial index and parameter to measure of model test  $W_1 * X_1 + W_2 * X_2 + \dots + W_n * X_n$  are the representative values of each non-financial governance performance indicators.

Decision criterion and interpretation: If FPI calculated is negative and  $< 0.50$  or 50 percent accept  $H_0$  and reject  $H_a$ ; but the FDPI is equal 0.50 (50 percent) and above positive, then, accept  $H_a$  and reject  $H_0$ . Hypotheses results are further categorized in line with the ordered performance.

## 4 Analysis and Results

### 4.1 Data Evaluation

In practice, time series data are often found to have the tendency to drift (trend) with passage of time, we tested for the presence of unit root in the model variables using the Augmented Dickey Fuller (ADF) and or Phillip-Peron (PP) techniques (Gujaranti & Sangetha, 2008), Johansen's or Geoffrey-Bresuch cointegration test were also implemented as part of data diagnosis as the check of stationarity. Furthermore, Wald and Dublin-Watson test were also performed to ascertain whether the selected governance variables used in our models were suitable for analysis and adoption in non-financial performance measurement metrics.

Unit root test for models 1, 3, 5 explanatory variables yield showed negative results at levels; whilst those in models 4 and 5 tested positive, were further differenced and normalized in order 1 (1). The control variables for timing lags in the partial regression analysis did not well fit into Breusch-Godfrey co-integration rank test testing due to zero variances. Since the paper developed static models that utilized the traditional non-monetary values in a ratio analysis for the qualitative governance performance indicators, it adopted these variables for the necessary analysis and tests. It is also pertinent to stress that in line with the principles of ex-post 'facto' analysis and measures used in the study did not require econometric estimation of future timing-lags, because our analyses were premised purely on past events only. Pair-wise fiscal governance variables of the models were statistically significant at 5 percent (0.05) significance level; Dublin-Watson tests fall below 2.4 level. Generally, results of these diagnosis checks and evaluation procedures undertaken established that the relevant pair-wise model variables were



suitable for use in analysis of financial performance and hybrid MDA / LR analysis and also fitted the model very well.

Summary of the relevant statistical analysis for the respective models are provided in the relevant tables for each model in the appendix pages (appendices).

## 4.2 Results of Analysis

The set of system equation to derive the impact of public financial management institutions on treasury management, financial management and financial distress in the federal treasury in MDA pattern in the first stage is expressed as:

$$FPI = (Z\text{-Score}) = W_1 * X_1 + W_2 * X_2 + \dots + W_n * X_n / n \quad (4.1)$$

$$FPI = (Y=1) = 1 / 1 + e^{- (B_0 + B_1 X_1 + B_2 X_2 + \dots + B_n X_n)} = 1 / 1 + e^{-Z_i} \quad (4.2)$$

$$FPI (Z) = (10.52X_1 * w_1) + (12.43X_2 * w_2) + (16X_3 * w_3) + (9.72X_4 * w_4) + (9.6X_5 * w_5) / 16\}$$

The re-arrangement of the above system equation into its LRM structure is given as:

$$FPI \text{ in LRM} = (Z\text{-Score}_5) = 1 / -1 \{f (0.65X_1) + (-0.78X_2) + (1.00X_3) + (0.61X_4) + (0.6X_5) / 5$$

Composite FPI result is 0.41 (41%); grade ('D') and fair but below average non-financial (governance) performance rating. Based on the result of analysis from performance measurement in this model's test,  $H_a$  is adopted for model one. This indicates is a fair and below average overall performance rating score.

The presentation of analysis results derived from the mapping of financial performance indicators of the pair-wise partial non-financial – governance ratios for the respective models are provided as follows:

(1) Result of analysis on budget planning, passage-cum-Implementation timing-Lag (BPIT-Model one) test result yield a non-financial performance indicator of  $0.65 > 0.50$  minimum cut-off mark for sound financial performance and solvency in the treasury. Thus,  $H_a$  is adopted. This result appears rather contradictory because Nigeria's federal budgets have been approved / assented around the second quarter of the fiscal budget year hence it is expected that delay in budget execution leads to poor performance. Empirical evidence in Hourerou and Taliero, (2002) and Gollwitzer, (2013) established that belated implementation of public budgets in some African countries resulted fiscal ineffectiveness and poor public financial performance.

(2) Result on statutory Auditing-with-government corporate financial reporting timing-lag (SART - Model two) record a non-financial performance indicator of  $- 0.75$  and a significant negative ratio far below  $0.50$  minimum cut-off points in the association between actual time spent and the constitutionally prescribed normal time frame for rendition of the Nigeria's annual financial statements.  $H_02$  was adopted in model two for the second objective. This result signifies that the belated issue of annual audit report and financial statements induced lack of financial accountability and suboptimal financial management system in the federal treasury and lead to financial distress.

(3) The analysis of the unqualified audit opinion as certificate of audit quality assurance by the government's independent external auditors by the Auditor-General of the Federation (OAuGF) in proxy of statutory audit quality assurance (model three); the result produced a performance indicator of a 100 percent and significant positive ratio that is above  $0.50$  minimum cut-off mark in the association between total actual clean audit opinion certifications (16 times for 16 annual financial statements).  $H_03$  was adopted for the third research objective.

(4) Performance appraisal on government accounting practices, financial reporting architecture and financial reporting system the test results produce 60 percent or  $0.60$  non-financial performance indicator. Therefore,  $H_04$  is adopted. This is an indication of a significant positive

in the association between the quality of government-wide accounting systems, financial reporting framework and financial reporting practices as a measure of public financial performance in Nigeria's federal treasury.

(5) The result of the performance evaluation on transparency in government financial reporting criterion of corporate financial governance yields 61 percent or 0.61 non-financial performance indicator. Based on this test result, Ho5 is adopted. This is an indication of a significant positive in the association between the quality of public finance management institutions and public financial performance in Nigeria's federal treasury. It implies that efficient and effective fiscal governance institutions is a major driver of transparency in government financial reporting which in turn leads sound public financial management system or practices in some countries.

### 4.3 Summary of Results of Analyses

Summary of results derived from the respective specified objectives and models are as follows:

(1) Result of analysis on budget planning, passage-cum-Implementation timing-Lag (BPIT-Model one) performance indicator of  $0.65 > 0.50$  and strong positive non-financial performance which supports solvency in the treasury.

(2) Result on statutory Auditing-with-government corporate financial reporting timing-lag (SART - Model two) record a non-financial performance indicator of  $-0.75 < 0.50$  and a significant negative ratio far below 0.50; a significant adverse non-financial performance which signifies that timing lags in the execution of statutory audit services and rendition of out-of-time corporate contribute to weak financial accountability with very high risk of the probability of inducing financial distress in Nigeria's federal treasury.

(3) On statutory audit quality assurance (SAUS in the third); the result produced a performance indicator of 100 percent  $> 0.50$ ; and the strongest significant positive ratio which is indication es that the issuance of unqualified audit opinion certificate, granting credence that the government financial reporting during the periods (16 times for 16 annual financial statements) are highly reliable. But this result is in conflict with the information in public domain and reported cases of missing funds in that treasury even though audit exercise does not detect fraud in at always.

(4) Performance appraisal on government accounting practices, financial reporting architecture and financial reporting system in model four (FRAP) the test results produce 60 percent or  $0.60 > 0.50$  non-financial performance indicator. Therefore, Ho4 is adopted. This implies that the quality of government-wide accounting systems, financial reporting framework and financial reporting practices support sound public financial performance in Nigeria's federal treasury. This is also debatable.

(5) The result of the performance evaluation on transparency in government financial reporting criterion of corporate financial governance (TGIS – the fifth model) yields 61 percent or 0.61 non-financial performance indicator and a strong positive performance. It implies that efficient and effective fiscal governance institutions is a major driver of transparency in government financial reporting which in turn leads sound public financial management system or practices in some countries.

Out of these five non-financial, governance performance indicators evaluated, statutory auditing-cum-financial reporting timing-lag produced the worst performance measurement indicators within the Nigerian government-wide accounting, financial reporting chain and treasury management practices. This arises from prolonged delays in completion, scrutiny, adoption and issuance (gazette) of FGN annual audit report and financial statements between the public accounts committee of the National Assembly and Supreme Audit Institution in Nigeria.

The overall composite financial performance index (FPI) the performance measurement on corporate financial governance or the impact of the public finance management institutions' quality on public financial management performance in the Nigerian federal treasury yield 41 percent which is lower than the 50 percent threshold we adopted as cut-off mark for solvency and stability. In effect, public finance management institutions dimension of government financial performance is a major causative factor for sub-optimal of financial performance in Nigeria's federal treasury.

The results of the papers is validated on the bases of the variety of data screening, estimation and evaluation procedures performed before the relevant data sets were utilized in the analyses and tests. In addition, the quality and plausibility of the analytical results hinge on exclusive use of secondary data from official documents obtained directly from government sources and also on predicated tenets of ex-post 'facto' research design where-in the outcome analysis are not manipulated, rather reproduced factually as there were. Finally, for the fact that the composite (non)-financial performance index (FPI) used as our corporate financial governance performance measurement metric produced below average and marginal weak governance grade, the result tell the bitter truth about the suboptimal nature and structure of the fiscal institutions and the prevailing operating in the federal treasury. The research findings are in agreement with available public information and reported cases of losses of public money. It is not useful in claiming that the public financial system is working properly whereas a reasonable large proportion of government funds have been found missing during the fiscal period of study.

## **5 Summary, Conclusions and Recommendations**

In this section, we present the summary of results, conclusions, policy implications, recommendations and suggestions for further studies.

### **5.1 Summary of Results**

The composite financial performance index (FPI) result yield of 41 percent; a grade 'D' in our governance (non-financial) performance rating is a clear demonstration that government financial management system is either inefficient and or that there still remains lingering deficiencies in Nigeria's fiscal governance hampering public performance and aggravating macroeconomic disturbances. This suggests that Nigeria's federal treasury is at risk of financial distress if adequate remedies to the situation are not urgently implemented. The detailed result of the five distinct models and representative of the objectives are synthesized as follows:

Summary of results derived from the respective specified objectives and models are as follows:

(1) Result of analysis on budget planning, passage-cum-Implementation timing-Lag (BPIT-Model one) show a strong positive non-financial performance and supports solvency in the treasury.

(2) Result on statutory auditing-with-government corporate financial reporting timing-lag (SART - Model two) show a significant negative ratio with significant adverse implication to induce weak financial performance as well as the prospect financial distress in Nigeria's federal treasury.

(3) On statutory audit quality assurance (SAUS) in the third); the result produced a performance the strongest significant positive ratio, indicative that the issuance of unqualified audit opinion certificate, granting credence that the government financial reporting during the periods (16 times for 16 annual financial statements) are highly reliable. However, this is misleading because it is in conflict with the information in public domain and reported cases of missing funds in that treasury even though audit exercise does not detect fraud in at always.

(4) Performance appraisal on government accounting practices; financial reporting architecture and financial reporting system in model four (FRAP) the result show a strong positive non-financial performance and supports solvency in the treasury.

(5) Similarly, the result of the performance evaluation on transparency in government financial reporting criterion of corporate financial governance (TGIS – the fifth model) also show a strong positive non-financial performance and supports solvency in the treasury.

The overall result of the composite financial performance for the study show a below average, fair and marginally weak (distress) in our (non)-financial government performance. This weak performance arises as a consequence of the worst performance measurement indicator recorded from our second research objective (SUART - model two) on statutory auditing and financial reporting timing-lag and weakest link within the government-wide accounting, financial reporting chain and treasury management practices for the Nigerian federal treasury.

## 5.2 Discussion of Results and Major Findings

(1) The result of obtained analysis in budget planning, passage-cum-Implementation timing-lag (BPIT) in Model one) show a strong positive non-financial performance and supports solvency in the treasury. This result is rather contradictory because Nigeria's federal budgets have been approved / assented around the second quarter of the fiscal budget year hence it is expected that delay in budget execution leads to poor performance. Empirical evidence in Hourerou and Taliero, (2002) and Gollwitzer, (2013) established that belated implementation of public budgets in some African countries resulted fiscal ineffectiveness and poor public financial performance. Oghuma (2009) examined Nigeria's federal budgets, and economic implication of misuse of unspent budgetary funds and its impact on effective implementation of government's annual budgets on fiscal planning. The paper finds that in some cases un-utilized budget funds – mostly for capital development programmes were misappropriated and shared by some government officers. This is un-disputable evidence that budgetary resource allocations for capital projects and socio-economic welfare services were not properly and fully utilized for the purposes for which they were disbursed.

(2) Result on statutory auditing-with-government corporate financial reporting timing-lag (SART) in the second model show a significant negative ratio with significant adverse implication to induce weak financial performance as well as the prospect financial distress in Nigeria's federal treasury. This signifies that the belated issue of annual audit report and financial statements induced lack of financial accountability and suboptimal financial management system in the federal treasury and lead to financial distress. This finding is in agreement with the Open Budget Initiatives (2012) report as cited in Petrie (2013) on 'budget management, accounting and engagement by the audit institutions and the legislature which indicated that is typically weak.

(3) We found that the result from model three to have produced the strongest significant positive ratio, indicative that the issuance of unqualified audit opinion certificate, granting credence that the government financial reporting during the periods (16 times for 16 annual financial statements) are highly reliable. This is an indication that the aggregate fiscal transactions capture in the operating financial statements, statement of cash-flows; the aggregate assets and liabilities, reflecting the financial position are reasonable and faithful representation of the financial affairs of the Federal Government of Nigeria in the national treasury. However, this is misleading because it is in conflict with the information in public domain and reported cases of missing funds in that treasury even though audit exercise does not detect fraud in at always. This is contradictory for several reasons. First, the capital expenditures used in acquisition of fixed capital assets were not duly captured in accounts. Second, there are several reported cases of leakages in government's duly collected revenues but not fully accounted for. This apparent

lack of financial information utility has trickling down effect to household or family units, business units and also government institutions as the trend erode public confidence in government financial reports except the annual budget in rational economic decisions.

Third, there are several cases of mismanagement of public fund and looting of public funds from the treasury which were not uncovered in through either the routine internal audit and or statutory audit functions. For example, Oghuma (2009) examined Nigeria's federal budgets, and the economic implication of misuse of unspent budgetary funds and its impact on effective implementation of government's annual budgets on fiscal planning. The paper finds that in some cases un-utilized budget funds – mostly for capital development programmes were misappropriated and shared by some government officers. This human behaviour hindered proper execution of capital project and plans and also imposed serious constraints to the leadership of the executive arm of government from attainment of fiscal goals. These are some of the notable case of financial practices perpetrated in fiscal operations but uncovered by both routine audits and external audit services. Oghuma (2009) advised that public officers to consider overall interest of the nation above individual interest; therefore enjoined public servants to ensure that budget disbursed for capital projects are effectively utilized. Whilst the Nigerian government and the same authorities also held these sets of financial statements in the right side of their hands; they are holding massive reports on massive leakages of federally generated revenues, misappropriation and management of public funds in the left ones or vice-versa. These developments can tell even the non-professional educated or trained people and concerned citizens is that these clean audit report might have been issued due to lack of audit independence or other unknown factors.

(4) The result in model four shows a strong positive non-financial performance and supports solvency in the treasury. This is an indication of a significant positive in the association between the quality of government-wide accounting systems, financial reporting framework and financial reporting practices as a measure of public financial performance in Nigeria's federal treasury. This implies that the level of the quality of government accounting and financial reporting is fairly good but suboptimal, thus there urgent need for improvement; the notable example is completion of implementation of the IPSASs new cash basis and accrual methods which is still a work-in-progress. Weber (2012), Hameed (2005) found that implementation of the IPSASs accounting systems in many countries have contributed very significantly in the improved financial reporting in some countries.

This result from this aspect of ex-post 'facto' is fair representative of the quality of financial, resource costing and management accounting practices followed in data capture of the Federal Government's financial transactions, fiscal operations, investments, fixed capital assets and public debts or repayable liability funds held in the federal treasury. It also reflects the financial reporting architecture as well as the quality of information content of the Nigerian federal general purpose consolidated financial statement rendered during the affected fiscal years. For instance, the old cash basis method followed in Nigeria's government accounting, thus, virtually all capital expenditures included within these 16 financial years from 1999 and 2014 were not captured in the financial accounting records, therefore the values of such fixed assets were not represented in the relevant financial statements. In the related arrangement, although the new International Public Sector Accounting Standards (IPSASs) has been adopted by Nigeria, both the new IPSASs cash basis method; the IPSASs prescribed accrual accounting method and treasury single accounting were all contemplated but there were not yet implemented and neither used in the preparation of the financial reporting we used in the analysis of this research.

The existing government accounting, budgetary reporting and corporate financial reporting in the federal treasury is not in harmony with the current international regime and therefore at variance with best practice in government accounting. This research finding is in agreement

with empirical evidence provided in Babatunde (2013) that accrual accounting enhances the quality of government accounting and public financial management systems in Nigeria. Babatunde (2013) already confirmed that accrual budgeting and government accounting have not taken roots in Nigeria's public sector.

(5) The result of corporate financial governance (TGIS – the fifth model) also shows a strong positive non-financial performance and supports solvency in the treasury. This is an indication of a significant positive in the association between the quality of public finance management institutions and public financial performance in Nigeria's federal treasury. It implies that efficient and effective fiscal governance institutions is a major driver of transparency in government financial reporting which in turn leads sound public financial management system or practices in some countries. Hameed (2005), Dabla-Norris and others (2010) earlier found that the developing countries that implemented / achieved greater transparency in their fiscal reporting recorded better credit ratings and better fiscal discipline in their sovereign treasury. This is further supported by Alt and Lassen (2006) which established that a greater transparency in fiscal reporting has been associated with lower public debts and budget deficits in 19 advanced countries. Given this governance performance rating on transparency in fiscal reporting, Nigerian government is expected to step up the quality of her external auditing, corporate financial reporting, accountability, open access and distribution of the published annual financial statements.

However, there are some remarkable corporate financial governance practices of our contemporary times which we have found to be conspicuously missing in Nigeria's government financial reporting practices. The most important one is the non-adoption of internet financial reporting in the federal treasury's financial reporting. It is only the authority of the federal treasury that can provide genuine reasons for this omission. Second, copies of Nigeria's FGN annual financial statements are rarely found in the University libraries, in New-stands, and other public libraries for the citizens, stakeholders and other interested parties to obtain the copies for their use. The scarcity or non-availability of government financial statements is a contradiction of international convention of the modern public financial management system; then, Nigeria's Freedom of Information Act, 2011, Fiscal Responsibility Reporting Act, 2007 and the World Banks / IMF's Code of Good Public Governance among other things.

The deficiencies identified in the public corporate financial governance or public finance management institutions' quality constituted significant sub-optimal moderating factors on Nigeria federal treasury management, and impact negatively on financial performance. In actual fact, corporate financial governance is one of the major influencing factors responsible for mismanagement of public funds, corrupt practices with great prospect of driving the entire government sector of Nigeria's economy into a state of financial distress.

The overall result of the composite financial performance for the study show a below average, fair and marginally weak (distress) in our (non)-financial government performance. This weak performance arises as a consequence of the worst performance measurement indicator recorded from our second research objective (SUART - model two) on statutory auditing and financial reporting timing-lag for the Nigerian federal treasury. This signify that Nigeria's sovereign treasury can be considered in a marginally financial distress position or risk of fiscal distress based strictly on this criterion of financial governance alone. It is correctly in correspondence with the prevailing development in the Nigerian financial management space as highlighted in the discussion of research results and deliverables. This is due to prolonged delays in completion, scrutiny, adoption and issuance (gazette) of FGN annual audit report and financial statements between the public accounts committee of the National Assembly and Supreme Audit Institution in Nigeria.

Research findings of the study has demonstrated that managerial behaviour and governance issues including government financial reporting practices in Nigeria's federal public service did not support positive public performance and sound public financial accountability, rather it enhance the prospect of financial distress. This is an indication of a high probability of financial distress in Nigeria's federal public sector, if appropriate measures are adopted to reverse the existing trend. Thus, the result of this paper can be justified on grounds of the publication of audited account and reports in most cases two years after year end which encourages both deliberate financial information asymmetry, mismanagement of public funds and corruption.

### 5.3 Conclusions and Implications for Policy

The prevailing trend of belated passage and implementation of the annual budget appropriation bills also induce ineffectiveness fiscal operations and financial performance which can contribute to fiscal distress in the economy. The only sub-performance indicator on audit certification of financial statements (clean audit report) used proxy for audit quality assurance that yielded a strong significant performance. The efficacy of this sub-index result in this model is highly deceptive and debatable because it is at variance with performance indicators from other governance variables within model due impaired public trust and confidence in FGN's government financial statement, judging from the avalanche of reported cases of misappropriation of public funds, fraud and the purportedly recovery of looted funds in recent times.

Policy implications of the empirical results of this study which in effect identified the institutional (PFMIs) quality as the weakest link in Nigeria's federal treasury and public financial management chain is a scientific demonstration that mismanagement of public resources, citizenship or service level distress, impaired economic growth and development are deeply rooted in the managerial behaviour and human side of public management. This is a clear demonstration that government financial management system is either inefficient and or that there are inherent deficiencies in Nigeria's fiscal governance that still lingering on and hampering public performance and aggravating macroeconomic disturbances.

### 5.4 Recommendations

Following recommendations are proposed for policy intervention:

(1) The relevant financial arms of government and financial authorities including the PFMIs should ensure that federal annual budget bills is approved and assented and implemented as from the first week of every fiscal year. This means that the budget process should always be completed before the Christmas week and before the commencement of the new fiscal years and incoming fiscal budget period. In addition, Federal Government is advised to establish an independent, non-political and non-partisan 'Fiscal Council to supervise the nation's federal budget system that will be rancor free.

(2) Statutory auditing time schedule, external audit execution, oversight activities, final approval and publication (gazette) should be completed, reviewed, approved, gazette and circularized within the stipulated nine months' time-frame after year-end under the existing law and within six months under the proposed new audit regime in this paper.

Under the proposed structure, the service of Office of the Auditor-General of Federation is retained as the coordinating comptroller of government and head of the federal audit services commission. Second, a statutory board of the Court Audit Scrutinizers or Governors should be constituted by eminent persons to be made of accomplished professional accountants; professionals from other fields, distinguished academics with strong background in public treasury and finance management should be assembled. The body will carry-out the oversight

scrutiny and final approving authority of government external audit function thus a replacement of the PAC.

(3) Certification of the statutory annual audit report and financial statements of the FGN should be not appearing as a rubber stamping action; therefore, the responsibility for final scrutiny and approval should be separated from the legislative body that approves the annual appropriation currently residing with the PAC in the spirit of segregation of authority.

(4) Fourth, the FGN's government-wide accounting system, financial reporting architecture together with both internal control, internal auditing, and statutory audit performance, preparation and presentation of financial statements should be comprehensively restructured, strengthened and modernized in line with the IPSAS and accrual accounting and rules-based accounting regime.

(5) Lastly, the Federal Government is advised to adopt internet financial reporting henceforth as a medium of enhancing transparency in the preparation and presentation its financial statements; and making it readily available and accessible in the public domain as it is the practice in many countries.

### **5.5 Limitations to Implementation and Realization of Results and Deliverables of the Paper**

Inadequate fiscal revenue generation, financial constraints, lack of prudence in public expenditure management and financial information asymmetry phenomenon of the public sector agency theory are some of the common factors that may likely constitute major impediments or severe limitations on the implementation of the recommended policy measures of this study. Furthermore, institutional quality the political audacity in getting the right things done in Nigeria and other developing countries also constitute major limiting factors.

### **5.6 Suggestions for Further Research Studies**

More empirical studies need to be conduct to further investigate the impact of institutional factors on public financial management and macro-economic disturbance in Nigeria. Such research activities will help the financial authorities and fiscal policy makers of the Federal Government of Nigeria to obtain useful and reliable research information formulate suitable public policies for more efficient and effective government financial management systems and practices in the federal treasury. Furthermore, intensive and extensive empirical investigations and analyses of the impact of financial management institutions in Nigeria will enthrone the regimes or rules-plus-principles based government accounting, public treasury management and good public governance in the Nigerian fiscal space.



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## Appendices

### Unit Root Test and Co-Integration Analyses with Results

<b>Model 5.1: Public Budget Passage + Implementation Timing-Lag</b>			
Variables	Levels	1 <sup>st</sup> Diff	Status
LOST_TIME	-5.343820* (0.0003)	-3.999581	I(0)
STANDARD TIME	-5.359661	-8.691461*(0.0000)	1(1)

<b>Model 5.2: Statutory Auditing &amp; Financial Reporting Timing-Lag (SAFR)</b>			
Variables	Levels	1 <sup>st</sup> Diff	Status
Delay in Financial Reporting (Months lost)	-3.236089	-5.091856* (0.0007)	I(1)
Minimum Required Standard Reporting Period (In Months)	-4.708805*(0.0005)	-4.693477	1(0)

<b>Model 5.3: Audit Quality Assurance in Annual Audit Reporting (SUAS)</b>			
Variables	Levels	1 <sup>st</sup> Diff	Status
Actual Clean Report	-2.608945	-4.185690* (0.0004)	I(1)
Standard Reports	-5.880522*(0.0006)	-3.934776	1(0)

<b>Model 5.4: Government-Wide Accounting System-Financial Reporting Practices (FRAP)</b>			
Variables	Levels	1 <sup>st</sup> Diff	Status
G-w FRAP Annual Rating	-3.582062*(0.0116)	-3.099960	I(0)
Total Audit Reports	-2.189654	-6.846637 (0.0000)	I(1)

<b>Model 5.5: Transparency in Government Financial Statements (TGIS)</b>			
Variables	Levels	1 <sup>st</sup> Diff	Status
Ranking of TGIS Actual Annual Access	-4.304492*(0.0010)	-3.785433	I(0)
Total (16) Annual Financial Statements	-0.982578	-4.529432*(0.0062)	I(1)

**Model 1 : Unrestricted Cointegration Rank Test (Trace)**

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value
None	0.459865	8.623111	12.51798

Trace test indicates no cointegration at the 0.05 level  
 \* denotes rejection of the hypothesis at the 0.05 level  
 \*\*MacKinnon-Haug-Michelis (1999) p-values

**Model 2: Unrestricted Cointegration Rank Test (Trace)**

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value
None	0.415452	7.516819	12.51798

Trace test indicates no cointegration at the 0.05 level  
 \* denotes rejection of the hypothesis at the 0.05 level  
 \*\*MacKinnon-Haug-Michelis (1999) p-values

**Model 3: Unrestricted Cointegration Rank Test (Trace)**

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None	0.142638	2.154530	3.841466	0.1421

Trace test indicates no cointegration at the 0.05 level  
 \* denotes rejection of the hypothesis at the 0.05 level  
 \*\*MacKinnon-Haug-Michelis (1999) p-values

**Model 4: Unrestricted Cointegration Rank Test (Trace)**

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.652897	14.81389	12.51798	0.0203

Trace test indicates 1 cointegrating eqn(s) at the 0.05 level  
 \* denotes rejection of the hypothesis at the 0.05 level  
 \*\*MacKinnon-Haug-Michelis (1999) p-values

**Model 5: Unrestricted Cointegration Rank Test  
(Trace)**

Hypothesized	Trace	0.05		
No. of CE(s)	Eigenvalue	Statistic	Critical Value	Prob.**
None	0.524281	10.40098	12.51798	0.1101

Trace test indicates no cointegration at the 0.05 level

\* denotes rejection of the hypothesis at the 0.05 level

\*\*MacKinnon-Haug-Michelis (1999) p-values

*Data Sources: FGN – Audited Annual Financial Statements (1999-2014) and Domestic Reports*

*E-Views 8 is the analysis software system package used in processing of analytical results.*

**MODEL 1: PUBLIC DEBT AND REVENUE STATISTICAL ANALYSIS**

Dependent Variable: REVENUE

Method: Least Squares

Date: 07/16/17 Time: 11:54

Sample: 1 16

Included observations: 16

Variable	Coefficient	Std. Error	t-Statistic	Prob.
TOTAL_DEBT	0.404255	0.166992	2.420799	0.0297
C	92.71778	901.3470	0.102866	0.9195
R-squared	0.295075	Mean dependent var	2173.355	
Adjusted R-squared	0.244723	S.D. dependent var	1249.632	
S.E. of regression	1086.014	Akaike info criterion	16.93488	
Sum squared resid	16511964	Schwarz criterion	17.03146	
Log likelihood	-133.4791	Hannan-Quinn criter.	16.93983	
F-statistic	5.860270	Durbin-Watson stat	0.345322	
R	0.54321			
Prob (F-statistic)	0.029662			

Breusch-Godfrey Serial Correlation LM Test:

F-statistic	11.68621	Prob. F(2,12)	0.0015
Obs*R-squared	10.57204	Prob. Chi-Square(2)	0.0051

## MODEL 2: EXTERNAL DEBT-TO-EXPORT REVENUE SUSTAINABILITY STATISTICS

Dependent Variable: REVENUE(2)

Method: Least Squares

Date: 07/16/17 Time: 12:25

Sample: 1 16

Included observations: 16

Variable	Coefficient	Std. Error	t-Statistic	Prob.
EXT_DEBT	-2.353100	0.646093	-3.642043	0.0027
C	12705.13	1622.502	7.830579	0.0000
R-squared	0.486511	Mean dependent var	7932.750	
Adjusted R-squared	0.449834	S.D. dependent var	5159.839	
S.E. of regression	3827.218	Akaike info criterion	19.45413	
Sum squared resid	2.05E+08	Schwarz criterion	19.55071	
Log likelihood	-153.6331	Hannan-Quinn criter.	19.45908	
F-statistic	13.26448	Durbin-Watson stat	0.449441	
R	0.69750			
Prob(F-statistic)	0.002667			

$$\text{REVENUE2} = 12705.13 - 2.353100 (\text{EXT-DEBT})$$

Wald Test:

Equation: Untitled

Test Statistic	Value	Df	Probability
t-statistic	-3.642043	14	0.0027
F-statistic	13.26448	(1, 14)	0.0027
Chi-square	13.26448	1	0.0003

### Model Diagnostic Checking

Breusch-Godfrey Serial Correlation LM Test:

F-statistic	6.685460	Prob. F(2,12)	0.0112
Obs*R-squared	8.432281	Prob. Chi-Square(2)	0.0148



### MODEL 3.3: TOTAL PUBLIC DEBT AND GDP SUSTAINABILITY STATISTICS

Dependent Variable: GDP  
 Method: Least Squares  
 Date: 07/16/17 Time: 12:14  
 Sample: 1 16  
 Included observations: 16

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DEBT	13.52781	3.134096	4.316336	0.0007
C	-37894.20	16916.40	-2.240087	0.0418
R-squared	0.570957	Mean dependent var	31731.38	
Adjusted R-squared	0.540311	S.D. dependent var	30062.09	
S.E. of regression	20382.21	Akaike info criterion	22.79918	
Sum squared resid	5.82E+09	Schwarz criterion	22.89575	
Log likelihood	-180.3934	Hannan-Quinn criter.	22.80413	
F-statistic	18.63076	Durbin-Watson stat	0.622382	
R	0.75562			
Prob(F-statistic)	0.000711			

$$\text{GDP} = -37894.20 + 13.52781 (\text{DEBT})$$

Wald Test:  
 Equation: Untitled

Test Statistic	Value	df	Probability
t-statistic	4.316336	14	0.0007
F-statistic	18.63076	(1, 14)	0.0007
Chi-square	18.63076	1	0.0000

#### Model Diagnostic Checking

Breusch-Godfrey Serial Correlation LM Test:

F-statistic	5.456254	Prob. F(2,12)	0.0206
Obs*R-squared	7.620297	Prob. Chi-Square(2)	0.0221

# Issues of Implementation of Accruals-Based Accounting in Public Sector (The Case of Ukraine)

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## Abstract

The article stresses that the general trend in public sector accounting reform consists of alignment of its methodology to corporate accounting approaches. In this case the implementation of accruals-based accounting is crucial. The following issues of implementation of accruals-based accounting in public sector are studied: the absence of proper measurement and recognition in accounting and reporting of all assets and liabilities of state (including all rights owned by the state, all natural resources that make a state asset and property, pension liabilities of state, etc.); uncertainty about the moment of recognition and measurement of revenue from paid taxes. The authors prove the necessity for development and implementation of IPSAS “Expenses” as the methodological guidance for accounting for public entities expenses, including expenses from exchange transactions, in particular for the providing of public services.

## Accrual Accounting Implementation: Ukraine Experience

The reform in public sector accounting is the element of general reform process of Public Finance Management system (PFM) according to the Strategy of Reforming of Public Finance Management till 2020 adopted by the Cabinet of Ministers of Ukraine this February (Cabinet of Ministers of Ukraine, 2017).

One of the innovations of this reform is the application of accruals-based accounting by budget entities, state and local budgets execution. Despite the advantages of this accounting method, its application at the budget execution level is a difficult process.

The general trend in public sector accounting reform consists of alignment of its methodology to corporate accounting approaches. This is caused, on the one hand, by the progress and development of conceptual approaches and methodological techniques developed in corporate accounting methodology, and, on the other hand – by the willingness to provide users of financial and budget reporting with the information, which can become the efficient basis for decision-making process on the state level.

There are two accounting models for recognition of revenue and estimation of financial performance (results) in international and national practice. The first model is cash-based accounting (revenue is recognised when cash from sale of goods and services is received). The second model is accruals-based accounting (revenue is recognised after transfer of ownership on goods and services). The financial result according to accruals-based accounting is recognised on the basis of matching costs and revenues regardless of the receipt of proceeds from sales.

Historically, the cash-based accounting preceded the accruals-based accounting. Its absolute advantages relate to full correspondence of recognised revenue with its cash equivalent on the bank's current account. In terms of private individual property, the profit indicator, estimated with the cash-based method, is absolutely relevant (in this context it is informative and useful for financial decision-making).

Joint-stock ownership requires accounting the profit indicator that reflects the efficiency of the entity's activity. The profit of joint-stock company, on the one hand, characterizes the investment attractiveness of entity; on the other hand, it is a part of revenue distributed between owners. In this case it is important to remember that this indicator has to be published. It can be calculated only with the help of accrual method.

It should be noted that the accruals-based accounting is one of the principles on which the contemporary accounting system is based. This provision is declared in the international standards as well as in the national (Ukrainian) and in the Law of Ukraine "On Accounting and Financial Reporting in Ukraine" (the Law of Ukraine, 1999). It is formulated as the principle of accrual and matching costs and revenues (accrual basis of accounting). In accordance with this principle, financial result is estimated by comparing of annual revenues with expenses, incurred while obtaining revenues. Revenues and expenses are recorded at the moment of their recognition regardless of the cash receipt. Thus, the consequence of the application of this principle is the separation of cash flows from the process of generating of financial results. From the point of view of economic nature of reproduction of capital, such approach is justified, since it enables to identify changes in the structure and amount of equity during the reporting period. At the same time, in order to enforce the real value indicator of financial result in terms of its separation from cash flows, the accounting system was enriched by other principles that serve as certain limitations for accrual accounting. In particular, these principles include prudence (conservatism) and substance over form (materiality).

Let's consider the issues of implementation of accruals-based accounting in public sector.

The application of accruals-based accounting in public sector envisages the measurement, recognition and presentation in reporting of all assets and liabilities of the state. Not only property, plant and equipment, tangible and other current and non-current assets are the objects now, but also all intangible assets. These intangible assets include all rights owned by the state, all natural resources that make state asset and property, pension liabilities of the state. This information is of great importance for decision-making process at state level.

At present, not all assets and long-term liabilities of budget entities are subject to real assessment. In particular, the cost acquiring fixed assets is written off on appropriate funding resources without further depreciation.

In addition, there are problems with the transition of the formation of budget revenues accounting from paying taxes to accruals-based accounting. The state requirements to taxpayers may arise at the moment of receipt of tax return by the State Fiscal Service or when the taxpayer committed the action, the result of which is the obligation to pay tax. The assessment of such transactions makes the difficulty of accruals-based accounting. The general advantage of this method is the reliability of reporting from the point of view of the economic content of its indicators/items.

The abovementioned problems lead to the use of the modified cash-based and modified accruals-based accounting in public sector.

Reference: The assessment of expenditures and revenues in accordance with accruals-based accounting also affects the assessment of assets and liabilities.

The modified cash-based method in accounting for state debt involves the fixing of cash flows, while recognizing the state debt and loans is carried out by accruals-based accounting. This method is also applied while recognizing other settlement, the need for which arises during the budget execution process. Some assets and liabilities, other than mentioned above, affect the liquidity and solvency of the state, therefore, they are assessed by the accrual-based accounting.

The modified accrual-based accounting is applied for assessment of assets and liabilities. At some point of its implementation it became clear that this method cannot provide the ability to assess the above mentioned accounting objects reasonably. The modified accruals-based accounting is applied as transitive, in order to create necessary conditions for implementation of full accruals-based accounting. For example, the implementation of accruals-based accounting of fixed assets depreciation requires the recognition by fair value, determination of useful life of such assets by groups. Taking into account the condition of fixed assets in the public sector, it can be concluded that this process requires a lot of organizational work, methodological preparation and time.

Comparison of accruals-based and cash-based accounting indicates the predominance of the first method. This method is more progressive. Under the accruals-based accounting the transactions are recognized at the moment of fulfillment or change in economic value of assets or liabilities.

The statement of budget execution in accordance with the budget legislation of Ukraine is prepared on cash basis. The content of this statement reflects cash flows: revenues and expenditures, funding sources for deficit. This reporting is public, in fact, that is the reporting on government transactions.

The research showed the lack of clarity and uniqueness of the theoretical substance and practical application of different methods of recognition of revenues and expenses in public sector of Ukraine. This also applies to legislative support of this issue. Unlike the “cash-based” and “accruals-based” accounting, terms “modified cash-based” and “modified accruals-based” accounting are not used either theoretically or in practice. The application of cash-based accounting is indicated only in one legislative act. The mechanism for its application is not specified.

The transition to accruals-based accounting cannot be the one-stage process and needs long period. For this period, it is necessary to apply the modified accruals-based accounting with the preservation of cash basis. This should be taken into account while carrying out the public sector accounting in budget entities of the state.

The gradual application of accruals-based accounting in public sector of Ukraine will allow the transition to medium-term budgeting, and control the flow of any assets and liabilities as well as take into account cash balances.

One of the reasons of the difficult way of implementation of accruals-based accounting into practice of public entities is a lack of methodological guidance provided by IPSAS on accounting for expenses (including expenses from exchange transactions, in particular, providing of public services). Actually, the IPSAS package doesn't include the Standard "Expenses" as well as it is not present in the IFRS package. However, the absence of IFRS "Expenses" is due to concept of determining of corporation's financial results and economic nature of non-governmental property: all spendings and outflows from the entity of resources are recognized as expenses.

In the public sector the state is an owner of capital that is the basis of formation of budget entity. Therefore, economic essence of public entities' expenses in these terms acquires a slightly different meaning. Thus, expenses of public entity arise from events, the settlement of which expected to result in an outflow from the entity of resources and increase of obligations. But because the financial resources of the state are spent, the purpose-oriented character of the resources use, social and economic effect of such use is important. The methodology of planning and accounting for expenses of providing public services and its cost calculation is of great importance. The reliable indicator of public services cost is a basis for substantiated defining of the amount of budget funding of public entity's activities.

We consider it relevant to discuss the development of a particular IPSAS “Expenses” or an appropriate consultative document. Such standard is developed in Ukraine: National Public Sector Accounting Standard (Provision) 135 “Expenses” (NPSAS(P)). Difficulties that arise while implementing this process emphasize its significance. Its structure and content can be taken as a basis for the development of relevant international standard.

NPSAS(P) 135 “Expenses” has the following structure:

1. General provisions
2. Classification of expenses
3. Recognition and measurement of expenses
4. Cost of products and services
5. Disclosure of information on expenses in Notes to Financial Statements (the Ministry of Finance of Ukraine, 2012).

At the same time taking into account the IPSASB initiative for the development of Consultation Paper “Accounting for Revenue and Non-Exchange Expenses” issued by IPSASB (the proposals on application of revenue recognition model proposed by IFRS 15 “The Revenue from Contracts with Customers”) and the outcomes of discussing it by the Ad Hoc Committee on International Accounting Standards ICGFM, we suggest the following structure of IPSAS “Expenses”:

1. General provisions
2. Classification of expenses in public sector
3. Recognition and measurement of expenses from non-exchange transactions
4. Recognition and measurement of expenses from exchange transactions
5. Cost of products and services
6. Disclosure of information on expenses in Notes to Financial Statements.

The mechanism of formation of public services cost on the example of state higher educational institutions is presented on figure 1.

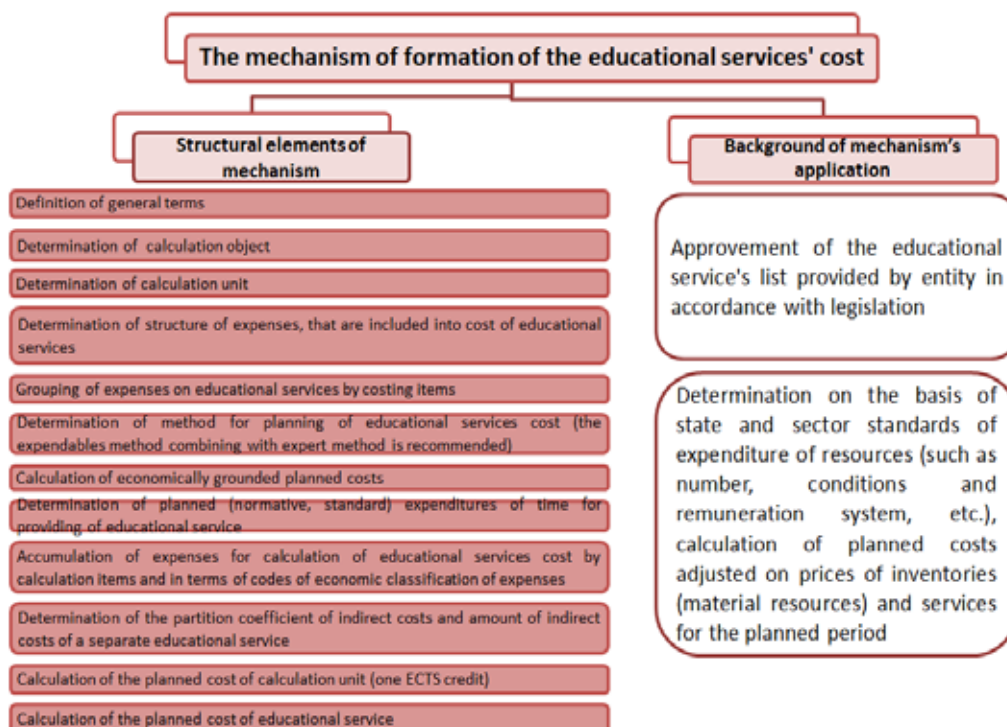


Figure 1. The mechanism of formation of the educational services' cost

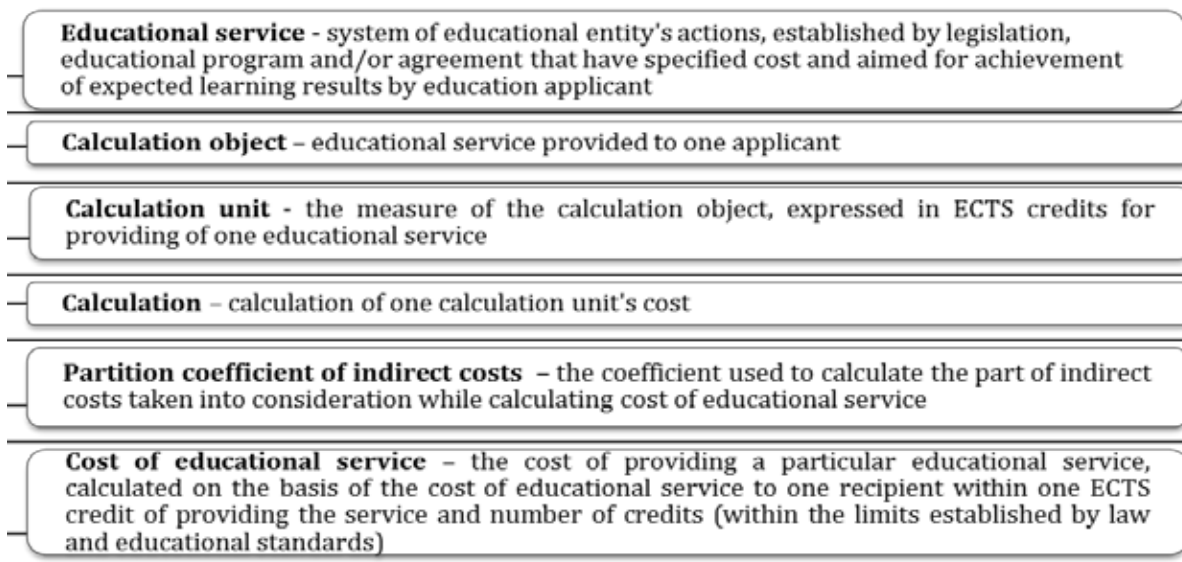
In Ukraine, for a long period of time, there was no necessity to determine the cost of public services. Budget entities receive budget funding and spend it in accordance with approved cost estimate for the completion of relevant activity.

It is widely-known that when budget is allocated only on the basis of functional and economic classification of expenses then budget is a summary of data on general categories of expenses. In this case budget doesn't contain any information about target and potential impact of expenses. Thus, such a methodology doesn't establish the clarified link between spent resources and results received. Moreover, such allocation doesn't make it possible to determine the efficiency and successfulness of funded services.

In this case, the general purpose of funding is the maintenance of the net of historically formed institutions. In fact, the target for budgeting is to become the quantity and quality of the service obtained by the customer from the provider.

Taking into consideration the information mentioned above, it is topical to achieve a definite, usually long-term, result that meets the needs of society. Thus, financial results should be assessed in terms of delivery of services results. That is, budget entities need to calculate the cost of services provided by these institutions in accordance with legislation. The structural elements of mechanism and implementation precondition for the formation of public services' cost is presented on figure 1.

Definition of the general terms and approaches to formation of planned cost of educational service is presented on figure 2.



**Figure 2. Definitions of the general terms and approaches to formation of planned cost of educational service**

Under the cost of services it is necessary to understand the amount of spending of budget entity directly related to providing of public services. In accordance with the Law of Ukraine “On education” dated September 5, 2017 № 2145-VIII the definition of category “educational service” is the following: “educational service – system of educational entity's actions, established by legislation, educational program and/or agreement that have specified cost and aimed at achievement of expected learning results by education applicant”.

Cost is the basis of public services pricing. Estimation of the public service cost is calculation. The reliability of the calculation in many cases depends on choice of items of expenses, accounting for expenses object and calculation, calculation units, methods of distribution of indirect expenses.

Difficulty of determining of calculation items on providing of services by budget entities consists in multiple nature of activity of these entities. However, these issues can be solved at the level of sector ministries with the involvement of practitioners to methodological work.

The types of homogeneous services are the object of accounting for expenses. Calculation object is a separate type of public service provided in accordance with legislation.

The objects of calculation are closely related to the concept of calculation unit that is measure of product taken for estimation of the relevant calculation object.

In order to determine the cost the appropriate calculation of services method is used. That is a set of methods for mapping, grouping and aggregation of data on expenses for providing services in accounting that ensure the determination of actual product cost. Such methods can include direct-costing and standard-costing. However, unlike material production (issue of accounting for expenses of this production is developed in detail and reasoned way both from the theoretical and practical sides) the methodology of accounting for expenses and calculation of services of budget entities is at the initial stage of development.

In addition, there is a need for harmonization of calculation items with the codes of economic classification of expenses that are the general indicator for regulation and enforcement of planning and spending of budget entities.

The connection between calculation units of planned cost of educational service and codes of economic classification of expenses are presented on figure 3.

<b>STRUCTURE OF EXPENSES</b>	<b>CALCULATION ITEMS</b>	<b>CODES OF ECONOMIC CLASSIFICATION OF EXPENSES</b>	
<b>DIRECT EXPENSES</b>			
<b>Direct expenses on wages and social contributions</b>	Wages	2111	Wages
	Social contributions	2120	Social contributions
<b>Direct material expense</b>	Materials and services	2210	Inventories
		2240	Settlement for services (except utility services)
<b>Other direct expenses</b>	Other direct expenses	2210	Inventories
		2240	Settlement for services (except utility services)
		2250	Expenses on business trip
<b>INDIRECT EXPENSES</b>	Indirect manufacturing expenses		
<b>Wages and social contributions of administrative, economic, managerial, service personnel</b>		2111	Wages
		2120	Social contributions
<b>Indirect material expense</b>		2210	Inventories
<b>Payment of business trips for those employees</b>		2250	Expenses on business trip
<b>Depreciation of fixed assets and intangible assets of general purpose</b>			
<b>Maintenance, operation and repair of fixed assets, other fixed assets of general purpose</b>		2240	Settlement for services (except utility services)
<b>Payment for heating, electricity, water, wastewater, natural gas and other energy</b>		2270	Settlement for utility services and energy

**Figure 3. The connection between calculation units of planned cost of educational service and codes of economic classification of expenses**

In order to sum up, it should be noted that implementation of accruals-based accounting as the element of public finance system reform (in particular, the implementation of program-target method into the budget process) requires the restructuring not only the accounting and reporting areas, but also planning and management systems. This can be proved by the next argument. The grouping of expenses related to cost of services and, consequently, efficiency indicators of budget program (cost and product indicators) can be carried out in accordance with requirement of IPSAS “Expenses”.

Public sector financial reporting, prepared with accruals-based accounting, will enhance the level of public awareness of the realized economic policy and strengthen public confidence in Government.

The application while preparation of reporting with accruals-based accounting of understandable for users’ format (that is similar to those, provided by commercial sector) will



enhance the transparency of public sector activity, investments and commitments of public entities, changes in their financial position.

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# The Musings of Frustrated Government Accountants

**Jesse Hughes and Michael Parry**

## Introduction

Government accountants are well versed on preparing financial statements on the accrual basis of accounting and interpreting those statements to assist in making critical financial decisions. However, political issues will often override those logical financial recommendations made by the accountants. It is difficult to find the balance between social needs and financial sustainability. Implementation of accrual accounting in government is a case in point. The International Public Sector Accounting Standards Board (IPSASB) was established in 1997 to develop international accounting standards for the public sector. Using the International Financial Reporting Standards (IFRS) as the foundation for the development of the standards for the public sector, the IPSASB issued pertinent cash and accrual bases standards after due process specifically for the public sector. In addition, the IPSASB issued case studies identifying action taken by three countries [France (2002), UK (2002), and USA (2006)<sup>1</sup>] in their efforts to implement accrual accounting. Even though countries were warned about the overly sophisticated aspects of accrual accounting, the EU, IMF, UN, and World Bank have been strong supporters of the movement toward accrual accounting for governments throughout the world since better accountability and transparency in government finances will be available to its citizens.

- a. The following are some of the actions taken in the USA since publication by the IPSAS Board of the USA case in 2006:

## Central Government

The Budget and Accounting Procedures Act of 1950 had legislated that the Government Accountability Office (GAO) was responsible to set accounting standards for federal agencies. By law, the Director of Office of Management and Budget (OMB) is responsible for identifying the form and content of the financial statements and the Treasurer in the U.S. Treasury is responsible for preparing the financial statements. These two individuals and the Comptroller General (head of GAO) agreed to establish the Federal Accounting Standards Advisory Board (FASAB) in 1991. The Board is an advisory board and their recommendations for new accounting standards require the approval of the three positions that had established FASAB. Since then, FASAB has issued a number of accounting standards and is moving closer to be in line with the internationally approved accrual IPSAS. As a result of implementing Generally Accepted Accounting Principles (GAAP), the published federal consolidated financial statements provide a higher level of transparency and hold the elected officials more accountable for their actions (or inactions).

The Chief Financial Officer's (CFO) Act was approved by Congress in 1990 to establish CFO positions for 24 federal agencies and to have audited financial statements. However, the qualifications for the CFO positions were not specified. The first CFO (Ed Mazur) for central government was the State Comptroller from Virginia and he was a well-qualified Certified Public Accountant (CPA). He took aggressive action to move toward a more fiscally sustainable position but was relieved from his duties with the change in political bodies in 1993. A new CFO was appointed with much less qualifications and much less interest in fiscal sustainability. And recent CFOs have had good political connections but not had stellar

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<sup>1</sup> See reports in IPSASB.org.

qualifications for the job. Candidates for the Presidency or Congress are elected on their promises of how much they can give away; they are not elected on how much they can take away if there is a political crisis!

The Government Management Reform Act of 1994 is one of several financial reforms that received bipartisan support from Congress and the President. The law requires that 24 major departments and agencies in the executive branch of the government prepare annual, audited financial statements. These reports are to be submitted to the OMB by March 1st. The law also requires the Department of the Treasury to prepare annual consolidated, government-wide financial statements and the GAO to audit and report on these financial statements by March 31st. In their audit of the 2017 Consolidated Financial Statements, GAO expressed the following: “The comprehensive long-term fiscal projections presented in the Statement of Long-Term Fiscal Projections and related information show that absent policy changes, the federal government continues to face an unsustainable long-term fiscal path.”<sup>2</sup>

At the federal level, financial management has always been on a cash budget proposed by the OMB, submitted to Congress by the President, and legally approved by the legislators after much deliberation. Cash budgeting is very beneficial since it provides the basis for fiscal discipline within government. However, budgeted cash can be manipulated. If a bill is due and there are no budgeted funds available, payment can be delayed until the next budget cycle when budgeted funds are available. In many countries, this creates arrears in the delay and frustration among vendors who have not received payments when due. Accrual accounting and accrual budgeting can correct that problem by recognizing the expenditure when the liability is incurred not when the cash is paid.

Much has been done in the USA to improve accountability and transparency at the federal level by preparing consolidated financial statements on the accrual basis of accounting. However, debt is a real problem in the United States with a debt to Gross Domestic Product (GDP) ratio<sup>3</sup> of 76%<sup>4</sup> in 2017. The first USA CFO has carried on his fight for more control over debt after he left government service in 1993. In addition, Charles Bowsher (prior Comptroller General) resigned his appointed 15-year term to enter the fight with Congress for less debt. Even though there is a legally approved debt limit from Congress, this limit is routinely raised by Congress when debt approaches its legally mandated limit. As noted earlier in the GAO report, the current fiscal path is not sustainable. Not only is debt a problem in the USA, it is also a problem in many other countries especially in the underfunding of government pensions. Based on a study by OECD<sup>5</sup>, eight countries (Australia, Canada, France, Netherlands, Norway, Sweden, UK, and US<sup>6</sup>) had a funded ratio for public pension plans ranging from 9.3% to 112.5% in 2008 with an average of 77.9%.

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<sup>2</sup> <https://www.gao.gov/products/GAO-18-316R>

<sup>3</sup> The informal international standard is 60% established by the Maastricht Treaty in 1992 for countries to enter the European Union.

<sup>4</sup> [https://www.fiscal.treasury.gov/fsreports/rpt/finrep/fr/fr\\_index.htm](https://www.fiscal.treasury.gov/fsreports/rpt/finrep/fr/fr_index.htm) (p. 19 of Management’s Discussion and Analysis).

<sup>5</sup> Ponds, E., C. Severinson and J. Yermo (2011, p. 23), “Funding in Public Sector Pension Plans: International Evidence”, *OECD Working Papers on Finance, Insurance and Private Pensions*, No. 8, OECD Publishing, <http://dx.doi.org/10.1787/5kgcfm8rgmp-en>

<sup>6</sup> State and local governments only since the federal government does not reflect its funded ratio in their consolidated financial reports.

Even though consolidated financial statements are being prepared on the accrual basis of accounting for the U.S. government, they are seldom used for decision-making by elected officials. Congressional committees often deliberate the value of the consolidated statements but little action comes from these committee hearings. GAO made the following comments in their audit report concerning the 2017 consolidated financial statement: “Three major impediments continued to prevent GAO from rendering an opinion on the federal government’s accrual-based consolidated financial statements: (1) serious financial management problems at DOD that prevented its financial statements from being auditable, (2) the federal government’s inability to adequately account for and reconcile intragovernmental activity and balances between federal entities, and (3) the federal government’s ineffective process for preparing the consolidated financial statements.”<sup>7</sup> In addition, the Association of Government Accountants has a Certificate of Excellence in Accountability Reporting (CEAR)<sup>®</sup> program<sup>8</sup> that reviews the consolidated statements prepared by the 24 federal agencies and make recommendations for improvement, where necessary.

With respect to the FASAB standard for pensions, Other Retirement Benefits (ORB), and Other Post-Employment Benefits (OPEB)<sup>9</sup>, there is some question as to whether the full costs of administering the dedicated collections for those trust funds are allocated to the 24 agencies. If true, the full costs of services provided in these agencies are not included in their financial statements. This is especially important for the Social Security Administration where the trustees forecast that the Social Security scheme will be bankrupt by 2034 and Medicare for Hospital Insurance will be bankrupt in 2029.<sup>10</sup> These programs will be bankrupt much sooner if the questioned full costs of pensions, ORB, and OPEB for retired civil service employees were included in their financial statements.

## Local Government

In 1968, the Accounting Principles Board implemented a version of the modified cash basis of accounting for the 87,000 state and local government entities (S&LG). This was changed to a modified version of the accrual basis of fund accounting in 1984. Then, in 2002, GASB 34 established government-wide accrual accounting for all 87,000 S&LGs. Since that time, the S&LGs have been implementing the accrual GASB standards with various degrees of success and publishing their results annually in 200+ pages of a Comprehensive Annual Financial Reports (CAFRs). The GASB standards are very similar to the accrual IPSAS.

However, at the S&LG level, most governmental decisions are still based on the cash budget since it is a good tool to assure fiscal discipline. And all of the 50 states except one (Vermont) require a balanced budget where expected expenditures do not exceed anticipated revenues. Cash is king and more easily understood by the decision-makers (both elected and appointed) in government. Accrual accounting is more concerned with fiscal sustainability and is difficult for most decision-makers in government to fully understand. This is especially true of the elected officials since they are more interested in good performance within the legally approved cash budget in the immediate future if they hope to be re-elected. Using accrual accounting, any deficit reported in the Statement of Financial Performance is of less concern to these decision-

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<sup>7</sup> <https://www.gao.gov/products/GAO-18-316R>

<sup>8</sup> <https://www.agacgfm.org/CEAR/About.aspx>

<sup>9</sup> SFFAS 33. Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates

<sup>10</sup> <https://www.ssa.gov/OACT/TRSUM/index.html>

makers since most voters are not aware of the statement's contents. Even though a deficit in the Statement of Financial Performance is reconciled to a deficit in the cash budget, most voters do not understand the explanation of the difference between the two.

Most S&LGs in the United States attempt to fund 70% of their outstanding pension costs since this is the measure that bond rating agencies informally use to rate investment grade government bonds. "A state pension plan's annual funded ratio gives an end-of-fiscal-year snapshot of the assets as a proportion of the accrued liabilities. In aggregate, the funded ratio of these plans dropped to 72 percent in 2015 from 75 percent in 2014. Across the country, funded ratios for plans reviewed by The Pew Charitable Trusts ranged from 37 percent in New Jersey to 104 percent in South Dakota."<sup>11</sup> Anything less than 70% will generate General Obligation Bonds at a higher interest repayment rate than those that are greater than 70%. Further, the bond rating agencies do not appear to look at the funding of OPEB. Consequently, most S&LGs do not fund the OPEB liabilities.

- b. The following are some of the actions taken in the UK since publication by the IPSAS Board of the UK case in 2002:

The UK started to reform government financial management and reporting as long ago as 1995 with the decision to introduce "resource accounting", a form of accrual accounting<sup>12</sup>. Implementation took place over the period to 2001, by which date departmental accounts and "supply estimates" (the UK terminology for departmental expenditure budgets) were all accrual based. Today the entire UK government budget, accounting and reporting systems are all accrual based. Accounting standards are based on IFRS, adapted for the UK public sector as set out in the UK Treasury Resource Accounting Manual (RAM). The UK Financial Reporting Advisory Board (FRAB) provides an independent oversight of resource accounting and the RAM standards.

Despite the early adoption of accrual budgeting and accounting, government financial reporting in the UK has continued to be criticized. In part this is the result of the unique structure of government financial management in the UK, too complex to describe in a short article, but the main features are as follows. The UK government budget as approved by parliament is very high level. Responsibility for the detailed expenditure budgets is devolved to the Treasury (the UK equivalent of a Ministry of Finance). The Treasury sets out Departmental (in the UK, Ministries are referred to as Departments) expenditure limits in the "supply estimates". Each Department is then left to establish its own accounting system and chart of accounts - provided it complies with Treasury RAM standards. Similarly, each Department publishes its own financial reports, referred to as resource accounts i.e. accrual financial reports.

This makes it difficult to find financial information. As the UK Guardian newspaper commented "public spending by government departments is a mystery. It shouldn't be: the Treasury publishes a guide to public spending every year. But if you want detail - and final figures the departments will stand by, you have to go direct to departmental annual reports."<sup>13</sup> This newspaper article goes on to raise various criticisms of Departmental reports, including a

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<sup>11</sup> <http://www.pewtrusts.org/en/research-and-analysis/analysis/2017/07/19/measuring-the-fiscal-health-of-state-pension-plans>

<sup>12</sup> "Resource accounting and Budgeting in Government", HMSO, 1994

<sup>13</sup> The Guardian Newspaper, December 4, 2012

lack of consistency of format, lack of consistency between years, problems of reconciling with government budgets and with other financial data.

A study of the implementation of resource accounting in one region of the UK<sup>14</sup> recorded a comment by one accountant “What is produced is not worth doing because, frankly, the accounts themselves are so complicated that nobody understands them. . . They are just totally incomprehensible”. The same study concluded “Overall, the arguments presented by various proponents of accruals accounting systems in many countries often contain similar themes and claims ... these claims should be treated with caution .... is quite possible that the rhetoric of government about accruals accounting (often in advance of implementation) can be very different from the reality”.

There have been a series of reforms by the UK Treasury in attempts to make better information on government finances available to the general public, each known by a series of acronyms - Public Expenditure System (PES), Government Online Data System (GOLD), General Expenditure Monitoring System (GEMS), Combined Online Information System (COINS) and the latest iteration “Online System for Central Accounting and Reporting (OSCAR)”. More recently there have been moves to simplify and make more accessible government financial reports.

Despite these reforms, a Parliamentary Committee in 2017 concluded “The consensus of evidence to our inquiry makes it clear that many Government Departments’ Annual Reports and Accounts remain badly written and difficult to understand or follow, despite recent reforms, and despite being prepared to a high technical standard”. One problem cited was that “Departments’ current reporting is primarily based around their organisational structure ... for an area such as Child and Adult Mental Health Services, for instance, it is almost impossible for the public to find out from the Department of Health’s Annual Report and Accounts how much is being spent on this, or other types of service, and therefore to assess the value for money of that spending”<sup>15</sup> The report makes a number of suggestions including some which are of generic importance, summarised as follows:

- Financial data should clearly link measurable outputs and outcomes
- Report not just by organisational unit but also by policy area
- Clearly relate spending to outputs
- Publish unit costs (on a consistent basis) for key services
- Reports should be published in Excel or another similar usable format
- Reports should enable the reader to see how final outturn compares to original plans
- There should be an audited statement reconciling, as far as reasonably practicable, the financial commitments made with what eventually happens
- The materiality level applied should be disclosed

There is an ongoing programme to implement the above recommendations.

The UK Government has also initiated the publication of Whole of Government Accounts. (WGA) – financial reports embracing the whole of government. These were first published for the financial year 2009/10. As with Departmental accounts, WGA are prepared on an accrual

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<sup>14</sup> “The Actual Implementation of Accruals Accounting”, Ciaran Connolly and Noel Hyndman, Accounting, Auditing & Accountability Journal Vol. 19 No. 2, 2006

<sup>15</sup> UK “The Public Administration and Constitutional Affairs Committee Report” April 2017, HMSO Hansard

basis in accordance with IFRS with various adaptations to meet the requirements of the public sector. In consequence the reporting standards are close to IPSAS. The latest available WGA is for the year 2014-15 – one of the criticisms has been the delays in the publication of the WGA, currently some 14 months after the year end. The WGA are audited by the UK National Audit Office (NAO). So far, the NAO has qualified its opinion on all of the published WGAs, though the number of qualifications has been reduced over time. The overall NAO comment on the 2014-15 WGA is that “better analysis by the Treasury of the nature of the assets across the government’s portfolio, the extent and sources of liabilities and the financial risks it is exposed to, will help Parliament and the public to understand better the full range of the government’s financial commitments and its approach to managing them.”<sup>16</sup> The NAO qualifications on the 2014-15 WGA all relate to scope and coverage of the financial reports.

Despite of all of the above reforms, the London Telegraph newspaper of March 18, 2018, stated “official figures gave an “over-optimistic picture” of the country’s debt because they excluded billions of pounds in future payments, including on private finance initiative (PFI) contracts and state and public sector pensions. ... the figures for net public sector debt, currently around £1.8 trillion (approximately \$2.4 trillion), are largely based on the value of gilts.” Yet the latest available WGA indicate that total UK government liabilities, including pensions, PFIs, and other liabilities, are £3.6 trillion (approximately \$4.8 trillion).

The conclusion must be that reforming government financial reporting and making useful information publicly available is a major challenge. Despite more than 20 years of reforms, the UK has not as yet been able to resolve all of the issues and problems. The very scale and complexity of the accrual financial reports works against their utilization, even by those who are responsible for the preparation of such reports.

- c. Since many countries around the world have public corporations (state-owned enterprises), recent research about the world of commercial financial reporting is reflected below:

The above experience of the usability and impact of financial reports is mirrored in the world of commercial financial reporting. An important recent book by Baruch Lev and Feng Gu<sup>17</sup> finds that in the USA corporate financial reports provide only 5% of the information relevant to investors and concludes that financial report information is “largely unfit for twenty first century investment and lending decisions”. The authors’ research indicated that over time the correlation between reported earnings and book value, on the one hand, and share value on the other hand, had declined. A major cause is identified as what the authors refer to as dispersion – the very complexity of financial reporting makes the figures less certain and their interpretation more dispersed. This reflects the above comments about public sector financial reports in the USA and UK.

The study further identified three causes for the decreasing relevance of corporate financial reports:

1. The treatment of intangible assets – increasing corporate value is determined by intangible assets, yet these are not properly recognised in financial reports.

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<sup>16</sup> <https://www.nao.org.uk/report/report-of-the-comptroller-and-auditor-general-whole-of-government-accounts-2014-15/>

<sup>17</sup> “The End of Accounting and the Path Forward for Investors and Managers” Baruch Lev and Feng Gu, Wiley New Jersey, 2016’

2. Financial reports are increasingly based on estimates, e.g. the value of assets, pension liabilities, provisions for bad debts, etc.
3. Increasing importance of unrecorded events, e.g. software development, gain or loss of contracts, new regulations, etc.

Finally, the study makes three recommendations for the future of financial reporting:

1. Capitalize the cost of intangibles;
2. Avoid valuations of assets and liabilities that are not traded in active markets; and
3. Reduce financial reporting complexity.

The Lev and Gu study cited above relates to commercial entity financial reporting. Yet in many ways the challenge for the public sector financial reporting is even greater because accrual reporting is relatively new and has to establish its importance to both decision makers and citizens.

## Conclusion

It can be very frustrating for a dedicated government accountant to sit in on financial decision-making meetings and to have the accrual information ignored. So often, government decision-makers manage on the cash basis but report on the accrual basis. These decision-makers are well meaning but they are interested in the here and now for re-election not in the future for our children and grandchildren. It is often said that “government employees are mediocre; they are mediocre when employed or they are beaten into mediocracy”.

Hopefully, in time, the value of government accountants’ recommendations will be recognized and fiscal sustainability of the current benefits provided by governmental entities for our children and grandchildren can be assured. Perhaps, the USA (and other countries) will implement accrual budgeting as some countries have done, i.e. Australia and the UK. It may be necessary to have two types of budgets; one on the cash basis for fiscal discipline and the other on the accrual basis for fiscal sustainability with a statement to explain the difference between the two. The IPSASB does not have the authority to establish standards for budget preparation but they have published a Recommended Practice Guide for Reporting on the Long-Term Sustainability of an Entity’s Finances<sup>18</sup>. These recommended reporting practices may be of assistance in transitioning to accrual budgeting.

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<sup>18</sup> RPG 1-Reporting on the Long-Term Sustainability of an Entity’s Finances (July 2013), IPSASB 2017 Handbook Volume 2 (Secured) at the IPSASB.org website: [www.ipsab.org](http://www.ipsab.org)



# An Appropriate Financial Reporting Framework for the Public Sector in East and Southern Africa

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## Abstract

Historically, governments have been reporting in terms of a cash basis of accounting. There is a widely accepted view that accrual based financial reports that are robust and transparent can improve the decision making and accountability of governments. However, there are contrasting views on the accrual based accounting framework that is appropriate for financial reporting in the public sector. As a consequence, governments have either adopted EPSAS, GFS, IFRS, IPSAS, national accounting standards or continued with cash basis accounting for financial reporting.

This paper seeks to identify the perspectives of experts and senior officials that prepare financial reports in the Office of the Accountants-General in the public sector of the ESAAG region on the attributes that define the appropriate financial reporting framework for the public sector. Fourteen (14) experts and senior officials in the region were interviewed. Interviews are the main method used by researchers to collect data on various perspectives and attitudes of those interviewed.

An Interpretative Thematic Analysis was used to analyse the data collected from the interviews in order to identify themes and principles and construct an initial assessment on the perspectives or views of the experts and senior officials in the Office of the Accountants-General in the public sector of the ESAAG region on the attributes that define the appropriate financial reporting framework for the public sector in that region.

**Key words:** Appropriate financial reporting framework, EPSAS, ESAAG, GFS, IFRS, IPSAS, National Accounting Standards and Thematic Analysis.

## Introduction

Most governments have been reporting in terms of a cash basis of accounting. According to the International Federation of Accountants (IFAC), (2014), most governments that adhere to a cash basis of accounting provide minimal disclosures relative to what the banks, credit providers, employees, investors and the public expect of the private sector. This has resulted in a growing demand for public sector entities to achieve the same level of financial transparency and accountability as their private sector counterparts.

The Organisation for Economic Co-operation and Development (OECD) and IFAC (2017), explained that financial reporting is one of the foundations of good fiscal management. An increased demand for a more 'open' government, reduced public spending capacity and increased efforts to achieve greater efficiency in delivering public services have prompted governments to produce high quality financial reports that can be used as a mechanism for legislatures, auditors and the public to hold governments to account for their financial performance. (OECD and IFAC 2017),

Cavanagh, Flynn, and Moretti (2016), stressed that accrual accounting assists policymakers and the public to pay more attention to the acquisition, disposal and management of government assets, liabilities and contingent liabilities.

Governments around the world own public assets worth US\$75 trillion dollars that are not managed and accounted for appropriately and a positive return of 1% on global public assets would add up to US\$750 billion to the public revenues of governments.

(Detter, Folster and Buitter 2015). The inappropriate accounting for public assets and returns could be due to the fact that most governments record their transactions on a cash basis of accounting.

Wynne (2016), explained that most governments could improve the quality of their financial reports if they only focused on 'best practice' as opposed to adopting international accounting standards that are more onerous to comply with. The elements of 'best practice', are:

- Timeliness - governments producing financial reports within a few months of their respective financial year end;
- Understandability – governments producing financial information that is understood by many of the key users of the financial statements, that are usually not financially literate, such as the general public and political representatives;
- Openness/Transparency – governments ensuring that key financial information of interest to politicians and the public is made available; and
- Consistency – governments ensuring that financial information that is reliable and free from material errors is prepared from one year to the next.

Aggestam-Pontoppidan (2011), is of the opinion that the decision to adopt accrual accounting may involve a desire to either establish local (national) standards to fit the purpose, or adopt standards such as International Financial Reporting Standards (IFRS) or International Public Sector Accounting Standards (IPSAS) that are developed by international standard setters.

Aggestam-Pontoppidan (2011), pointed out that little or no research has been conducted on the accounting framework that is appropriate for the public sector and recommended that research be conducted to create a more in-depth understanding of the overall challenges and costs versus benefits of adopting either IPSAS or IFRS in the public sector.

The public sector is required to move towards an appropriate set of accounting and financial reporting standards because public administrators face a challenge to harmonise accounting systems within countries and across borders.

(Aggestam-Pontoppidan and Andernack 2016).

There is a long running debate on whether business-like standards should be applied to both private and public sectors or whether separate accounting standards should be promulgated for each sector. (Ellwood and Newberry 2016). Aggestam-Pontoppidan (2011), concurred that implementing IFRS in the private sector is often associated with better financial information, enhanced comparability and increased capability to secure cross-border listing and funding for shareholders, regulators and other stakeholders and cautioned whether such benefits could translate to the public sector.

Researchers have produced contradictory results on the framework that is appropriate for the public sector. Laswad and Redmayne (2015) conducted research and sought views from the preparers and users of financial reports on the appropriate financial reporting framework for the public sector in New Zealand. According to Laswad and Redmayne (2015), most respondents preferred IFRS and perceived IPSAS to be an alternative option. Conversely, Ijeoma (2014), conducted research for the government of Nigeria and the findings of the study showed that the

implementation of IPSAS could improve the reliability, credibility and integrity of financial reporting and enhance service delivery for the Nigerian government.

From the above, it can be seen that there are contrasting views on the accounting standards or frameworks that are appropriate for the public sector. As a consequence, some entities in the public sector have adopted IPSAS, whilst others have either implemented European Public Sector Accounting Standards (EPSAS), Government Finance Statistics (GFS), IFRS, national accounting standards or continued with cash basis accounting.

The researcher has been working in the public sector in Africa and wanted to assess the perspectives of the experts and senior officials who prepare financial reports in the Office of the Accountants-General in the East and Southern African Association of Accountants-General (ESAAG<sup>1</sup>) region on the attributes that define the appropriate financial reporting framework for the public sector in that region.

This paper reviews relevant literature and considers the appropriateness of the EPSAS, GFS, IFRS, IPSAS or national accounting standards for financial reporting in the public sector to uncover elements or attributes that define the appropriate financial reporting framework for the public sector.

Finally, this paper aims to explore the reactions of the experts and senior officials that prepare financial reports in the Office of the Accountants-General in the public sector of the ESAAG region in order to understand their perspectives or views regarding an appropriate financial reporting framework for the public sector.

## A review of relevant literature

### Financial Reporting in the Public Sector

Aggestam-Pontoppidan and Andernack (2016), explained that the first issue considered when applying any set of accounting standards is to ensure that the scope is well defined and the preselected set of standards are appropriate to the current situation and entity.

The Conceptual Framework for General Purpose Financial Reporting by Public sector entities published by the International Public Sector Accounting Standards Board (IPSASB<sup>2</sup>) in 2014, (Conceptual Framework), does not define a public sector entity but explains that such entities encompass the following characteristics:

- National, central, federal, regional, state, local, provincial governments and international organisations;
- Receive large volumes of non-exchange transactions because they receive value from another party without giving approximate equal value in exchange;

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<sup>1</sup> The ESAAG is a regional body for Accountants-General with a mission to develop sound Public Finance Management (PFM) practices in 14 countries in East and Southern Africa. The current members of the ESAAG region are: Botswana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Rwanda, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe. (About ESAAG. Available from <http://www.esaag.co.za>.)

<sup>2</sup> The IPSAS Board (IPSASB), is a member of IFAC and an independent standard setting body that develops the IPSAS and consists of 18 members with an expertise in public sector financial reporting. The IPSASB also publish Recommended Practice Guidelines (RPG) which are pronouncements that provide guidance on good practice in preparing General Purpose Financial Reports.

- Provide large volumes of non-exchange transactions in the form of public goods such as defense, education and social grants without receiving approximate equal value from the recipients in exchange;
- Required by statute to prepare budgets;
- Exist for the long term, irrespective of a change in political control; and
- Hold property, plant and equipment for service delivery rather than profit motive.

Furthermore, IFAC (1991 & 2006), stated that governments differ from business in both their objectives and financing since the primary goal of a business entity is profit, whilst governments provide public services and redistribute wealth for a variety of social and economic purposes. This is supported by Barton (2005), who argued that businesses that operate in the private sector must maintain sound financial positions and remain solvent to survive, whilst the market values of their assets are determined from supply and demand factors as opposed to public sector entities that hold non-financial assets that cannot be sold to provide future economic benefits.

Barton (2005) concluded that the accountability responsibilities of entities in the public sector exceed that of their private sector counterparts who are only accountable to their shareholders and investors, whilst the former is elected by citizens to provide public goods and services on their behalf.

Cash and accrual are the most common bases of accounting used for financial reporting in the public sector and an increasing number of entities in the public sector were migrating from a cash to an accrual basis of accounting for financial reporting. In 2015, 41 governments (21%) had transitioned to accrual, 16 governments accounted for their transactions on modified accrual (8%), 28 governments (17%) reported on a modified cash basis and 114 governments (57%) remained on pure cash accounting. (Cavanagh et al 2016).

The European Commission Staff Working Document (2013), acknowledged that accrual accounting is indispensable at the macro (general government) and micro (government entity) level. A cash basis of accounting is inadequate for the complex operations of government as they own vast stocks of assets needed to provide for cultural services, defense, education and health services, sporting and recreational facilities and public roads. (Barton 2005).

Fergus McCormick, Chief Economist and Co-Head of sovereign ratings at DBRS Agency concurs that accrual accounting in the public sector could boost the credit rating score and improve accuracy of the score since quality, consistent and transparent data is assessed by credit rating agencies (Rumney, 2017a).

Andreas Bergmann, (cited in Rumney 2017b), former IPSASB chair and professor at Switzerland's Zhaw School of Management and Law contended that the benefits of accrual accounting included downward pressure on government debt, lower interest rates and decreased the likelihood of economic shocks. Voters in Spanish municipalities utilised accrual fiscal information during elections and the Swiss media used accrual information when covering the public finances of its government. (Bergman, cited in Rumney 2017b).

### **Adopting IFRS for financial reporting in the public sector**

Barton (2005), and Aggestam-Pontoppidan (2011), explained that Australia and New Zealand followed a sector-neutral approach and adopted IFRS in both the public and private sector because:

- This promoted comparability and consistency for both sectors;

- Stakeholders argued that assets utilised in government were similar to those used in the private sector and thus distinction on applying IFRS needed not to be based on the sector (public or private) of the entity;
- Practitioners advised the public sector to adopt already existing standards and not to ‘waste time and reinvent the wheel’;
- Stakeholders believed that introducing robust accounting practices of the private sector to the public sector was the ‘righteous thing to do,’ as governments needed to reform according to concepts of the market; and
- Accounting standards for the private sector were deemed to be ‘best practice’.

Kris Peach, the Chair of the Australian Accounting Standards Board (AASB), acknowledged that IFRS were useful in keeping the public sector in Australia up to date in addressing financial reporting issues and that no alternative approach was acceptable there (Ernst & Young 2016).

Whilst IFRS was seen as a suitable reporting framework for the private sector, it has its limitations from a public sector perspective. In 2009, the Controller and Auditor General of New Zealand, K. B. Brady (2009), presented a discussion paper to the House of Representatives and expressed the following concerns in terms of adopting IFRS in the public sector:

- The standards were complex and could not be understood by the preparers of the financial statements which resulted in the government hiring external consultants to prepare the financial reports;
- The standards provided limited guidance for the public sector since the standards were built on fundamental premises that mainly did not apply to that sector such as exchange transactions whose values were largely arrived at based on future cash flows, whilst many of the transactions for the public sector were non-exchange in nature;
- The standards are applicable mainly to users of the General Purpose Financial Reports (GPFR) which are analysts, investors and regulators whilst the main users of the financial statements of the public sector are the parliament and public;
- The standards are only applicable to large profit oriented entities for the private sector and not the public sector whose mandate is not to earn profits; and
- The standards use language and terminology such as profit and loss which is not applicable for the public sector because the objective of the public sector is not to earn profit.

Barton (2005), added that IFRS had to be amended in areas such as accounting for donations, assets used for defense, cultural, heritage and infrastructure assets, and non-cash generating assets to cater for those public sector entities that had such elements and transactions in their financial reports.

The failure to recognise the uniqueness of the public sector resulted in irrelevant accounting concepts and standards which undermined the faithful representation, relevance and understandability of financial information of the public sector. (Barton 2005).

Oulasvirta (2014) concurred that IFRS relied heavily on concepts such as fair value accounting, which could cause problems in the identification, measurement and valuation of assets and liabilities in the public sector.

The Controller and Auditor General of New Zealand, K. B. Brady (2009), advised the House of Representatives that the financial reporting frameworks of the public sector needed to incorporate the following important attributes:

- Clear description of performance which is understood and in line with the entity's objectives;
- Financial performance that is comparable to the plans of the entity at the start of the reporting period;
- Financial performance that is congruent to non-financial performance;
- Stewardship that is referenced to the entity's balance sheet and supporting notes; and
- Long-term sustainability which can be assessed.

As a consequence, all non-profit oriented entities operating in the public sector in New Zealand, referenced IPSAS and modified the IFRS to suit the public sector, whilst the profit oriented entities in the public sector remained on the IFRS framework.

### **Adopting IPSAS for financial reporting in the public sector**

Aggestam-Pontoppidan (2011) highlighted that, in most cases, IPSAS were applied for accrual accounting within the public sector since the primary objective of most public sector entities is to deliver services to the public, rather than to make profits and generate a return on equity to investors.

IPSAS provides more guidance on accounting for non-cash generating assets, revenue from non-exchange transactions, social benefits and budget reporting, whilst IFRS does not provide such guidance as such transactions are unique to the public sector. (Aggestam-Pontoppidan 2011).

According to the European Commission (2012 & 2013), Ernst & Young (2013), Federation of European Accountants (FEE) (2014), and PWC (2014), the European Union member states chose not to implement IPSAS in its entirety because of the following shortcomings:

- There was concern amongst member states of the governance, independence and oversight of the standard setting process followed by the IPSASB;
- The standards are issued by a private sector entity and public authorities were not involved in the process of drafting and issuing such standards;
- IPSAS principles are translated from IFRS, a private sector accounting framework that did not take sufficient account of the specific needs and interests of public sector financial reporting;
- The standards had limited coverage as these standards did not have a conceptual framework which set the core principles for the design of standards and did not prescribe the accounting practices of important transactions for the public sector such as heritage assets, social benefits and taxation;
- The standards were regarded as incomplete because no counterpart IPSAS was developed for standards that had been adopted for the private sector such as exploration for and evaluation of mineral resources and retirement benefit plans;
- The criteria for control under IPSAS leads to the consolidation of controlled entities such as Government Business Enterprises (GBE) that use IFRS whose accounting policies

differ from those applied by the controlling public sector entities and needed to be reconciled and adjusted to match the IPSAS compliant financial statements of the controlling public sector during consolidation;

- The standards offer too many alternative accounting policy treatments, as non-financial assets are valued at historical cost or fair value; interest/borrowing costs are expensed or capitalised; cash flow from operating activities is determined using the direct or indirect method and expenses are presented using the nature or function method which could impair comparability and discourage harmonisation;
- The standards are applicable to all types and sizes of public sector entities and this may be excessively costly and burdensome for small and less complex entities in the public sector;
- There is limited linkage between IPSAS and GFS statistical data as the consolidation principles of the General Government Sector (GGS) according to the GFS differ from the control concept in IPSAS; and
- There is limited linkage between IPSAS, budgeting and management reporting and the standards needed to be used as a management tool that enables the public sector entity to measure the cost of operations when compared with appropriations.

As a result of the abovementioned shortcomings, the European Commission chose not to adopt IPSAS in its entirety and elected to use the standards as an indisputable reference for developing their own accrual standards known as EPSAS.

Kris Peach concurred that one of the remaining difficulties of IPSAS is that the IPSASB takes a long time to amend IFRS based standards, and therefore transitioning to IPSAS meant reversing some recent IFRS changes for those countries that were up to date with IFRS (Ernst & Young 2016). This is supported by Kimberley Crook, a partner at Ernst & Young in New Zealand who explained that IPSAS tends to lag behind IFRS resulting in unnecessary differences with the potential to create additional cost and complexity during the consolidation process for mixed groups that comprise of private and public sector entities (Ernst & Young 2014).

It should be noted however, the IPSASB has attempted to address some of the concerns that were raised. Since 2014, the IPSASB has published a Conceptual Framework, issued Consultation papers on heritage assets and social benefits and established the Public Interest Committee (PIC) and the Consultative Advisory Group (CAG) to strengthen the governance of the standard setting process. A process has already been put in place by the IPSASB and the International Monetary Fund (IMF) to harmonise IPSAS and GFS statistical reporting systems (European Commission Staff Working Document 2013).

### **Adopting GFS in the public sector**

According to the European Commission Staff Working Document (2013), governments produce two types of financial data to report on their activities. The GFS reports are produced for economic, fiscal and statistical purposes at macro level whilst the financial accounting reports are produced for accountability and decision making purposes at a micro-level for an individual or group of entities.

The GFS are a macroeconomic statistical framework suitable for analysing and evaluating the fiscal policy and performance of the GGS, which are non-profit government entities controlled by the government that receive funding from appropriations, taxes, transfer, and undertake non-market activities to deliver services to the communities (IMF 2014).

Alexandre Makaronidis, Project Leader and Head of GFS Quality Management at Eurostat, the Statistics Directorate of the European Commission, lamented that, whilst the GFS were based on the accrual principle, the data used to produce GFS was extracted from cash data that was converted into accrual data which led to deficiencies in the reported information (Ernst & Young 2013).

The European Commission Staff Working Document (2013), acknowledged that the GFS were similar to international accounting standards in the form of IFRS and IPSAS, because both standards were integrated, consistent datasets with data on both stocks and flows, and used accruals as a guiding principle for reporting. Stock positions refer to assets and liabilities and the resulting net worth, whilst flows are changes in the economic value within a reporting period (IMF 2014).

Ball and Pflugrath (2012) explained that the GFS excludes several assets and liabilities from the balance sheet that would otherwise be recognised if governments adopted IPSAS for financial reporting. Ball and Pflugrath (2012), the European Commission Staff Working Document (2013), and IMF (2014), elaborated that the accrual standards developed for GFS differed from the accrual standards developed from IPSAS or IFRS because they:

- Adopted a general philosophy of using current market prices as the valuation basis for assets and liabilities, whilst IPSAS requires an accounting policy choice to measure classes of assets and liabilities at current market prices or historic cost;
- Excluded entities that are similar to GBE that engage in market activities, whilst the 'reporting entity' in terms of IPSAS is a government or public sector entity that prepares GPFR and consolidates the financial information of any bodies controlled by the reporting entity, despite some of them being entities engaged in market activities;
- Recorded holding gains and losses (revaluations) in a separate account as these are viewed not to be under government control whilst IPSAS recognises holding gains in the bottom line in the statement of financial performance to measure the activities of government;
- Recognised fewer assets as they only account for assets if governments can establish strict legal ownership rights, as opposed to IPSAS that recognises such transactions when control is established. Military assets are usually not reported as assets in terms of the GFS Manual; and
- Recognised fewer liabilities as they apply caution in anticipating future outflows of cash and may only account for provisions, guarantees and contingent liabilities when they are called, as opposed to IPSAS that recognises such transactions when there is a present obligation and the cash outflow can be measured reliably.

### **Adopting EPSAS in the public sector**

Some members of the European Union states led by France and Germany have opposed the adoption of EPSAS in Europe. The German Federation issued a position paper that called for governments to have the freedom to choose between the accrual and cash basis of accounting even after the EPSAS are issued (German Federation/Lander 2017). The position paper highlighted the following concerns for adopting EPSAS in Europe:

- The goal of improving the comparability and quality of data could not be achieved by introducing EPSAS due to structural differences between the administrative and political systems amongst the member states;



- There was no evidence to date that any deficits relating to the comparability, completeness and reliability of fiscal statistics and budgetary surveillance on the EU level, would be remedied through the introduction of common accrual public sector accounting standards;
- There were no investigations carried out to identify whether there are simpler and less expensive alternatives to EPSAS; and
- It continued to be questionable whether the benefits of introducing EPSAS on a mandatory basis could justify the accompanying costs. The benefits were difficult to quantify, long-term in nature and only realisable in combination with other reform measures, whilst the costs to procure hardware and software, consulting and training services were significant.

The position paper (German Federation/Lander 2017) concluded that EPSAS needed to possess the following attributes in their accounting standards for the public sector:

- The standards must be based on a conceptual framework which is a foundation that must be adopted before the statutory introduction of the individual EPSAS;
- The standards should develop simplified rules for smaller and less risk-prone public sector entities; and
- The standards should limit discretionary leeway on accounting policy options to recognise, verify and value assets and liabilities to ensure comparability.

### **Adopting National standards in the public sector**

The approach to adopting IPSAS or IFRS is varied in different jurisdictions. Some jurisdictions adopt the international accounting standards in their pure form, whilst other nations raised the issue of subsidiarity and asserted that it was their sovereign right to develop their own national accounting standards rather than to adopt international standards that are imposed upon them. (European Commission 2012). Therefore, most countries indirectly reference IPSAS or IFRS when developing their own national accounting standards to suit their local accounting environment.

The direct adoption of IPSAS and IFRS by national governments is low, as countries favour national standards to accommodate a number of specific deviations. The majority of countries in the OECD use IPSAS or IFRS as primary references for developing their national standards (OECD & IFAC 2017). National accounting standards undermine comparability as nations develop their own accounting rules that are tailored to suit their systems, thus leading to diverse financial reporting in the public sector (Oulasvirta 2014).

### **Conclusion of the relevant literature**

From the literature review, it can be established that there are numerous frameworks that are available for adoption in the public sector. The GFS are more useful for statistical reporting and exclude entities that engage in market activities. The IFRS are seen as a suitable reporting framework for the private sector because they do not recognise the uniqueness of the public sector. IPSAS is the more appropriate financial reporting framework for the public sector as it provides guidance that suits that sector. However, some nations have been reluctant to adopt IPSAS in its entirety and have referenced the standards to prepare their local accounting standards. National accounting standards undermine comparability. The implementation of EPSAS in Europe has raised controversy with countries such as Germany resisting the adoption

of the accounting standards in that region. The costs of adopting EPSAS are perceived to be higher than the benefits thereof.

### **Interview process adopted to collect data**

An interpretative research philosophy was followed to capture the perceptions and feelings of people. Saunders, Lewis and Thornhill (2012), elaborates that the interpretative research framework is selected when:

- The researcher is concerned about capturing feelings, attitudes and not facts;
- The population to be considered during the study is small; and
- When scientific (positivism) research might not work.

Interviews are the primary method of qualitative research used to collect data and interpret the perceptions of those interviewed. (Aronson 1994 and Saunders et al 2012). An interpretative research method was used to interpret the perspectives of the 14 experts and senior officials working in the Office of the Accountants-General in the ESAAG region because the topic area is under-researched, and as such, it was reasoned that scientific research might not have worked as the study was carried out before accrual accounting IPSAS or IFRS frameworks were fully adopted for financial reporting in the ESAAG region. To add on, the researcher wanted to obtain the perceptions and feelings of a small population of 14 experts and senior officials through a series of interviews.

The interviews were focused on the 14 experts and senior officials in the Office of the Accountants-General that prepare financial reports in the public sector of the ESAAG region because they are initially impacted by the reform of implementing international accounting standards. Those interviewed (participants) were informed of the nature and purpose of the interview and guaranteed anonymity. Participants were allowed to deal with the issues raised without interruption. Additional questions were presented as they arose, usually in direct response to a statement from the participant. The interviews lasted between 45 and 60 minutes and were carried out between January and June 2017<sup>3</sup>.

### **Thematic analysis - Analysis of the information collected from the interviews**

Thematic analysis is a common method used to analyse the experiences provided by participants during an interview and is useful to investigate an under-researched area in order to identify and report patterns and themes. (Aronson 1994 and Braun and Clarke 2006). A theme is a key idea in relation to the research question that captures something important about the data and represents some level of patterned response or meaning within the data set. (Braun and Clarke 2006).

The following steps were performed by the interviewer to identify themes from the data or perspectives provided by the experts and senior officials that were interviewed<sup>4</sup>:

- Step 1 – Recordings and data collected from the interviews of the experts and senior officials were transcribed verbatim.

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<sup>3</sup> The aforementioned steps that were used by the interviewer during the interview process to collect data are adapted from studies by Atkins and Maroun (2015).

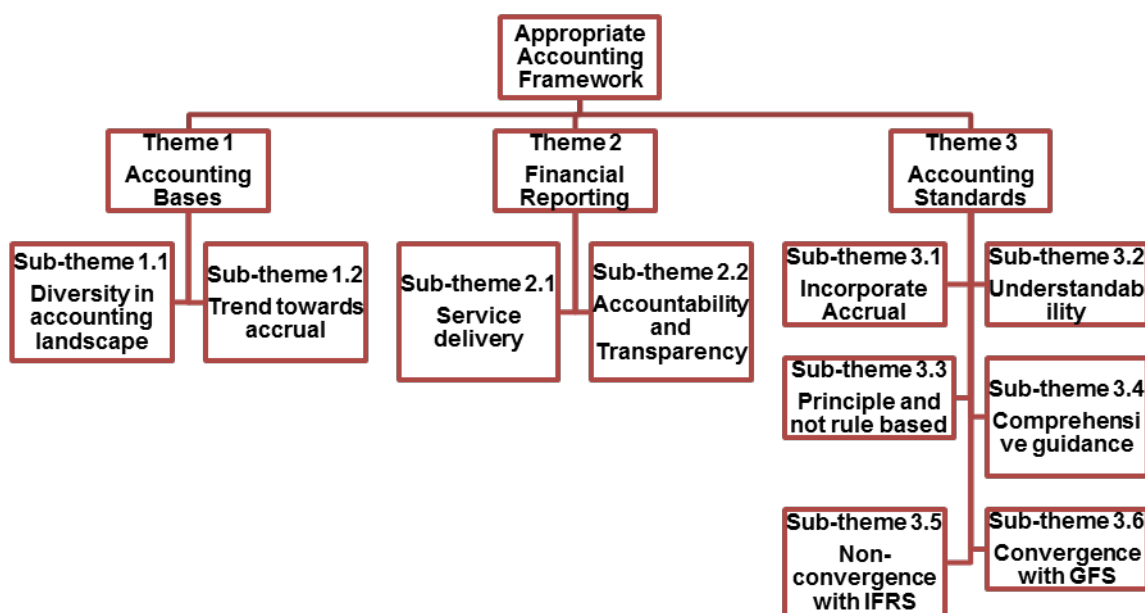
<sup>4</sup> The steps performed for the thematic analysis were adapted from studies by Aronson (1994), Braun and Clarke (2006) and Thomas (2003).

- Step 2 – Listened to transcripts a number of times to understand the answers or raw data that were collected from the interviews.
- Step 3 - Answers that were provided by each expert and senior official during the interview were recorded on an excel spreadsheet in written form and coded in a table to identify the main themes (categories), patterns and sub-patterns in relation to the research objective and the supporting reasoning.
- Step 4 – Within each category, the interviewer searched for new insights and selected appropriate quotes that conveyed the key themes. The interviewer also combined or linked similar patterns into main themes.
- Step 5 – Theme statements were documented by the researcher and valid arguments for selecting themes were also provided.

## Results

The entire population of 14 experts and senior officials from the ESAAG region were interviewed either face to face or telephonically. The ideal outcome of the thematic analysis coding process is to create between three to eight major themes and an inductive coding which produces more than eight themes could be seen as incomplete as smaller categories may not have been combined into main themes. (Thomas 2003). The interviewer identified 3 themes and 10 sub-themes that are illustrated in the diagram below and discussed in detail in the subsequent sections.

Figure 1: Diagram illustrating the themes that define the Appropriate Accounting Framework for financial reporting in the public sector



### Theme 1: Accounting bases

#### Sub-theme 1.1: Diversity in the current central government accounting landscape

The interviewer discovered that there is diversity in the bases of accounting adopted for financial reporting within the ESAAG region. Participants from four countries, namely, Lesotho, Mozambique, Namibia, and Zimbabwe, or 29% of the population, explained that

financial reports of their respective countries are prepared on the cash basis of accounting to match the framework used to prepare their institutional budgets.

Participants from three countries, namely, Kenya, Malawi and Zambia, or 21% of the population, explained that the financial reports of their respective countries are prepared in terms of Cash Basis IPSAS.

Participants from six countries, namely, Botswana, Mauritius, Rwanda, South Africa, Swaziland and Uganda, or 43% of the population, stated that the financial reports of their respective countries are prepared on the modified cash basis of accounting.

The participant from one country, Tanzania, or 7% of the population, highlighted that “the Public Finance Management Act (PFMA) in that country, had mandated IPSAS to be the reporting framework for government and the country is already preparing consolidated (Whole of government) financial reports in terms of Accrual IPSAS”.

Therefore, the norm in the ESAAG region is to prepare financial reports in terms of the modified cash basis of accounting. Participants elaborated that irrespective of the bases of accounting used by their governments, cost of borrowings is usually accounted on an accrual basis to portray a true picture of debt.

### **Sub-theme 1.2: Similarity in future central government accounting landscape or trend towards accrual accounting**

The interviewer discovered a similarity in the accounting landscape and a clear trend towards the adoption of an accrual basis of accounting in the near future. Only two countries, Mozambique and Namibia, or 14%, explained that the financial reports of their countries will remain on the cash basis of accounting.

Participants from ten countries, namely, Botswana, Kenya, Lesotho, Malawi, Mauritius, Rwanda, Swaziland, Uganda, Zambia and Zimbabwe, or 71%, stated that their respective countries intend to follow the IPSAS adoption roadmap developed by the ESAAG and adopt Accrual IPSAS in the future. Some of the countries intend to follow a phased approach, and adopt Cash Basis IPSAS as a stepping stone to adopting Accrual IPSAS.

The participant from one country, South Africa, or 7%, added that “the country intends to utilise Generally Recognised Accounting Practice (GRAP) which is referenced from IPSAS for financial reporting at a central government level.

The participant from one country, Tanzania, or 7%, declared that, “Tanzania will continue to apply Accrual IPSAS in the foreseeable future and added that the country was ahead of its African counterparts as most of the countries in the ESAAG region had only recently announced their intention to adopt IPSAS”.

## **Theme 2: Financial Reporting**

### **Sub-theme 2.1: Service delivery objectives should be referenced to the financial reports**

The interviewer discovered that financial reports in the public sector are enhanced when governments reference the reports to service delivery objectives.

The participant from Botswana advised that “accounting standards that are developed for the public sector need to provide guidance on how costs incurred by governments when rendering services should be disclosed in the financial reports”.

Participants from Malawi and South Africa stressed that financial reports should allow governments to disclose how financial resources were utilised to fulfil their service delivery mandate.

The participant from Swaziland maintained that “the costs incurred for service delivery need to be reported and that governments cannot deliver services if there is no basis to account for the costs of service delivery. Information about the costs incurred for service delivery was vital for donors and development partners as they need the information to determine the amount of funding that is required”.

The participant from Mozambique explained that “the purpose of the public sector is to satisfy the public. The public is satisfied when services are delivered regularly, in an economic, efficient, effective and legal manner and such information needs to be disclosed in the financial reports”.

Participants from Uganda and Zimbabwe concurred that governments need to report on the efficiency and state of services as they are entrusted resources by taxpayers.

### **Sub-theme 2.2: Accountability and transparency should be referenced to the financial reports**

The interviewer discovered that financial reports prepared by public sector entities are enhanced when they are used as tools to showcase accountability and transparency.

The participant from Zimbabwe highlighted that “governments are accountable to a wider base of users including civil society and taxpayers. Financial reports prepared for the public sector need to show a fair picture of the financial position of the government’s finances”.

The participant from Swaziland stated that “financial reports should show a true picture of debt, investments and other assets. In addition, the participant from South Africa explained that “financial reports prepared for the public sector should show the assets in place, consumed, impaired, and the condition thereof”.

Participants from Botswana and Mauritius stressed that governments should prepare financial reports that show how public resources and taxes are utilised, as they are stewards of the public office.

Participants from Rwanda and Zambia, advised that governments should use financial reports as instruments to provide feedback on how resources are utilised, thus showing accountability. The Rwandan participant, added that “financial reports are important as they give information for more prioritising and decision making in the future because failure to have a post-mortem for what governments were entrusted for, results in limited planning”.

“Financial reports give citizens insight on the true and fair view of resources entrusted to the public sector entity. IPSAS has an advantage over IFRS because it provides guidance on financial reporting of the General Government Sector through the standard IPSAS 22 and compares actual financial transactions versus amounts budgeted for through the use of the Budgeting standards (IPSAS 24)”, declared the representative from Tanzania.

### **Theme 3: Accounting standards**

### **Sub-theme 3.1: Accounting standards should incorporate accrual basis of accounting**

The interviewer identified that accounting standards that are developed for the public sector should incorporate the principles of accrual basis of accounting.

Participants from eleven countries, namely, Botswana, Kenya, Lesotho, Mauritius, Namibia, Rwanda, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe, or 79%, prefer the accrual basis of accounting for financial reporting in the public sector. The participant from Botswana elaborated that “the accrual basis of accounting provides a complete picture of the financial performance and position of the government as opposed to the cash basis of accounting that produces incomplete information on assets, liabilities, equity and performance of governments, which does not allow for better decision making”.

Two participants from South Africa and Malawi, or 14%, prefer both accrual and cash basis of accounting for financial reporting in the public sector. The participant from South Africa explained that “it is more appropriate for financial reports of public sector entities to follow the cash basis of accounting to match the budgets that are prepared in terms of the cash basis. The cash basis of accounting is more appropriate for government departments that are merely ‘cost centres’ and do not generate substantial revenue but rely solely on cash transfers from governments to fund their activities and remit surplus or unused funds to central government at the end of each financial year and see no benefit to account for non-cash transactions such as depreciation. The accrual basis of accounting is more appropriate for municipalities that should in theory be ‘self-sustaining’ as they generate revenue to cover costs”.

One respondent from Mozambique, or 7%, did not comment on the accounting basis that was preferred for financial reporting in the public sector.

### **Sub-theme 3.2: Accounting standards should be understandable**

The interviewer identified that accounting standards that are developed for the public sector should be more understandable.

The participant from South Africa asserted that “the accounting standards that are developed for the public sector are too technical and do not consider the needs of the users. The preparers who are usually not up to date with the latest developments in accounting are forced to apply their judgment to decide on the recognition, measurement and presentation of complex transactions. Preparers need to understand why a standard is set in a certain way. Standard setting bodies employ accountants who are inherently not good at explaining concepts in a simpler way. Narrative information would assist preparers to understand the accounting of certain transactions. For example, Post implementation reviews are conducted in GRAP to assess whether information produced by applying the Standards is relevant to users, and to identify application and implementation issues that may require a resolution. Standard setting bodies need to consider the maturity of environments and implement transitional provisions and reliefs in their accounting standards to make them more understandable”.

Participants from Lesotho, Malawi, Mauritius, Namibia, Rwanda, Swaziland, Zambia and Zimbabwe concurred that accounting standards should not be complex, to cater for different stakeholders such as the public and members of parliament that are usually not financially literate. Accounting standards should not be complex, as the primary users do not understand the accounting jargon.

“Accounting standards should be developed in local languages to make them more understandable”, suggested the Malawian representative.

Participants from Mauritius and Swaziland stated that accounting standards should be more understandable, as the public sector has not professionalised the accountancy cadre and finance departments.

The participant from Mauritius added that “users of financial information are diverse with different levels of skill and require other statements, reports and explanatory notes to make them easier to read and understand. Most public sector entities across the world are unable to adhere to international accounting standards such as IPSAS in spite of their willingness to do so. Accounting standards should be designed in a flexible manner to cater for the different levels of preparedness to apply such standards. One way in which this could be done would be to have different levels of accounting standards. For example, level 1 of accounting standards would be simpler to apply; level 2 accounting standards would be of moderate complexity and level 3 accounting standards would be the final required standard. Public sector entities would be required to disclose the level of each standard that they selected when preparing their financial reports. The overarching objective is to get everybody on board in their quest to improve accountability and transparency in their financial reports. It should not be an ‘all or nothing game’, as is presently the case”.

The participant from Rwanda added that “understandability is one of the qualitative characteristics of accounting standards that are developed for the public sector. Accounting standards should be presented in a language that is simple”.

“Accounting standards should be concise, objective and understandable so that the more relaxed reader can have a proper understanding of their content”, declared the participant from Mozambique.

The participant from Tanzania cautioned that, “users of financial reports will not make decisions to invest or lend if the financial information is not understandable. Preparers should not only focus on numbers but also on the qualitative information such as accounting policies, commentary, disclosures and notes to ensure that the layman understands the key messages”.

Participants from Botswana and Uganda, explained that accounting standards need to be understandable to allow specific countries to tailor such standards to suit the requirements of their respective countries, and that the relevance of the accounting standards should not be lost and quality compromised in an attempt to make them more understandable.

“The public does not even understand the current financial reporting frameworks that are adopted by their governments that are perceived to be less complex and it is the responsibility of the media to simplify the financial reports and use different forums to educate the public”, cautioned the participant from Botswana.

“Governments need to focus on training and building the capacity of the finance departments instead of focusing on simplifying accounting standards. Governments need to implement the simpler accounting standards and subsequently adopt the more onerous accounting standards as they mature”, declared the participant from Kenya.

### **Sub-theme 3.3: Accounting standards should be principle based**

The interviewer identified that accounting standards that are developed for the public sector should be principle based. The use of accounting policy options is encouraged despite comparability being compromised.

Participants from Botswana, Kenya, Lesotho, Malawi, Mauritius, Namibia, Rwanda, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe support the use of accounting policy options in the accounting standards.

The participant from Botswana explained that “integrity and transparency of accounting standards should matter more than comparability. Accounting policy options are allowed as long as they are compliant to the accounting standards”.

The participant from South Africa acknowledged that “the use of accounting policy options undermine comparability but it is beneficial to have policy options as this allows accounting standards to be flexible. Policy options cater for the different characteristics of public sector entities. For example, it is beneficial to value assets of municipalities at fair value as they need to generate revenue to replace those assets and the policies on assets need to take into account the increase in the value of such assets. Conversely, departments receive grants to replace assets and therefore, such assets may be measured at cost”.

The participant from Zimbabwe elaborated that “accounting policy options should be adopted to accommodate the legislations of different countries”.

Accounting standards should not be prescriptive to enable acceptance for the use of the accounting standards. Governments can select the policy options that suit their requirements, advised the participants from Kenya and Mauritius.

The participant from Kenya elaborated that “accounting standards should have policy options to allow countries the privilege to decide on the best option. Comparability is not an issue as the alternative policy option can be disclosed in the notes of the financial reports. Countries will not adopt the standards that are rigid and strict”.

The participant from Malawi maintained that “accounting policy options are important as governments may present the first option on the face of the financial reports and disclose the second option in the notes to the financial reports”.

The participant from Mauritius added that “accounting standards should make it clear that any change in accounting policy must be disclosed and the impact adjusted and disclosed in the statement of financial position”.

The participant from Tanzania explained that “the fair presentation of financial reports is still achieved irrespective of the accounting policy option that is selected. Options are important as the standard setters allow governments to apply their minds and develop their own accounting policies by considering the benefits of each method. For example, information is tied up when presenting cash flows using the indirect method, whilst the direct method allows for more information to be opened up and makes it easier for users to make economic decisions. Comparability can never be compromised by selecting policy options. Accounting policy options allow countries to select the option that best suits that country”.

The participants from Uganda mentioned that “accounting standards should have policy options as stakeholders may have differing views on the accounting options to be adopted and not allowing options increases rigidity”.

Participants from Rwanda, South Africa, Swaziland and Uganda cautioned that accounting policy options should not be too broad as this could add to the complexity of the accounting standards.

Participants from Rwanda and Uganda, added that too many policy options were not good and accounting standards should limit the options to a maximum of two.



The participant from Swaziland argued that “accounting standards that are developed for the public sector should initially allow for one accounting policy option and be flexible for more policy options to be adopted once the finance departments of governments mature”.

The participant from Mauritius mentioned that “ESAAG should firstly apply policy options and adopt uniform options once the finance departments are robust”.

The participant from Kenya warned that “there are instances when the use of accounting policy options is not appropriate. For example, an entity cannot select between using Cash Basis IPSAS or Accrual IPSAS Cash Flows as the two formats are distinctively different”.

#### **Sub-theme 3.4: Accounting standards should be complete**

The interviewer identified that accounting standards that are developed for the public sector should be complete and provide a comprehensive guidance on accounting for transactions.

Participants from Botswana, Malawi, Namibia, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe advised that accounting standards that are developed for the public sector should be complete.

The participant from Botswana advised that, “accounting standards that are complete enable comparability. Accounting standards that are developed for the public sector should also provide guidance on the Budgeting cycle process and Accrual budgeting. Currently, the standard on Budgeting in IPSAS only provides guidance for comparing Actual versus Budgeted amounts and the variances thereof. The standard on Budgeting should provide more guidance on the Budgeting process. This may encourage Budgeting departments to lobby for the adoption of IPSAS”.

The participant from South Africa recalled that, “a similar problem occurred in South Africa when municipalities that needed to adopt Standards for Generally Accepted Municipal Accounting Practice (GAMAP) were forced to reference IFRS to ‘fill the gaps’ as the GAMAP were not complete. Currently, there are gaps between IFRS and IPSAS because the IPSASB is not a full time Board and has to ‘play catch-up’ to fill the gaps. Standard setting bodies need to complete the core standards and focus on developing Recommended Practice Guideline (RPG) in the long term. Accounting standards that are developed for the public sector also lack guidance on measurement”.

The participant from Zimbabwe lamented that “accounting standards that are developed for the public sector do not provide guidance on accounting for exploration of mineral assets”.

The participant from Mauritius argued that, “it is essential for accounting standards to cover all economic events that impact the public sector to ensure consistency and remove any element of subjectivity”.

“Accounting standards need to be complete for areas covered by IFRS and provide guidance on recognition, measurement (initial and subsequent measurement) and presentation of transactions. Accounting standards need to be adaptable to the evolving environment and should not limit guidance to financial reporting only but also provide guidance on reporting Policy, Program Based Performance, Output and Outcomes”, declared the participant from Rwanda.

The participant from Tanzania reasoned that “it takes time to develop accounting standards for the public sector as transactions are evolving and the standards are derived from IFRS”.

The participant from Kenya maintained that “in a nutshell, accounting standards should cover most areas but need to take into consideration the complexity of the areas not covered. Topics

on Heritage Assets and Natural Resources are complex and guidance on accounting for such transactions takes time to develop. A 'big bang approach' might not be appropriate. Accounting standards also need to expand their guidance to assessing the uniformity of Chart of Accounts (COA) as ministries, SOE and Counties/Municipalities have different COA. Experienced implementers need to be consulted by standard setting bodies to provide guidance for developing COA”.

The participant from Malawi warned that “accounting standards should not be complete for the sake thereof and not provide guidance on transactions that are not relevant to the public sector”.

Accounting standards that are developed for the public sector should comprise of the Conceptual Framework, confirmed the participants from Botswana, Lesotho, Malawi, Mauritius, Rwanda, South Africa, Zambia and Zimbabwe.

The participant from Botswana recalled that “there was a low take up on the adoption of the IPSAS because the accounting standards did not have a Conceptual Framework”.

The participant from Zimbabwe added that the “Conceptual Framework could be used to develop future standards”.

The participant from Mauritius elaborated that “the Conceptual Framework sets the basis within which reporting should be undertaken. Ideally, the Conceptual Framework should be produced before the standards are produced”.

The participant from Rwanda stated that “the Conceptual Framework should be the starting point as it is the ‘mother’ of all standards”.

The participant from Malawi commented that “the Conceptual Framework defines the principles of accounting standards. The Conceptual Framework was developed way after most IPSAS were developed and is only applicable to the Accrual Basis IPSAS and not the Cash Basis IPSAS”.

The participant from Tanzania indicated that “the Conceptual Framework should be developed first because it defines and elaborates issues that are not covered in the accounting standards. There is no need to develop accounting standards if Standard setting bodies develop a complete and comprehensive Conceptual Framework as it reduces gaps in accounting standards”.

The participant from Uganda stressed that “the Conceptual Framework is the ‘backbone’ and should be developed before the accounting standards are issued”.

The participant from South Africa cautioned that “the Conceptual Framework is important but can be challenging to use in areas where there is no clear direction. The interpretation of the Conceptual Framework may be subjective in areas where guidance is lacking on specific transactions that are unique to the public sector such as Heritage assets”.

The participant from Lesotho argued that “it is not appropriate to have a Conceptual Framework before developing accounting standards”.

### **Sub-theme 3.5: Accounting standards should not be copied from IFRS.**

The interviewer discovered that accounting standards that are developed for the public sector should not be copied from IFRS.

Participants from Botswana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Rwanda, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe concurred that it is important for public sector officials to be involved in the development of accounting standards for the public sector as they have more insight on public sector specific issues. The standards should be

developed by an independent body. It is also important for standard setting bodies to have independent oversight.

The participant from Botswana added that “public sector officials do not need to prepare accounting standards, but need to be involved in the process of setting the standards. Botswana is currently implementing IPSAS and the Financial Reporting Act (FRA) states that the Botswana Accounting Oversight Authority (BAOA) should oversee the implementation of IPSAS”.

The participant from South Africa recalled that “the IPSASB was criticised by stakeholders such as the European Commission because the process that they followed to develop standards was perceived not to be transparent and fair. As a result, the IPSASB put in place independent oversight in the form of the CAG and PIC. From a credibility perspective, the governance of the standard setting body should be put in place. In South Africa, the National Treasury under the Minister of Finance monitors the activities and due process followed by the ASB when developing accounting standards for the public sector of the country”.

The participant from Swaziland elaborated that “accounting standards on biological assets and financial instruments that are based on IFRS need to be modified to suit the public sector”. The participant from Lesotho noted that “accounting standards should reflect the unique features of the public sector”.

The participant from Mauritius added that “the development and application of any standard requires a thorough knowledge of the environment. Participation of public sector officials will provide a deeper insight of the socio-economic environment, the legal framework as well as other critical aspects of the public sector. The governance of the standard setting process can be improved through enlarged discussions and publications of Exposure drafts and Discussion papers to all stakeholders such as IASB, IMF, external auditors, Investment (Banking and lending) institutions, government and public at large”.

The participant from Malawi noted that “the IPSAS on investment property and impairment of cash generating assets are derived from the private sector standards (IFRS) but do not specifically address public sector specific characteristics. Investment property that is held for the private sector is usually not the same as Investment property held for the public sector”.

The participant from Rwanda added that “accounting standards that are developed for the public sector should not be copied from the private sector accounting standards (IFRS) but cover the reality of the public sector when developing accounting standards for that sector”.

### **Sub-theme 3.6: Accounting standards should be converged with statistical bases**

The interviewer discovered that accounting standards that are developed for the public sector should be converged with statistical reports such as GFS.

Participants from Botswana, Kenya, Malawi, Mauritius, Rwanda, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe advised that accounting standards that are developed for the public sector should be used to produce statistical reports such as GFS.

The participant from Botswana explained that “it is better for government to use the same information that it has produced for financial reporting as a base to preparing GFS reports in order to reduce gaps and getting information from the same pot could be better. The government of Botswana is currently developing COA that accommodate both GFS and IPSAS”.

The participant from South Africa advised that “there is common agreement to use one set of information. I was appointed on the Task force team to harmonise and align IPSAS and GFS.

IPSAS and GFS cannot be aligned fully (100%) as the reports have different objectives that drive certain policy decisions. It is important for preparers to understand the differences and account for the reconcilable differences. COA should be flexible to cater for both IPSAS and GFS. For example, military assets are expensed according to the GFS and not capitalised as assets in terms of IPSAS”.

Participants from Zambia and Zimbabwe, added that accounting standards can be used to compile GFS as they provide more reliable data.

The participant from Swaziland noted that “accounting standards can also be used to measure debt, GDP, investments and the overall liquidity of the government”.

The participant from Mauritius added that “GFS requirements have been aligned as far as possible to the IFRS or IPSAS requirements. The use of a commonly agreed standard is favourable as this will not allow different figures to be used”.

The participant from Malawi cautioned that “the majority of the transactions may be recognised with the two frameworks but additional data may still need to be provided for GFS information”.

The participant from Rwanda acknowledged that “accounting standards that are developed for the public sector should not only be harmonised to GFS but to additional reports such as The Public Expenditure Framework Accountability (PEFA) and Public Investment Management Assessment (PIMA). PEFA is a methodology for assessing public financial management performance. PIMA is a framework that assesses and measures public investments”.

The participant from Tanzania, mentioned that “Tanzania adopted the GFS for statistical reporting and the GFS information is derived from IPSAS reports. IPSAS reports are comprehensive and cover large amounts of information as the public sector covers the General Government Sector (GGS) and public corporations. In Tanzania financial reports that are prepared in terms of IPSAS are used as inputs to compile GFS. However, GFS information prepared in Tanzania is on a cash basis”.

The participant from Kenya commented that “IPSAS reports are a good basis to prepare GFS information with some minor adjustments. The Institute of Statistics in Kenya uses IPSAS reports to produce quality statistics for that country. Some of the information that has not been produced for many years by the Institute is now made available due to IPSAS”.

### **Concluding comments**

Little or no research has been conducted on the appropriate financial reporting framework in the public sector. As a result, there are contrasting views on the accounting standards that are appropriate for the public sector. Therefore, entities in the public sector have either adopted GFS, IFRS, IPSAS, nationalised their standards, or continued with cash basis accounting for financial reporting purposes. This has undermined the comparability of governments.

The IPSAS have become the recommended choice for financial reporting in the public sector because the standards provide enhanced information for accountability and decision making purposes, and guidance on transactions that are unique to the public sector. However, the IPSAS framework also has its limitations and some nations have been reluctant to adopt IPSAS in its entirety.

The aim of the article was to identify the elements or attributes that define the appropriate financial reporting framework for the public sector in the ESAAG region. According to the 14 experts and senior officials working in the Office of the Accountants-General in the public

sector of the ESAAG region, accounting standards that are developed for the public sector should: not be subjective, and should meet high levels of accountability and transparency; be prepared in terms of the accrual basis of accounting; be prepared by officials working in the public sector and not derived from IFRS; be less complex and understandable; allow accounting policy options; be complete and cover all transactions; have a conceptual framework; and be compatible to GFS statistical information.

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# Local Government Accounting: Hodgepodge or Harmony

**Nagalingam Nagendrakumar**

## Abstract

The Sri Lanka Public Sector Accounting Standards -introduced in 2009- had not yet been implemented. Instead, the Local Governments (or Local Authorities) continue with the Wickramanayake's Accounting System –introduced in 1975- which is criticized not appropriate. Yet again, the Ministry of Provincial Councils and Local Governments has taken a step to introduce the simplest version of all the Sri Lanka Public Sector Accounting Standards called “Sri Lanka Public Sector Accounting Standards for Local Authorities.” The present study attempts to explain why Local Governments stick to Wickramanayake's Accounting System and castoff the Sri Lanka Public Sector Accounting Standards. The study adopted the qualitative methodology and case study strategy. Data for this study were gathered through semi-structured interviews in the selected cases. The study found that the continuation of Wickramanayake's Accounting System and rejection of Sri Lanka Public Sector Accounting Standards respectively are due to the existence and nonexistence of coercive pressure.

**Key Words:** Local Government, Sri Lanka Public Sector Accounting Standards, Wickramanayake's Accounting System, Coercive Pressure

## Introduction

Public sector refers to the Government and Government owned institutions, and it provides services to the general public (Nagendrakumar, 2017). Sri Lanka is a unitary democratic republic which has comparatively a larger public sector in Asia (Iqbal, 2002) and it spreads over a wide range of sectors of the economy (Kumara & Handapanagoda, 2008). Sri Lankan Public Sector comprise three levels of governmental organizations: central governmental organisations (Central Government (CG), line ministries and departments) provincial governmental organisations (Provincial Councils (PCs), provincial ministries and departments) and local governmental organisations (Municipal Councils (MCs), Urban Councils (UCs) and Pradeshiya Sabhas (PSs)) (Nagendrakumar, 2016).

The Local Authorities are responsible for providing services which the laws (Municipal Councils Ordinance (1947), Urban Councils Ordinance (1939), and Pradeshiya Sabhas Act (1987)) specifically allow them to do. Local Authorities are expected to provide services for the comfort, convenience, and wellbeing of the community in respective geographical areas. Hence, the Local Authority carries out; regulatory and administrative functions, promote public health and sanitation, environmental sanitation, and public thoroughfares, and public utility services. Once the 13th Amendment to the constitution in 1987 was enacted, Local Governments became a devolved subject under the PCs. As a result, the powers to control and supervision of Local Authorities transferred from CG to PCs. However, powers relating to the formation, structure and national policy on local governments remained with the CG. Accordingly, the Local Governments - 23 MCs, 41 UCs, and 271 PSs - became the third and lowest level of Government in Sri Lanka. The Ministry of Provincial Councils and Local Governments is responsible for policy and legislation at the national level, while the Provincial Ministers of Local Governments are responsible for the implementation at local level. Accordingly, the Local Governments receive grants from CG and PG. In addition, they raise fund from taxes, fees, rent, and rates.



## Problem Statement

The Local Governments followed the Cash based accounting in line with the other Government organizations till 1975. Then, by the gazette notification, the Local Governments have introduced the accrual based accounting which is referred to as Wickramanayake's Accounting System. The Wickramanayake's Accounting System has been criticized not appropriate to the Local Governments (Nagendrakumar, 2016). Again, during 2009 by a Treasury circular the Local Governments were introduced the Sri Lanka Public Sector Accounting Standards which are applicable to other Government organizations as well. However, it is noted that those standards are not implemented in Local Governments (Abeysinghe, and Samanthi, 2016; Nagendrakumar, 2016). Yet again, the Ministry of Provincial Councils and Local Governments has taken a step to introduce the simplest version of all the Sri Lanka Public Sector Accounting Standards called 'Sri Lanka Public Sector Accounting Standards for Local Authorities'. Thus, a dilemma exists whether the Local Government Accounting reforms lead to hodgepodge or harmony.

## Methodology

The study followed the qualitative methodology and case study strategy to understand and explain the research problem. Data for this study were gathered through semi-structured interviews conducted from among the MCs, UCs, and PSs in Kurunegala and Trincomalee districts. The interviews were transcribed and then coded using the NVIVO data management system. The codes were further analyzed, and themes were found. Accordingly, themes became the base for the discussion and findings.

## Significance of the Study

It is noted that the Local Governments in Sri Lanka are exposed to the accounting reforms at regular intervals. However, it is noted that they have not yet settled down with an appropriate accounting mechanism. As a result, this study explains the inevitability of the harmony in Local Government accounting environment.

## Discussion and Findings

It is noted that the Wickramanayake's Accounting System and the Sri Lanka Public Sector Accounting Standards are based on accrual accounting principles (Nagendrakumar, 2016). Besides, the respondents admitted that the accrual based accounting reforms are the massive change exercise in the Government Accounting System (GAS). Provided that the unwillingness and the lethargic attitude of the Public Sector Accounting staff in accepting the reforms, the respondents argued that they positioned greater effort to make the GAS aware of the significance of the application of the accrual accounting practices in the public sector. As a result, the Government, of course somewhat, realized that not only the accrual accounting practices to be the most informative for decision making but also certain countries have already adopted the change. That motivated the Secretary of Treasury to stretch the consent to the Institute of Chartered Accountants of Sri Lanka (ICASL) in introducing the Sri Lanka Public Sector Accounting Standards (volume 1 and II). However, it is noted that the sanction for the adoption of Sri Lanka Public Sector Accounting Standards was given only to the Statutory Boards (non-commercial public corporations) and Local Governments (ICASL, 2009). Similarly, the respondents confirmed that the Local Governments, Corporations, and Statutory Boards had adopted the accrual accounting practices well before the introduction of the Sri Lanka Public Sector Accounting Standards.

Therefore, the approval of the Secretary of the Treasury to the Sri Lanka Public Sector Accounting Standards and the existence of accrual accounting practices in those organizations

stimulated the ICASL to trust that it would become easy for them to introduce the Sri Lanka Public Sector Accounting Standards in those entities. However, though these organizations have adopted the accrual accounting practices, respondents pointed out that, it has not been fully functional and further, they highlighted that the Sri Lanka Public Sector Accounting Standards are not applied so far in those organizations. More to say, the Local Governments have unconsciously institutionalized with the Wickramanayake's System of Accounting for the preparation of financial statements which is of course based on the accrual accounting principles but on limited aspects. Further, though space is available for depreciation of fixed assets under Wickramanayake's System of Accounting, it has not been followed. Bizarrely, the Local Governments provide 100% depreciation at the inception of the fixed assets which is again the violation of generally accepted accounting principles. The reason for non - provision of depreciation according to the generally accepted accounting principles is that the fixed assets management in Local Governments is very poor (Nagendrakumar, 2016). Further, it was pointed out that the Wickramanayake's System of Accounting is simply 'filling the form' prescribed and nothing involved with the 'principle based professional judgments' in presenting general purpose financial statements as expected by the Sri Lanka Public Sector Accounting Standards. Also, most of the Local Governments are not headed by the Accountants. Instead, they are headed by the Financial Assistants and Management Assistants. Hence, they argued that it is convenient for them to fill the forms as stipulated in the Wickramanayake's Accounting System and pointed out that they are not familiar with the application of accounting standards. Thus, application of Sri Lanka Public Sector Accounting Standards is not possible since the system already in practice, though it comes under accrual accounting principles and the capacity of the human resource does not suit to the present accounting reforms.

Despite the above fact, since the Sri Lanka Public Sector Accounting Standards manual supports the application of the accrual based accounting standards initially to the Statutory Boards and Local Governments and blessed with Secretary to the Treasury, the respondents positively endorsed the reforms and appreciated the move and said that it could be better to incorporate them in those institutions. The reason why they supported the Secretary to the Treasury's statement in the Sri Lanka Public Sector Accounting Standards manual was that the Local Governments had already been switched on to the accrual accounting principles. Subsequently, the Department of Public Enterprises issued circulars (PED/54/2010 and PED/POL/CIR/2013-3) in 2010 and 2013 instructing the Local Governments and Statutory Boards to prepare the final accounts based on the Sri Lanka Public Sector Accounting Standards. Then, the Ministry of Provincial Councils and Local Government also issued the circular (PAL/05/2014) in 2014 instructing the PCs to prepare the final accounts based on the Sri Lanka Public Sector Accounting Standards. However, it was noted that neither the PCs nor the Local Governments had implemented the Sri Lanka Public Sector Accounting Standards. Above and beyond, Nagendrakumar (2013) argues that the accounting system that is being followed by the PCs is not effective and Nagendrakumar (2016) argues that the accounting system that is being followed by Local Governments also is not effective.

Another important point is that the Department of Local Government follows the cash accounting practices. Though the Local Governments have adopted the accrual accounting practices, the Department of Local Government which is the ultimate controlling body of all the Local Governments in the PC setup has adopted the cash accounting practices. As a result, on the one hand, the Local Governments submit the financial statements to the Department of Local Governments based on the accrual accounting practices and the other hand, the Department of Local Governments submit the financial statements based on the cash accounting practices to the respective PC's Treasury. As a result, the respondents argued that the

accounting practices that are being adopted by the Local Governments and the PCs contradict each other and hence lead to hodgepodge.

However, the Government involvement in this endeavor commenced long after the initiation of the reforms. Further, the involvement of the Government has not been concrete. As a result, though the Treasury has issued the circulars, all the Local Governments had not adhered to the circular instructions, and they had not presented the final statements based on the Sri Lanka Public Sector Accounting Standards. The problem that the Local Governments faced in implementing the Sri Lanka Public Sector Accounting Standards was that the reforms were not legally supported. As opposed to that the Wickramanayake's System of Accounting has been supported by the Government Gazette notification.

## Conclusion

The initiation of accounting reforms has not been copiously supported by the Government. The fundamental criteria for the accounting reforms in the Local Government are that 'political reform promoters' commitment (Luder, 2002) and the resultant Government's policy decision with regard to the absorption of Sri Lanka Public Sector Accounting Standards into the GAS; which has not yet happened. Thus, it is argued that the coercive pressure in implementing the Sri Lanka Public Sector Accounting Standards not existed in a Local Government environment. Instead, the coercive pressure to continue with the Wickramanayake's System of Accounting existed. Yet again, the move in implementing the Sri Lanka Public Sector Accounting Standards under the label of "simplest version" is also underway. As a result, the accounting reforms in Local Governments have become the hodgepodge and need urgent attention to harmony in a Local Government environment.

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# Response to Exposure Draft 62 “Financial Instruments” - August 2017, ICGFM

**Michael Parry**, Chair of the Ad Hoc Committee on International Accounting Standards

## Overview

It is not as yet clear how ED62 will be reflected in accounting standards. The documentation includes both a standalone ED62 and also proposed amendments to ED29. This needs to be clarified.

This is a very complex set of proposals. ED62 alone is 410 pages, with additional documentation amounting a further 330 pages. The documents themselves are also very complex, with the use of terminology unfamiliar to most government accountants, and multiple cross references to other standards. Only a limited number of specialists in some governments will need to understand the full complexity of the proposed standards and the implications for financial reporting. But all governments will need to be able to apply the basic principles of reporting on lending to or by governments, and equity investments held by governments.

Therefore, our first **recommendation** is for a structure to any resulting standard, or standards, that is accessible to government financial managers who neither have, nor require, specialist knowledge of the more arcane financial products and situations. **This is very important if the standard is to be properly implemented by many smaller or poorer countries without access to specialist expertise.** In particular the excellent summary and diagrams in the “At a Glance” publication should be incorporated within the Standard.

## Specific Matters for Comment

There are just three specific matters for comment as summarised in the table below, together with our response.

Comment request	ICGFM Response
<b>Specific Matter for Comment 1:</b> Consistent with the relief provided in IFRS 9, the IPSASB has agreed in [draft] IPSAS [X] (ED 62) to allow an option for entities to continue to apply the IPSAS 29 hedging requirements. Do you agree with the IPSASB’s proposal?	Agreed. This seems sensible  There should be provisions for additional disclosure in the notes to the financial reports on conditions relating to risk hedging, peculiarities of repayment on financial liabilities, the acquisition and maintenance of financial assets.
<b>Specific Matter for Comment 2:</b> The IPSASB recognizes that transition to the new standard [draft] IPSAS [X] (ED 62) may present implementation challenges as a result of the number of significant changes proposed. Therefore, the IPSASB intends to provide a 3 year implementation period until [draft] IPSAS [X] (ED 62) is effective (early adoption will be permitted). Do you agree with the proposed 3-year implementation period before [draft] IPSAS [X] (ED 62) becomes mandatory? Please explain.	Agreed As above, a sensible provision in view of the changes

Comment request	ICGFM Response
<p><b>Specific Matter for Comment 3:</b> Do you agree with the proposed transition requirements in paragraphs, consistent with those provided in IFRS 9? If not, what specific changes do you recommend and why?</p>	<p>Agreed The illustrative examples provided are useful for interpreting ED62. We would suggest these examples should be expanded to include some of the situations and issues faced by members of the ICGFM, as indicated below.</p>

## Comments on the proposals

As indicated, most governments do not invest in, or issue, financial derivatives, and there is limited hedging of currency transactions. However, where such situations do occur they can be of national significance. We therefore **support** an approach based on IFRS9 to ensure consistency with commercial practice.

## Definition of cash

ED 62 contains no definition of cash and cash equivalents, yet these are the most pervasive of all financial instruments. Cash and cash equivalents are defined in IPSAS 2, para 8. We **recommend** the definition of cash and cash equivalents be repeated in any Standard that results from ED62.

## Classification of financial instruments

We support the broad classification of financial instruments between financial assets, financial liabilities and equity.

The classification structure in Paragraphs 39-56 is on the valuation basis. This is not necessarily the most informative presentation for financial reporting. The IMF Government Finance Statistics (GFS) Manual requires classification based on the maturity and source of the financial instrument. We **recommend** that for General Purpose Financial Reports the GFS classification structure is adopted.

## Practical problems identified by ICGFM members

The practical problems identified by ICGFM members primarily relate to loans between public sector institutions, e.g.

- Loans by multilateral or bilateral donor organisations, either directly to governments and then on lent to public sector entities, or directly to public sector entities, with various covenants attached. Problems relate to valuing the on lent loan asset when some of the covenants are breached but the loan is not called in. Also, where the loan is directly to the public sector body, impact of the above events on the valuation of other loans to that entity.
- Lending to or by state-owned banks by public corporations on preferential terms (e.g. below market interest rates, repayment at the end of the contract period, informal but regular loan extension, very large lending). The fair value of such lending may be below the nominal value of the loan, but there is often resistance to provisioning against loans to other public sector entities.
- The risk of default by public sector borrowers is real, yet is difficult to assess and quantify. Often political considerations make it very difficult to write off or provide against loans by other public sector entities.

In all of the above situations clear guidance and examples in the IPSAS would support appropriate valuations.

### Valuation of financial instruments

As a matter of principle, the value of any financial instruments is the discounted expected future cash flows to be generated or incurred from such financial instrument. Any other measure is a surrogate for the present value of such future cash flows.

Where available, market values provide the best indicator of the above present value of future cash flows, since such values are generated by multiple investor estimates. This will normally be what is referred to as “fair value” and hence the approach is **supported**. For governments, the distinction between fair value through surplus/deficit or through net assets/equity is of limited significance, but we accept it is necessary to keep the distinction for consistency with IFRS 9. We also **support** the amortised cost basis in the limited circumstances described.

However, we **recommend**:

1. The section on valuation should start with a statement of basic principles
2. The clarity of this section be improved by concluding with a simple set of rules (without cross references).

### Impairment

We **support** the revised impairment rules which address a criticism of the existing rules particularly for commercial entities.

# Response to Exposure Draft 63 “Social Benefits” - October 2017, ICGFM

**Michael Parry**, Chair of the Ad Hoc Committee on International Accounting Standards

## Overview

The Exposure Draft 63 on Social Benefits raises two fundamental issues:

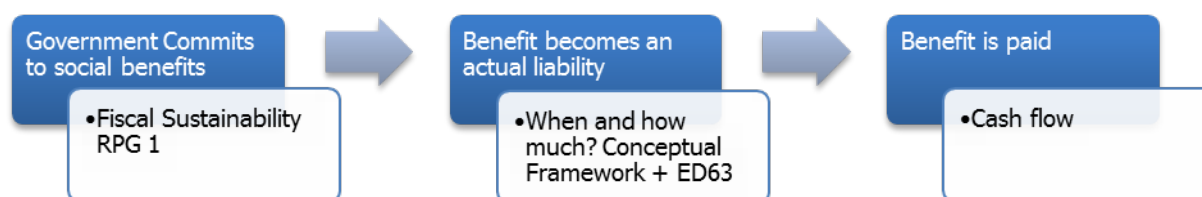
1. The recognition as liabilities commitments made by a government to specific groups of citizens – even though there is no contractual obligation (other than a social contract) requiring future governments to honour such commitments
2. The inter-generational impact of such commitments, e.g. the cost of a state pension payable to all citizens.

Governments across the world commit to certain social benefits, e.g.:

1. Health care benefits
2. Unemployment benefits
3. State pension benefits.

There is a flow from the commitment through liability to the actual payment of social benefits as illustrated in Figure 1 below.

**Figure 1: The flow of social benefit obligations**



In most countries social benefit commitments made by a current government are honoured by subsequent governments, but such commitments do not amount to legally binding contractual obligations. There are numerous examples where the terms of the social benefit obligation have been retrospectively changed, e.g. raising the age for state pension, reducing the amounts to be paid.

These issues are addressed in the IPSAS Conceptual Framework. This identifies when non-legally binding obligations become liabilities in Para 5.24 as follows:

1. *The entity has indicated to other parties by an established pattern of past practice, published policies, or a sufficiently specific current statement that it will accept certain responsibilities;*
2. *As a result of such an indication, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities; and*
3. *The entity has little or no realistic alternative to avoid settling the obligation arising from those responsibilities.*

The first two conditions are normally part of governments making social benefit commitments. The issue of recognition as a liability is when condition (3) above is met. At some stage social benefits do meet condition (3) and hence become liabilities.

The ICGFM supports the principle of recognising social benefits as liabilities when the three conditions specified in the Conceptual Framework are met

### Specific matters for comment

Matter for comment	Response
<p><b>Specific Matter for Comment 1:</b> Do you agree with the scope of this Exposure Draft, and specifically the exclusion of universally accessible services for the reasons given in paragraph BC21(c)? If not, what changes to the scope would you make?</p>	<p>We agree with the scope</p>
<p><b>Specific Matter for Comment 2:</b> Do you agree with the definitions of social benefits, social risks and universally accessible services that are included in this Exposure Draft? If not, what changes to the definitions would you make?</p>	<p>There is no actual definition of social benefits in the ED. Para 6 says to whom social benefits are provided but not what they are and Para 5 and AG 1 – 7 what they are not, but nowhere does the ED actually define social benefits</p> <p>As indicated in our comments on the Discussion Paper, we consider the GFS definition should be used: “6.96 Social benefits are current transfers receivable by households intended to provide for the needs that arise from social risks—for example, sickness, unemployment, retirement, housing, education, or family circumstances.”</p> <p>We also consider that the two categories of social benefit in GFS should be recognised in the proposed Standard:</p> <ol style="list-style-type: none"> <li>1. Pensions and other retirement benefits</li> <li>2. Non-pension social benefits</li> </ol> <p>Social risks are defined in GFS as “Social risks are events or circumstances that may adversely affect the welfare of the households concerned either by imposing additional demands on their resources or by reducing their income”. We can see no good reason for using a different definition.</p> <p>One member of our committee considered it important that that social risks are defined by law and the source of social benefits (i.e. the entity that makes the payment) should be specified</p>
<p><b>Specific Matter for Comment 3:</b> Do you agree that, with respect to the insurance approach: (a) It should be optional; (b) The criteria for determining whether the insurance approach may be applied are appropriate;</p>	<p>(a) and (b) Our comments on the Discussion Paper identified four possible combinations and recommended recognition and measurement approaches as follows:</p> <ol style="list-style-type: none"> <li>1. Pensions and other retirement benefits <ol style="list-style-type: none"> <li>a. Funded – in accordance with IPSAS 25</li> <li>b. Unfunded – Obligating event approach as described in the ED</li> </ol> </li> <li>2. Non-pension social benefits <ol style="list-style-type: none"> <li>a. Funded – Insurance approach as described in the ED</li> <li>b. Unfunded – obligating event approach</li> </ol> </li> </ol>



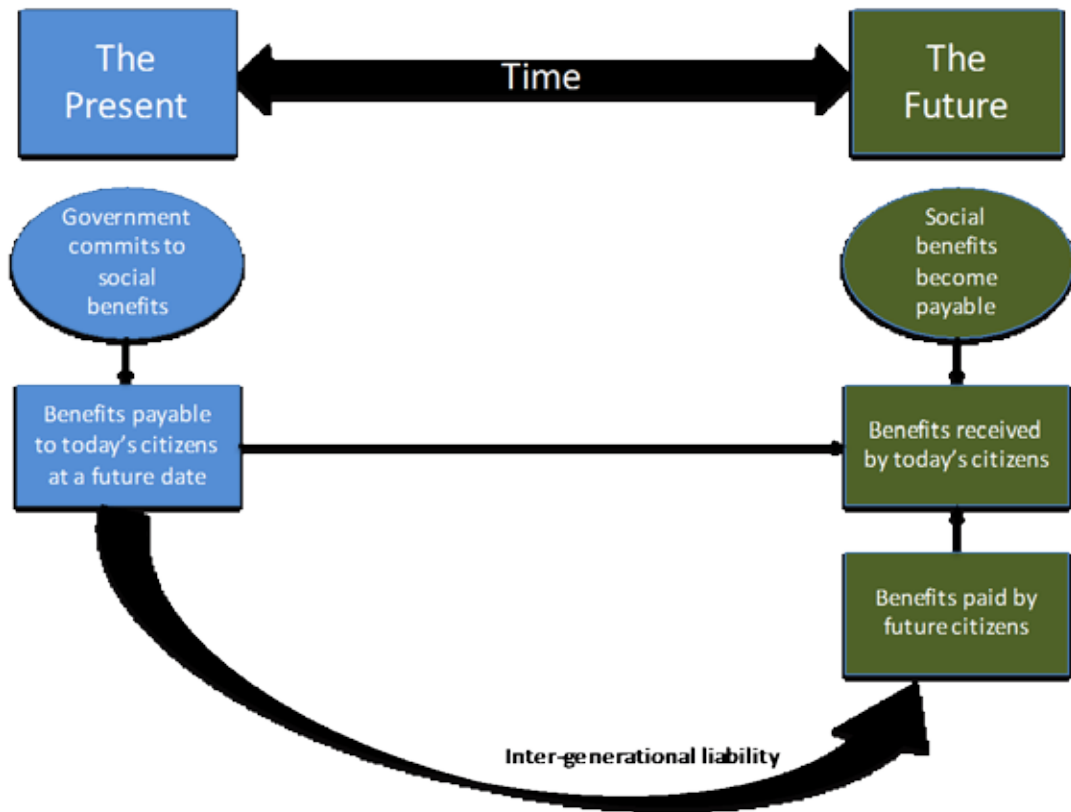
Matter for comment	Response
<p>(c) Directing preparers to follow the relevant international or national accounting standard dealing with insurance contracts (IFRS 17, Insurance Contracts and national standards that have adopted substantially the same principles as IFRS 17) is appropriate; and</p> <p>(d) The additional disclosures required by paragraph 12 of this Exposure Draft are appropriate?</p> <p>If not, how do you think the insurance approach should be applied?</p>	<p>(c) Agreed</p> <p>(d) Agreed</p>
<p><b>Specific Matter for Comment 4:</b></p> <p>Do you agree that, under the obligating event approach, the past event that gives rise to a liability for a social benefit scheme is the satisfaction by the beneficiary of all eligibility criteria for the next benefit, which includes being alive (whether this is explicitly stated or implicit in the scheme provisions)?</p> <p>If not, what past event should give rise to a liability for a social benefit?</p>	<p>Agreed</p>
<p><b>Specific Matter for Comment 5:</b></p> <p>Regarding the disclosure requirements for the obligating event approach, do you agree that:</p> <p>(a) The disclosures about the characteristics of an entity's social benefit schemes (paragraph 31) are appropriate;</p> <p>(b) The disclosures of the amounts in the financial statements (paragraphs 32–33) are appropriate; and</p>	<p>(a) Agreed</p> <p>(b) Agreed</p>
<p>(c) For the future cash flows related to from an entity's social benefit schemes (see paragraph 34):</p> <p>(i) It is appropriate to disclose the projected future cash flows; and</p> <p>(ii) Five years is the appropriate period over which to disclose those future cash flows.</p> <p>If not, what disclosure requirements should be included?</p>	<p>(c) Agreed</p> <p>(i) Agreed</p> <p>(ii) The time period should be at least 5 years</p>

Matter for comment	Response
<p><b>Specific Matter for Comment 6:</b></p> <p>Do you think the IPSASB should undertake further work on reporting on long-term fiscal sustainability, and if so, how?</p> <p>If you think the IPSASB should undertake further work on reporting on long-term fiscal sustainability, what additional new developments or perspectives, if any, have emerged in your environment which you believe would be relevant to the IPSASB's assessment of what work is required?</p>	<p>Yes – see below</p> <p>One of the areas of such work may be assessing the balance sheet liquidity of the entities that make social benefits.</p> <p>The balance sheet liquidity reflects the coverage of liabilities by financial assets and the comparative maturity pattern of such assets and liabilities. The balance of maturity of assets and liabilities of the entity paying social benefits will indicate solvency, that is, the ability to fulfil its commitments with available stock of liquid assets.</p> <p>The balance sheet liquidity can be estimated on the basis of ratio analysis</p> <p>We suggest using the following indicators. Absolute liquidity ratio Formula: Absolute liquidity ratio = (C+CFI)/CL where:</p> <p>C – cash and cash equivalents; CFI – current financial investment, CL – current liabilities and provisions.</p> <p>This ratio shows the part of current liabilities that can be covered immediately by the social benefits entity. It is believed that its value should not be lower than the following threshold: 0.2-0.25.</p> <p>Overall liquidity ratio is calculated by comparing the total amount of current assets to current liabilities:</p> <p>Formula: Overall liquidity ratio = CA/CL where: CA – current assets.</p> <p>This ratio gives a general description of liquidity, showing the level of coverage of current liabilities by current assets. If the ratio value is equal to one, this indicates that the social benefits entity has sufficient current assets to cover its obligations.</p>

### Statement on Fiscal Sustainability

Certain types of social benefits transfers rights between groups of citizens. In many cases this is an intergenerational transfer, e.g. a commitment to a state pension imposes an obligation on future generations of citizens, as illustrated in Figure 2 below.

Figure 2: Intergenerational impact of social benefits



The model could be used to identify and measure the long term fiscal sustainability of social benefits. A supplementary statement long term financial sustainability could be used to summarise and report a range of decisions taken today which impact on future generations where these are not reported as actual liabilities in the statement of financial position. Such a supplementary statement could also include other potential intergenerational commitments, e.g. long-term subsidies of specific industries.

A future consultative paper may be required on including in the financial reports such a statement of fiscal sustainability. Issues to be considered would include what would be included in the paper, the extent to which revenue flows should be taken into account (or perhaps the required revenue flows be defined), the use of actuarial data, discount rates, handling of uncertainty, the number of years into the future, and so on.

# Response to Consultation Paper on Accounting for Revenue and Non-Exchange Transactions - August 2017, ICGFM

Michael Parry, Chair of the Ad Hoc Committee on International Accounting Standards

Preliminary View	Comments
<p><b>Preliminary View 1 (following paragraph 3.8)</b>            The IPSASB considers that it is appropriate to replace IPSAS 9, Revenue from Exchange Transactions, and IPSAS 11, Construction Contracts with an IPSAS primarily based on IFRS 15, Revenue from Contracts with Customers.            Such an IPSAS will address Category C transactions that:            (a) Involve the delivery of promised goods or services to customers as defined in IFRS 15; and            (b) Arise from a contract (or equivalent binding arrangement) with a customer which establishes performance obligations.            Do you agree with the IPSASB’s Preliminary View 1? If not, please give your reasons (p. 28)</p>	<p>Agree  <i>Comments.</i>            Combining the two IPSAS is logical.            IFRS 15 contains a number of guidelines (including legal) for accounting for exchange transactions. For example, the standard provides provisions on identifying the contract, combination of contracts, contract modification, identifying performance obligations, distinct goods and services, etc.            The application of this approach will avoid the issue of classification of exchange revenue and expenses transactions of the kind that, for example, Ukraine encountered while implementing IPSAS 9, 11 and 23.</p>
<p><b>Preliminary View 2 (following paragraph 3.9)</b>            Because Category A revenue transactions do not contain any performance obligations or stipulations, the IPSASB considers that these transactions will need to be addressed in an updated IPSAS 23.            Do you agree with the IPSASB’s Preliminary View 2? If not, please give your reasons. (p. 28)</p>	<p>Agree  <i>Comments.</i>            In Ukraine, the problem of classification of revenues receipt and implementation of expenses for transfers to citizen was apparent.</p>
<p><b>Specific Matter for Comment 1 (following paragraph 3.10)</b>            Please provide details of the issues that you have encountered in applying IPSAS 23, together with an indication of the additional guidance you believe is needed in an updated IPSAS 23 for:  <ul style="list-style-type: none"> <li>· Social contributions; and/or</li> <li>· Taxes with long collection periods.</li> </ul>           If you believe that there are further areas where the IPSASB should consider providing additional guidance in an updated IPSAS 23, please identify these and provide details of the issues that you have encountered, together with an indication of the additional guidance you believe is needed. (p. 28)</p>	<p>In Ukraine, the entity that should account for non-exchange transactions was not clear – the administering entity or the Treasury?            In Barbados, the lack of any guidance on the treatment of capital grants (i.e. grants for the creation of capital assets) was an issue</p>
<p><b>Preliminary View 3 (following paragraph 4.64)</b>            The IPSASB considers that Category B transactions should be accounted for using the Public Sector Performance Obligation Approach.            Do you agree with the IPSASB’s Preliminary View 3? If not, please give your reasons. (p. 44)</p>	<p>Agreed  <i>Comments.</i>            The IMF GFS 2014 Para 5.10 states “<i>transactions are recorded when the underlying activities, transactions, or other events occur that create the unconditional claims to receive the taxes or other types of revenue</i>”. This is consistent with the obligating event approach</p>

Preliminary View	Comments
<p>Specific Matter for Comment 2 (following paragraph 4.64)</p> <p>The IPSASB has proposed broadening the requirements in the IFRS 15 five-step approach to facilitate applying a performance obligation approach to Category B transactions for the public sector. These five steps are as follows:</p> <p>Step 1 – Identify the binding arrangement (paragraphs 4.29 - 4.35);</p> <p>Step 2 – Identify the performance obligation (paragraphs 4.36 - 4.46);</p> <p>Step 3 – Determine the consideration (paragraphs 4.47 – 4.50);</p> <p>Step 4 – Allocate the consideration (paragraphs 4.51 – 4.54); and</p> <p>Step 5 – Recognize revenue (paragraphs 4.55 – 4.58).</p> <p>Do you agree with the proposals on how each of the IFRS 15 five-steps could be broadened? If not, please explain your reasons (p. 44)</p>	<p>We consider the IFRS 15 approach equally valid for governments, though explanation and examples of its application would be very useful</p>
<p><b>Specific Matter for Comment 3 (following paragraph 4.64)</b></p> <p>If the IPSASB were to implement Approach 1 and update IPSAS 23 for Category B transactions, which option do you favour for modifying IPSAS 23 for transactions with time requirements (but no other stipulations):</p> <ol style="list-style-type: none"> <li>a. Option (b) – Require enhanced display/disclosure;</li> <li>b. Option (c) – Classify time requirements as a condition;</li> <li>c. Option (d) – Classify transfers with time requirements as other obligations; or</li> <li>d. Option (e) – Recognize transfers with time requirements in net assets/equity and recycle through the statement of financial performance.</li> </ol> <p>Please explain your reasons. (p. 44)</p>	<p>Option (e)</p> <p>This is the only approach which is consistent with accrual principles</p>
<p><b>Specific Matter for Comment 4 (following paragraph 4.64)</b></p> <p>Do you consider that the option that you have identified in SMC 3 should be used in combination with Approach 1 Option (a) – Provide additional guidance on making the exchange/non-exchange distinction?</p> <ul style="list-style-type: none"> <li>· Yes</li> <li>· No</li> </ul> <p>Please explain your reasons. (p. 44)</p>	<p>Yes</p> <p>Additional information would be needed to understand the transaction</p>

Preliminary View	Comments
<p><b>Preliminary View 4 (following paragraph 5.5)</b>  The IPSASB considers that accounting for capital grants should be explicitly addressed within IPSAS.  Do you agree with the IPSASB’s Preliminary View 4?  If not please give your reasons. (p. 45)</p>	<p>Agreed  <i>Comments.</i>  At present, there is no guidance on capital grants, this is an issue</p>
<p><b>Specific Matter for Comment 5 (following paragraph 5.5)</b>  (a) Has the IPSASB identified the main issues with capital grants? If you think that there are other issues with capital grants, please identify them.  (b) Do you have any proposals for accounting for capital grants that the IPSASB should consider? Please explain your issues and proposals. (p. 46)</p>	<p><i>Main issues are identified</i>  <i>Comments.</i>  Main issues encountered have been:</p> <ul style="list-style-type: none"> <li>· Timing of recognition</li> <li>· Treatment of revenue from capital grants</li> </ul>
<p><b>Specific Matter for Comment 6 (following paragraph 5.9)</b>  Do you consider that the IPSASB should:</p> <p>(a) Retain the existing requirements for services in-kind, which permit, but do not require recognition of services in-kind; or  (b) Modify requirements to require services in-kind that meet the definition of an asset to be recognised in the financial statements provided that they can be measured in a way that achieves the qualitative characteristics and takes account of the constraints on information; or  (c) An alternative approach.  Please explain your reasons. If you favour an alternative approach please identify that approach and explain it. (p. 47)</p>	<p>We favour an alternative approach (c): services in kind should be recognised if the conditions in (b) apply and in addition “if obtaining the information is cost effective”  To calculate the fiscal indicators used for analysis, these services should be excluded from revenues and expenditures. In particular, for the calculation of state final consumption as the element of GDP in the UN System of National Accounts, it is necessary to know whether, and to what extent, such flows are accounted for in the composition of income and expenditure. This is needed for diagnosing the General Government sector impact on economy.</p>
<p><b>Preliminary View 5 (following paragraph 6.37)</b>  The IPSASB is of the view that non-exchange transactions related to universally accessible services and collective services impose no performance obligations on the resource recipient.  These non-exchange transactions should therefore be accounted for under The Extended Obligating Event Approach.  Do you agree with the IPSASB’s Preliminary View 5?  If not, please give your reasons. (p. 56)</p>	<p>Agreed</p>
<p><b>Preliminary View 6 (following paragraph 6.39)</b>  The IPSASB is of the view that, because there is no obligating event related to non-exchange transactions for universally accessible services and collective services, resources applied for these types of non-exchange transactions should be expensed as services are delivered.  Do you agree with the IPSASB’s Preliminary View 6?  If not, please give your reasons. (p. 56)</p>	<p>Agreed  Such transactions are reflected in SNA in the same way (provision of collective services by General Government Sector). The obligations stay the same.</p>

Preliminary View	Comments
<p><b>Preliminary View 7 (following paragraph 6.42)</b>  The IPSASB is of the view that where grants, contributions and other transfers contain either performance obligations or stipulations they should be accounted for using the Public Sector Performance Obligation Approach (PSPOA) which is the counterpart to the IPSASB’s preferred approach for revenue.  Do you agree with the IPSASB’s Preliminary View 7?  If not, please give your reasons (p. 57)</p>	Agreed
<p><b>Preliminary view 8 (following paragraph 7.18)</b>  The Board considers that at initial recognition, non-contractual receivables should be measured at face value (legislated amount) of the transaction(s) with any amount expected to be uncollectible identified as an impairment.  Do you agree with the IPSASB’s Preliminary View 8?  If not, please give your reasons (p. 61)</p>	Agreed
<p><b>Preliminary View 9 (following paragraph 7.34)</b>  The IPSASB considers that subsequent measurement of non-contractual receivables should use the fair value approach.  Do you agree with the IPSASB’s Preliminary View 9?  If not, please give your reasons. (p. 63)</p>	Agreed
<p><b>Specific Matter for Comment 7 (following paragraph 7.46)</b>  For subsequent measurement of non-contractual payables do you support:  (a) Cost of Fulfilment Approach;  (b) Amortized Cost Approach;  (c) Hybrid Approach; or  (d) IPSAS 19 requirements?  Please explain your reasons. (p. 65)</p>	We support option (a), This is the simplest and most logical approach. It allows the identification of the amount in accordance with the approaches defined by IPSAS 19 “Provisions, contingent liabilities and contingent assets”.

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- § Translated books Adorno, T. W. *Negative Dialectic* (Frankfurt: Suhrkamp, 1966). *Negative Dialectics*, E. B. Ashton (trans) (1973) New York, Seabury Press.
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- § Dorotinsky, Bill (2008) *Public Financial Management Reform: Trends and Lessons*, ICGFM DC Forum, June.
- § <http://icgfm.blogspot.com> (6 September 2008).

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