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Accrual practices and reform experiences in OECD countries – Results of the 2016 OECD Accruals Survey

by
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Over the past two decades, a growing number of governments have begun moving away from pure cash accounting toward accrual accounting. In the wake of these reforms, the budget presentation, audit techniques, and accounting standards setting and consolidation practices have evolved significantly. This paper reviews the current accrual practices in OECD countries, challenges associated with accruals reforms, and assesses the benefits achieved. It finally considers initiatives in OECD countries to make better use of accrual information in the future.
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Keywords: accrual accounting, accrual budgeting, accounting practices, budgeting practices, consolidation, external audit, accounting standard setting.

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Foreword

The OECD Accruals Survey is carried out yearly by the OECD Secretariat since 2003. The present Survey is an update of results from previous Surveys of member countries' selected accounting and budgeting practices at the core national government level as well as the accounting treatment of specific transactions, consolidation practices, and standard-setting frameworks.

In addition, as many member countries have implemented accruals reforms in recent years, this Survey aims at gaining a better understanding of the design of these reforms, implementation challenges, and associated benefits.

The Survey was sent to Ministries of Finance and equivalent bodies of all thirty-four (34) OECD countries: Australia (AUS), Austria (AUT), Belgium (BEL), Canada (CAN), Chile (CHL), the Czech Republic (CZE), Denmark (DNK), Estonia (EST), Finland (FIN), France (FRA), Germany (DEU), Greece (GRC), Hungary (HUN), Iceland (ISL), Ireland (IRL), Israel (ISL), Italy (ITA), Japan (JPN), Korea (KOR), Luxembourg (LUX), Mexico (MEX), the Netherlands (NLD), New Zealand (NZL), Norway (NOR), Poland (POL), Portugal (PRT), the Slovak Republic (SVK), Slovenia (SVN), Spain (ESP), Sweden (SWE), Switzerland (CHE), Turkey (TUR), the United Kingdom (GRB), and United States of America (USA).

Answers from all 34 Ministries of Finance were collected from November 2015 to March 2016.

The OECD Accruals Survey's results will form the basis for a joint publication with the International Federation of Accountants and the *Accountability! Now!* initiative.

Summary

Around three quarters of OECD countries have adopted accrual accounting for their year-end financial reports, although they have not necessarily implemented all aspects of what may be regarded as a full accrual accounting framework. In particular, countries have progressed differently in populating their balance sheet: for example, civil service pensions and natural resources are not reported yet by a majority of countries.

More than a quarter of OECD countries prepare their annual budgets on an accrual basis. However, the Survey does not evidence shared understanding and practices with regards to the definition and meaning of accrual budgeting in terms of content and presentation of budgets, and nature of appropriations. The use of cash appropriations in a large majority of countries, including some of those that are using accrual budgeting to measure the impact of current and new public policies, suggests that governments are wary of the volatility and discretion in accrual valuations, with regards to control over resources spent by ministries and departments.

Looking at the accounting and budgeting framework as a whole, there are two dominant models: i) a majority of countries prepare accrual financial statements and cash budgets and budget execution reports; ii) a significant minority of countries prepare accrual financial

statements and budgets, the latter incorporating either accrual, or cash, or both accrual and cash appropriations and related budget execution reports.

Despite a large majority of number of countries having adopted accrual accounting, the direct adoption of international accounting standards (IPSAS or IFRS) by national governments remains very low. Countries seem to favour national standards in order to be able to accommodate a number of specific deviations. However, more than one third of standard-setters (in most cases, the ministry of finance or an independent standard setting board) use IPSAS or IFRS as primary or explicit references for developing the national standards.

Only 15% of OECD countries provide an overview of the public sector as a whole in their financial statements, and another 20% of countries do so at the federal level. Few countries declare that they plan to expand the coverage of their financial statements. Constitutional provisions on the independence of local governments, the technical and practical challenges of consolidation, combined with a lack of appreciation of the need and use the full view of public finances in financial statements, may be factors that explain that situation.

In all OECD countries, financial statements are subject to independent external control or audit, but only 62% of respondents indicated that their supreme audit institutions (SAIs) provide an opinion on the year-end financial report according to international auditing standards. Among this group of countries, a high proportion of the audit opinions are qualified.

A majority of OECD countries have completed their reform programs. Despite variations in the timescale, duration, and cost of reforms, countries encountered many similar challenges for preparing and implementing accrual accounting, including capacity building, establishing an inventory and valuation of assets and liabilities, the design and roll-out of new IT systems, and preparation of consolidated fiscal reports. A majority of countries expressed satisfaction that the reforms' objectives with regards to transparency and accountability have been fully achieved. Other objectives are not yet fully met by a majority of respondents. In particular, the use of full accrual costs for evaluating the management and performance of government entities is not widespread. A number of countries, including early adopters of accrual accounting and/or budgeting, note that politicians and the public at large have limited interest in accrual financial information. Several initiatives are on-going to address these issues, which undermines otherwise successful accruals reforms.

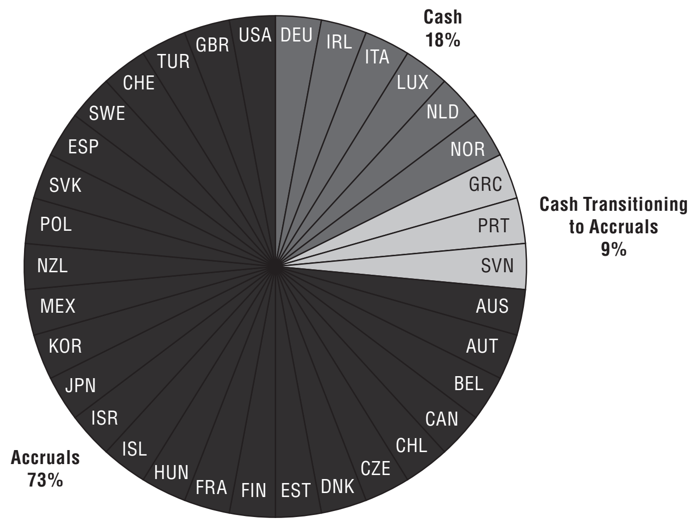
1. Accrual accounting Practices

1.1. Accounting basis

Annual financial reports are established on an accrual basis in the bulk of OECD countries (Figure 1):

- Twenty-five countries (73 %) identify their annual financial reports as being based on accrual accounting.[1] This figure is to be compared with results of the first OECD Accruals Survey, dating back to 2003: at that date, only a quarter of countries were declaring using an accrual accounting system. The accrual accounting frameworks of countries take a number of forms. At one end of the spectrum are countries (such as New Zealand), which has embraced accrual as the basis for fiscal policy, budgeting, financial management, and reporting. At the other end, others (such as Japan) produce accrual based financial

Figure 1. **OECD Countries: Accounting Basis for Annual Financial Reports**



Notes: The figure above, and following figures, reflects the answers provided by countries unless stated otherwise. Countries that answered as having both accrual financial statements and cash financial reports (Czech Republic and Hungary) are classified as "Accruals".
Luxembourg is currently using a modified cash accounting system and has therefore been classified as "Cash". However, it is planning a transition to accrual accounting (see Figure 7).
Source: OECD Accruals Survey (2016).

statements as supplementary information to the cash based accounts. In between, there are countries that produce accrual based annual financial statements as their main or official accounts – not supplementary information – in addition to producing cash based reports to show compliance with cash budgets;

- Another three countries (9%) indicated that they are in the process of transitioning to accrual accounting;[2]
- Six countries (18%) indicated that they follow cash accounting.[3] Among this group, 2 countries indicated that they are considering whether to require ministries and departments (Ireland), and agencies (Norway) to report on an accruals basis in addition to continuing to report on a cash basis; two countries (Italy and Luxembourg) have an ongoing reform process to move to accrual accounting, though progress has been limited. Only two countries (Germany and the Netherlands) indicated that they do not have any plans to adopt accruals, although one (the Netherlands) has agencies reporting on an accrual basis.

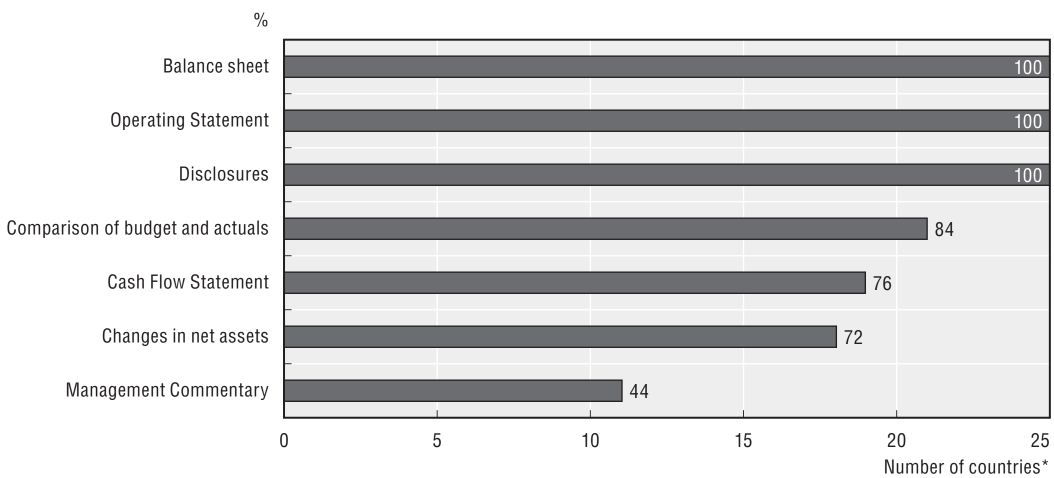
1.2. Presentation of Annual Financial Reports

This section discusses the presentation of the annual financial report, and identifies which statements (balance sheet, income statement, cash flows, changes in net assets, comparison of budget and actuals) and comments (disclosures and management commentary) are established at year-end by Governments. The presentation of financial reports is important because it affects the comprehensiveness and understandability of annual financial reports.

Countries that are following cash accounting or are transitioning to accruals establish only one primary statement at year-end. This group of countries provides either a comparison of budget and actuals or a cash flow statement with notes. The main objective the annual financial report is indeed to facilitate the discharge of accountability. Half of them also produce a simplified or incomplete balance sheets and income statements as supplementary information to budget outturn reports (Germany, Greece, Ireland, Portugal, and Slovenia).

More information is provided in accrual basis financial reports, although they do not always include all key statements and disclosures required by international standards (Figure 2). All countries that have adopted accrual accounting prepare a balance sheet (or statement of financial position), income statement (or statement of financial performance), and disclosures. Fewer countries prepare a statement of cash flows and changes in net assets. This could be explained by the fact that cash flow statements are perceived as redundant with other cash reports, in particular the comparison of budget and actuals, and changes in net assets are disclosed in the notes to the financial statements (France), or a concern with not overloading users with too many statements, and simplifying therefore as much as possible the presentation of the financial statements in the public sector. Less than half of countries establish a commentary to accompany the financial report.[4] This may suggest that they consider that the analysis of the government's financial position, financial performance, and cash flows is provided at other stages of the budget process. Countries that indicated they do not establish a comparison of budget and actuals in their financial statements do so in separate budget execution reports.

Figure 2. **OECD Countries: Presentation of Annual Financial Statements**



Source: OECD Accruals Survey (2016), based on the answers of the 25 countries implementing accrual accounting.

1.3. Content of Annual Financial Reports

This section discusses the content of the annual financial report, with regards to assets, liabilities, expenses or expenditures, revenues, and financial commitment. It allows the assessment of whether governments, regardless of the accounting basis, provide a complete picture of their financial operations and their impact on the financial position.

All countries reporting on a cash basis provide financial information that is not restricted solely to cash transactions. All but one of the six countries reporting on a cash basis provides information on cash balances, debt, guarantees, and commitments. This would suggest that countries operating on a cash basis acknowledge the need for inventorying and measuring assets and liabilities. Some countries also keep track of the stock and value of a number of other assets and liabilities. Germany and Norway, in particular, disclose the value of selected assets and liabilities. Norway also discloses the value of its natural resources albeit in the budget. The three countries that are transitioning to accrual accounting supply additional information on accrued expenses and tax receivables (Greece, Slovenia), or fixed assets (Portugal).

Countries that report on an accrual basis have progressed differently in populating their balance sheet with assets and liabilities (Table 1). All countries report their financial liabilities and assets, and accrued expenses. Other elements are reported in a less consistent way:

- A majority of countries that have adopted accrual accounting disclose on the balance sheet land and buildings (92%), infrastructure (92%), tax receivables (85%), defence assets and inventories (79%), and derivatives (75%). This suggests that operational issues for inventorying and measuring these items have been overcome. However, remaining difficulties are evidenced by the relatively large number of financial statements that received a qualified audit opinion due to issues with the reporting of fixed assets (see below);
- For civil and military service pension liabilities, practices vary greatly: 39% of countries record them on the balance sheet, 14% disclose them in the notes, and 36% do not disclose them at all. Among these last two groups of countries, some countries consider indeed that their employees –civil or military – do not have any *contractual* pension entitlements.[5]

  Similar reasons are mentioned for not reporting social benefits (53 % of countries do not report them).[6] The lack of reference accounting treatment in international standards can also explain this situation.

  Some countries mentioned that the sustainability of their pensions and social benefits policies was assessed in the *Long-Term Fiscal Sustainability Report* (also called *Intergenerational Report*). This report is able to assess both future liabilities and taxation to fund the liabilities, which compares future revenues and spending and therefore highlights possible fiscal imbalances, rather than in the balance sheet;
- With regards to PPPs, 36% of countries do not report the assets and liabilities on the balance sheet. This could be explained by technical difficulties for inventorying contracts and evaluating the related debt, or implementing the control approach required by international standards. Similarly to what was mentioned for pensions and social benefits, there might be a reluctance to report on potentially significant amounts of debt related to these contracts;
- Natural resources and heritage assets are reported respectively by 11 and 43% of governments, which could be explained by the lack of reference accounting treatment in these areas, and difficulties for establishing reliable and meaningful valuations. The other reason, for countries such as Australia, is that the Federal Government is not responsible for natural resources, which are the responsibility of State jurisdictions.

Table 1. **OECD Countries: Reporting Practices for of Selected Assets and Liabilities in Annual Financial Statements**

	Balance sheet	Disclosure	Not reported	N/A
Tax receivables	AUS, AUT, CAN, CHL, CZE, DNK, EST, FRA, GRC, HUN, ISL, ISR, JPN, KOR, NZL, POL, SVK, SVN, ESP, SWE, CHE, TUR, GBR, USA	BEL, MEX,	FIN, PRT	
Natural resources	ISR, SVN, SWE	EST, USA	AUS, AUT, CAN, CHL, CZE, FIN, GRC, HUN, ISL, KOR, MEX, NZL, POL, PRT, ESP, CHE, TUR, GBR	BEL, DNK, FRA, JPN, SVK
Land buildings	AUS, AUT, BEL, CAN, CHL, CZE, DNK, EST, FIN, FRA, HUN, ISR, JPN, KOR, MEX, NZL, POL, PRT, SVK, SVN, ESP, SWE, CHE, TUR, GBR, USA		GRC, ISL	
Infrastructure assets, excluding PPPs	AUS, AUT, BEL, CAN, CZE, DNK, EST, FIN, FRA, HUN, ISR, JPN, KOR, MEX, NZL, POL, PRT, SVK, SVN, ESP, SWE, CHE, TUR, GBR, USA		CHL, GRC, ISL	
PPP assets and liabilities	AUS, AUT, CAN, DNK, EST, FIN, FRA, ISR, JPN, KOR, NZL, POL, SVK, TUR, GBR, USA	CZE, HUN, MEX, ESP	BEL, CHL, GRC, ISL, PRT, SVN,	SWE, CHE
Heritage assets	AUS, AUT, CAN, CZE, FIN, FRA, NZL, POL, SVN, ESP, SWE, GBR	ISR, KOR, USA	BEL, CHL, DNK, GRC, HUN, ISL, MEX, PRT, CHE, TUR	EST, JPN, SVK
Defence assets and inventories	AUS, AUT, BEL, CAN, CZE, DNK, EST, FRA, HUN, ISR, JPN, MEX, NZL, POL, PRT, SVK, SVN, ESP, SWE, TUR, GBR, USA		CHL, FIN, GRC, ISL, KOR, CHE	
Derivatives	AUS, AUT, BEL, CHL, CZE, DNK, EST, FIN, FRA, ISR, JPN, KOR, NZL, SVK, SVN, ESP, SWE, CHE, TUR, GBR, USA	CAN, HUN	GRC, ISL, PRT	MEX, POL
Civil and military service pensions	AUS, CAN, EST, ISR, ISL, KOR, NZL, SVK, SWE, GBR, USA	AUT, FIN, FRA, CHE	BEL, CHL, CZE, DNK, GRC, MEX, PRT, SVN, ESP, TUR	HUN, JPN, POL
Social benefits	CAN, EST, FRA, ISR, JPN, NZL, POL, PRT, SVK	HUN, USA	AUS, AUT, BEL, CHL, DNK, FIN, GRC, ISL, KOR, MEX, ESP, SWE, CHE, TUR, GBR	CZE, SVN

Note: In Australia, natural resources are owned by State (i.e. regional) governments and therefore not reported in the Federal Government Financial Statements.
Source: OECD Accruals Survey (2016), based on the answers of the 28 countries that report on accrual or cash transitioning to accrual basis.

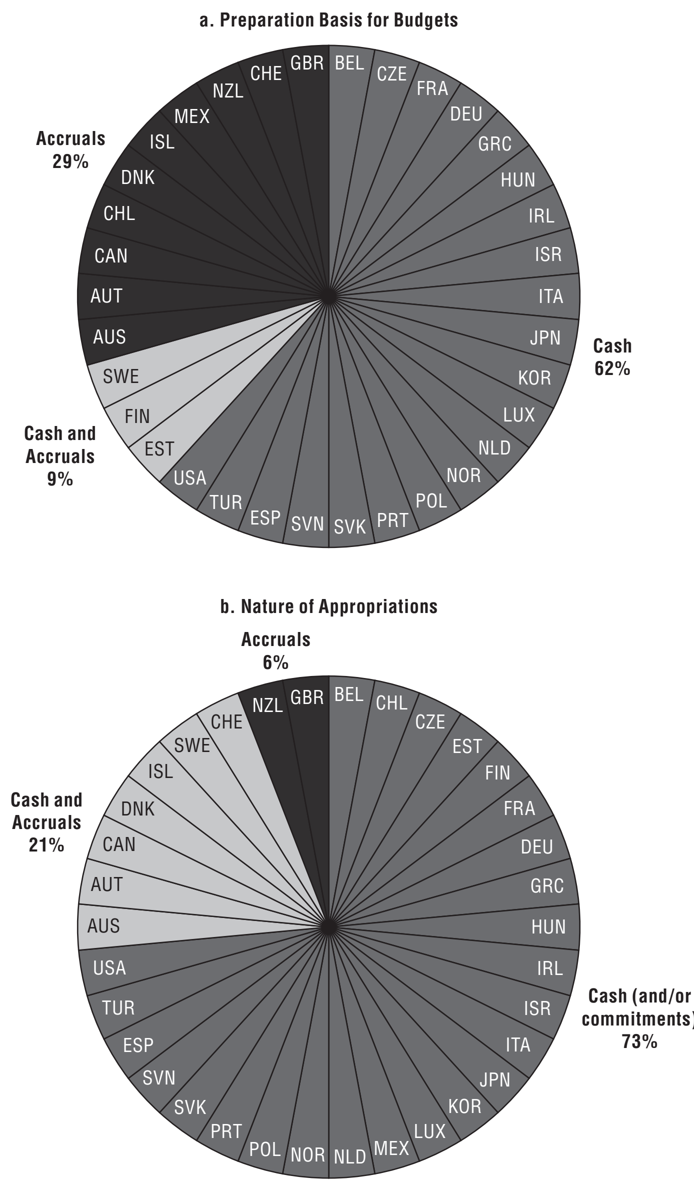
2. Accrual Budgeting practices

While a budget is prepared on the basis of a range of concepts and principles, for the purposes of this report the term "preparation basis of budgets" has been used to refer to the basis on which the financial implications of the budget policies and programs are reported and measured in the budget. This section also discusses Parliamentary appropriations, which in some countries are distinct from the "budget".[7] They are defined for the purpose of this report as "authorization by an act of parliament to permit government entities to incur obligations, and/or to pay for them from the treasury", even though appropriations' definition may differ between countries.

A majority of OECD countries prepare their budgets on cash or modified cash basis (Figure 3.a):

- Twenty-one countries (or 62%) use the cash basis for preparing the budget and appropriations. However, within that group, many countries provide information on debt, commitments, and guarantees in the budget, and therefore do not qualify their system as "cash basis" *per se*. In particular, commitments are considered as a special feature of budget systems that do not fall neatly into the cash or accrual categories.[8] In this group, one country (Luxembourg) plans to adopt accrual budgeting over the medium-term;

Figure 3. **OECD Countries: Selected Budgeting Practices**



Note: (Figure 3.a) Sweden and Finland are presented in figure in the "Cash and Accruals" category as the budget includes both accrual and cash elements, Estonia is planning a transition to accrual accounting to be completed by 2017.
Source: OECD Accruals Survey (2016).

- Three countries (or 9%) prepare budgets that are comprised of some items budgeted on an accrual basis: this group of countries has been designated as "Cash and Accrual".[9] Among this group, one country (Estonia) is well advanced in its preparatory work for a move to full accrual budgeting commencing with the 2017 budget. Other countries have indicated that despite forecasting some elements of their budget on an accrual basis, they did not contemplate a transition to accrual budgeting;
- Ten countries (or 29%) have adopted the accrual basis for the preparation of their budgets. A majority of countries within that group presents a full set of prospective financial statements (Australia, Canada, Denmark, New Zealand, Switzerland, and the United Kingdom). Other countries establish incomplete or simplified versions of the financial statements (Austria, Iceland, Chile, and Mexico).

Accrual budgeting does not entail systematically the use of accrual appropriations (Figure 3.b). Among the countries that use accrual budgeting, 2 countries (New Zealand and the UK) use full accrual appropriations.[10] Other countries within that group mix accrual and cash appropriations (Australia, Austria, Denmark, Iceland, and Switzerland), or use cash appropriations only (Canada, Chile, Mexico). This would suggest that countries may be are wary the volatility and discretion in accruals valuations (in particular with regards to provisions and depreciations), and believe that cash appropriations allow a better control over resources spent by ministries and departments, even when they are using accrual forecasts to measure the impact of current and new public policies.

Appropriations are used for authorising current and capital expenditures in a large majority of countries. All countries authorise annually the capital and current expenses or expenditures.[11] In more than half of countries, authorisations are also granted for incurring commitments. Three countries (Australia, Iceland, and the United Kingdom) indicate that an annual authorisation is also granted by the Parliament for incurring pension liabilities.

Overall, the survey draws a varied picture of budgeting practices. Budgeting is indeed an area where, contrary to accounting, standards or generally accepted principles have not been developed, and practices are related to the ways the Parliament authorises and controls public spending, and the nature of the national fiscal targets and rules. Categorising budget frameworks between cash and accrual therefore proves difficult – these are indeed accounting concepts that may not fully reflect the specificities of budget practices.

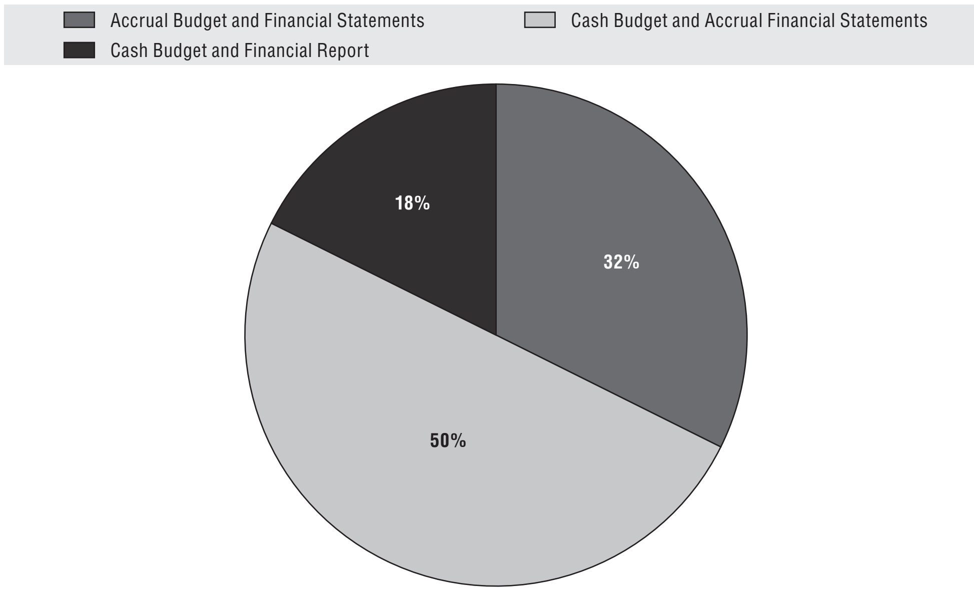
Looking at the accounting and budgeting framework as a whole, there are two dominant models (Table 2). Almost a half of countries (50%) prepare accrual financial statements and cash budgets and budget execution reports. A third of countries (32%) prepare accrual financial statements and budgets, the latter incorporating either accrual, or cash, or both accrual and cash appropriations and related budget execution reports. The remaining countries (18%) prepare cash budget and financial reports.

Table 2. **OECD Countries: Accounting Basis for Annual Financial Reports and Preparation Basis for Budgets**

	Countries
Accrual financial statements and budgets (1)	AUS, AUT, CAN, CHE, CHL, DNK, EST, GBR, ISL, MEX, NZL
Accrual financial statements and cash budgets (2)	BEL, CZE, ESP, GRC, FIN, FRA, HUN, ISR, JPN, KOR, POL, PRT, SVK, SVN, SWE, TUR, USA
Cash financial reports and budget	DEU, IRL, ITA, LUX, NLD, NOR

Notes: (1) Includes Estonia, which is transitioning to accrual budgeting in 2017; (2) Includes countries with cash transitioning to accrual financial statements (GRE, POR, and SVN) and budgets comprised of cash and accrual elements (SWE and FIN).
Source: OECD Accruals Survey (2016), based on the answers of the 28 countries that report on accrual or cash transitioning to accrual basis.

Figure 4. **OECD Countries: Accounting Basis for Annual Financial Reports and Preparation Basis for Budgets**



3. Institutional coverage of financial reports and budgets

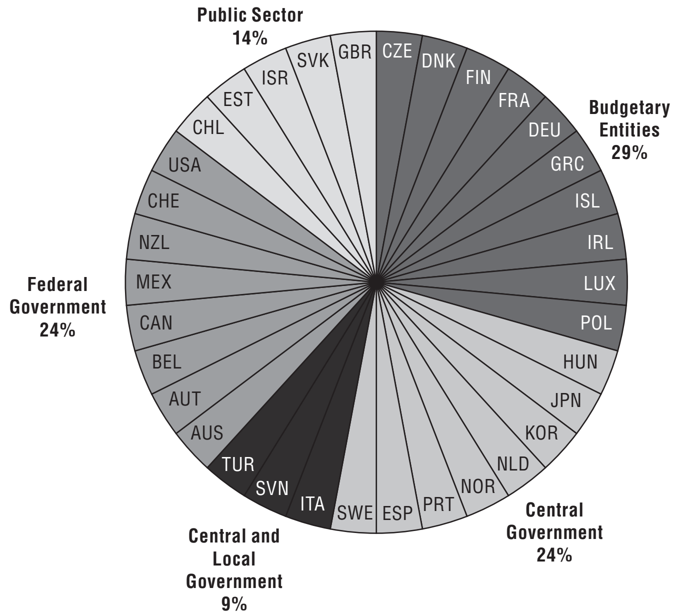
As fiscal activity is carried out by different levels of government, this section discusses what public sector entities are part of budgets and financial reports, and whether fiscal reports provide a full understanding of the amount and composition of public spending and revenue, and the related accumulation of government assets and liabilities.

Regardless of the accounting basis, very few countries present a full overview of the public finances across levels of government in their financial statements (Figure 5). At one end of the spectrum, five (or 14%) countries establish financial statements that encompass the central and local levels of government, and state owned corporations; another group of eight (or 24%) countries establish financial statements that cover all entities over which the national or federal government exercises authority (control). At the other end of the spectrum, eight (or 29%) of countries cover only the budgetary entities in their annual financial statements. Within that group, a number of countries provide supplementary information to the public and parliament. For example, Portugal presents a number of aggregated figures in the year-end financial statements for the regional and local governments.

The variety of practices with regards to consolidation is explained both by the consolidation criterion and national circumstances:

- A majority of countries indicates that the scope of their financial statements is defined by law. In this group of countries, local and regional governments are more often included in the consolidated financial statements than in countries that follow the "control" criterion for consolidation;
- About one quarter of respondents uses "control" as their consolidation criterion. In this group of countries, local and regional governments, or social security funds may not be consolidated in the financial statements of the government because they are constitutionally or legally independent;

Figure 5. **OECD Countries: Institutional Coverage in Annual Financial Report**



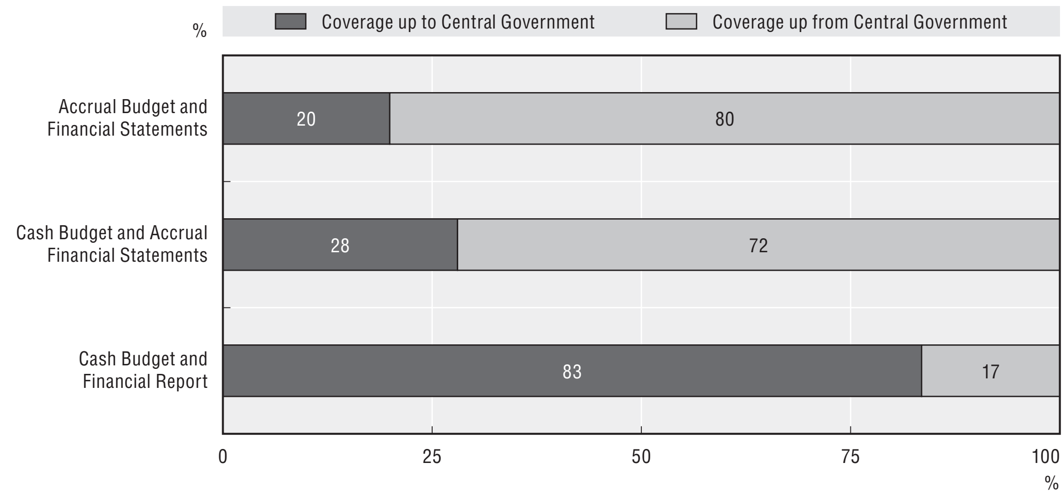
Note: Some of the countries classified in the category "Central Government" have specified that their financial statements include Social Security Funds (HUN, NLD, NOR, PRT, ESP); Countries classified in the category "Central and Local Governments" includes the Social Security Funds; Iceland's financial statements will present going forward a consolidated view of the public sector as required by the Organic Budget Law adopted in 2015.
Source: OECD Accruals Survey (2016).

- Some countries mentioned technical or operational difficulties as factors explaining the limited coverage of their financial statements;
- Finally, some countries mentioned that the full view of public finances was provided in fiscal statistics, and questioned the need and use of such information in financial statements.

It is to be noted that the coverage of fiscal statements tend to be wider in the group of countries that is implementing both accrual budgeting and accounting than in other groups: 80 percent of the countries within that group have financial statements that cover the general or federal government, or the public sector as a whole (Figure 6).

In a majority of countries, financial statements have broader coverage than the budget. A majority of governments that prepare consolidated financial statements do not establish budgets with a similar coverage.[12] The few countries that have aligned the coverage of fiscal reports, notably the United Kingdom[13] and New Zealand, consider that harmonisation is beneficial for a number of reasons including producing consistent and comparable figures which are believed to be more transparent, understandable, and easier to use. Where the coverage is not aligned, this likely reflects the fact that the budget and financial statements do not serve the same purpose: while the budget is mainly the vehicle used by the legislature for deciding how expenditures should be allocated, financial statements provide a more global view of the financial situation of the public sector, including public corporations and sub-national governments in certain cases.

Figure 6. **OECD Countries: Institutional Coverage by accounting and budgeting model**



Source: OECD Accruals Survey (2016).

With regards to consolidation, concepts and practices vary between countries. The concept of consolidation is understood differently by countries: entities that receive transfers disclosed in the Government's budget, or entities reported at equity value in the balance sheet are considered as "consolidated" in the budget or financial statement by certain countries. For those countries that do undertake a consolidation according to international standards,[14] some establish consolidated financial statements by "sub-sectors" (Slovak Republic, for example). About half of countries rely on a harmonised chart of accounts, while another half uses consolidation packages or templates to gather information necessary for consolidation purposes. Most governments use an automated integrated financial management information system (IFMIS) to undertake the consolidation. It should be noted that there are continuing problems in this area as evidenced by the relatively large number of financial statements that received a qualified audit opinion due to the issues with intragroup eliminations, as explained in the following section.

4. Standard setting and audit practices[15]

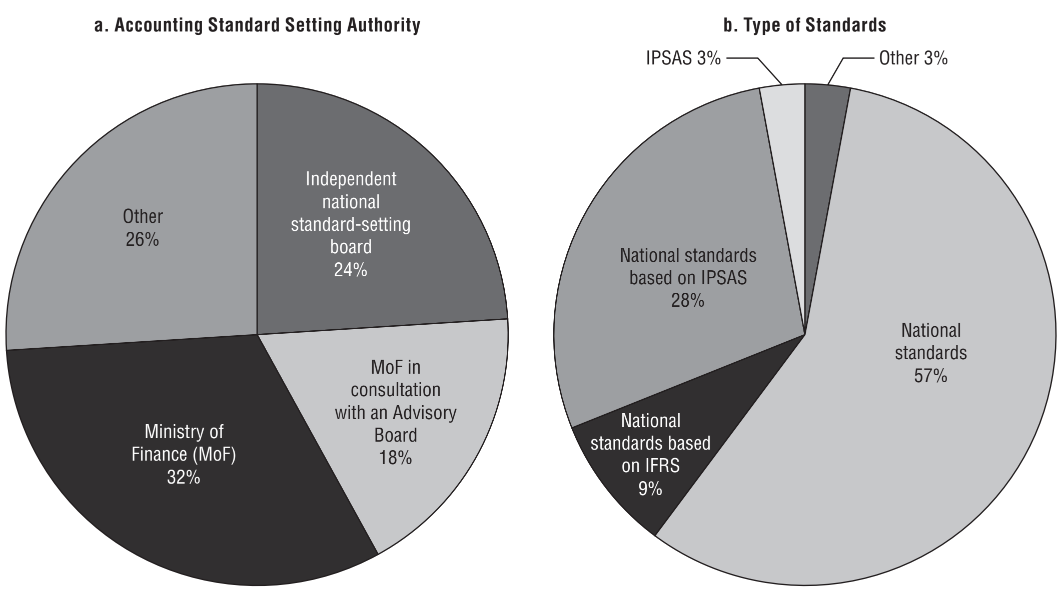
4.1. *Standard-Setting Practices*

This section discusses the various practices for setting accounting standards. Financial reporting standards – also referred to as accounting standards – define how financial statements are to be prepared and specific items are to be identified, recognised, valued and reported in financial statements. Governments may set standards directly (e.g., through the Ministries of Finance – MoF) or create independent standard-setting authorities. Regardless of the standard-setting process, the accounting standards may be specific to the country, or derived from international standards. Understanding these mechanisms is important to assess the level of quality and consistency of accounting practices in OECD countries.

The MoF is the standard-setting authority in about half of OECD countries (Figure 7a). The level of guidance on accounting principles and standards stipulated in the law varies according to countries. Where the legal framework only defines general principles, the MoF is in most cases tasked with setting out the accounting standards, either directly (32% of cases) or in consultation with an advisory board (18% of countries). Independent national standard setting boards are responsible for standard-setting in a further 24% of countries (Australia, Canada, France, Israel, Mexico, New Zealand, and USA).

Nearly all countries develop national accounting standards, but use international frameworks as a reference (Figure 7b). Standards are established at national level in all but one country. International standards (IFRS, IPSAS, or statistics frameworks[16]) are considered as an explicit or primary reference for developing national standards in 40% of countries. Other countries often mention them as guidance. Countries seem to favour national standards in order to be able to accommodate a number of specific deviations, such as limiting the quantity of disclosures (for example, Sweden), defining boundaries for the financial statements that are aligned with the ones used in the budget and the fiscal statistics (United Kingdom, Australia, or New Zealand), or reflecting the specificities of the national legal frameworks and public policies (France, for example, with regards to the accounting treatment for the public service pension system). In Switzerland, which is the only country that directly adopts IPSAS, the Cabinet of the Government can authorise deviations from IPSAS.

Figure 7. **OECD Countries: Accounting Standard Setting Authority and Type of Standards**



Note: In figure 3.a, Other is Government (Belgium, Hungary, Ireland, Poland, Sweden, and Switzerland); Comptroller General of the Republic (Chile); and Specific Committee (Germany); In figure 3.b, Other is National Standards based on European System of Accounts (Belgium).

Source: OECD Accruals Survey (2016).

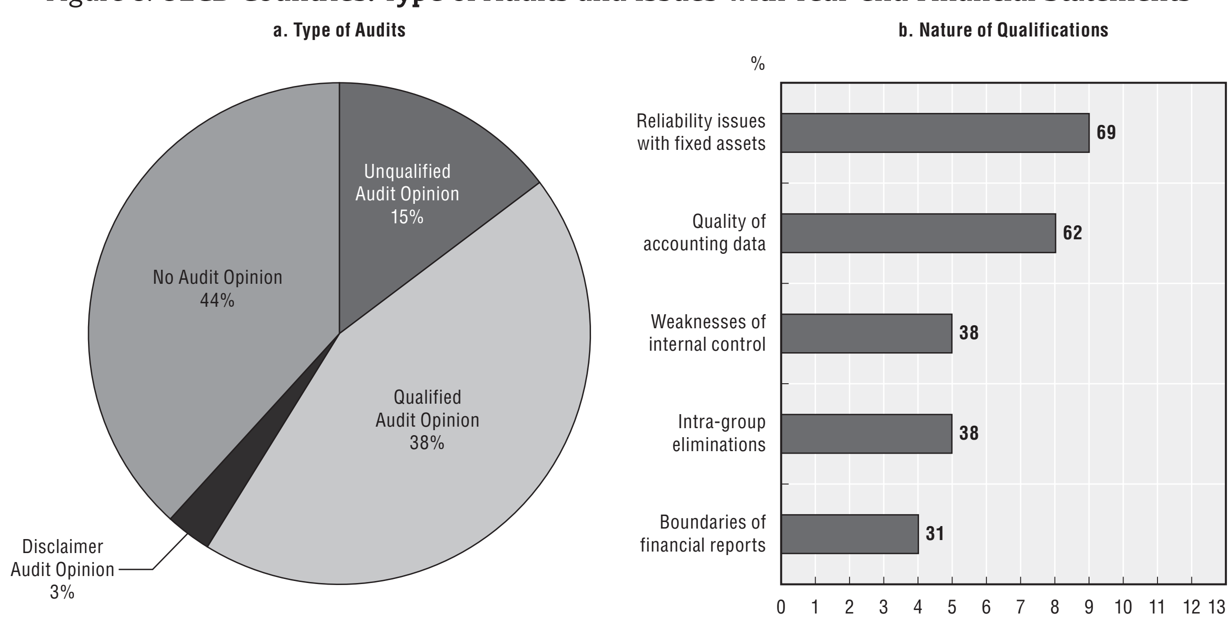
4.2. Audit practices

This section discusses the types of external controls and audits on annual financial reports. This function can be exercised by supreme audit institutions (SAIs), which are independent public institutions with a mandate for overseeing the management of public funds and the quality and credibility of the government's' reported financial data, or audit firms. The importance of high quality and independent audit as countries move towards accrual accounting cannot be over-emphasised: as governments adopt accrual accounting, there will be an increasing need for skills and judgments to prepare financial statements, which makes particularly important that audits provide the necessary assurances to the users that, among other things, the statements have been prepared with due care, are free from materials errors or misstatements, and comply with relevant standards and legal requirements.

The annual financial reports are subject to some form of external control and audit in all OECD countries (Figure 8.a). A majority of respondents (56%) indicated that their supreme audit institutions (SAIs) follow international auditing standards and provide an opinion on whether the financial statements present a true and fair view.[17] Another group of countries declare that the financial statements are audited, or controlled, by the SAI in accordance with national requirements set out in the constitution or law, which require in most cases to assess the compliance of annual expenditures with the Parliamentary authorisations, and regulations on financial controls.

A high proportion of the audits are qualified (Figure 8.b). In the group of countries where an audit opinion is provided on the financial statements according to international audit standards, a large majority are qualified. Issues with the inventory and valuation of fixed assets (in particular defence equipment) and the general quality and reliability of accounting data lead to the qualifications in a majority of cases. Issues with boundaries of government financial reporting and intra-group eliminations are also mentioned by around half of the countries, which may not fully reflect the scale of the challenges associated with consolidations, as few countries have started establishing consolidated financial statements. Continuing engagement and cooperation with the SAI is often mentioned by respondents as an important success factor for implementing accrual accounting, and improving the reliability of the financial statements over time.

Figure 8. **OECD Countries: Type of Audits and Issues with Year-end Financial Statements**



Note: Figure 6a: where no audit opinion is provided according to international auditing standards, SAI undertake compliance audits or other types of controls; Figure 6b: Percentage of countries that received a qualified opinion on their year-end financial statements, for the 13 countries that have received a qualified opinion on their financial statements.

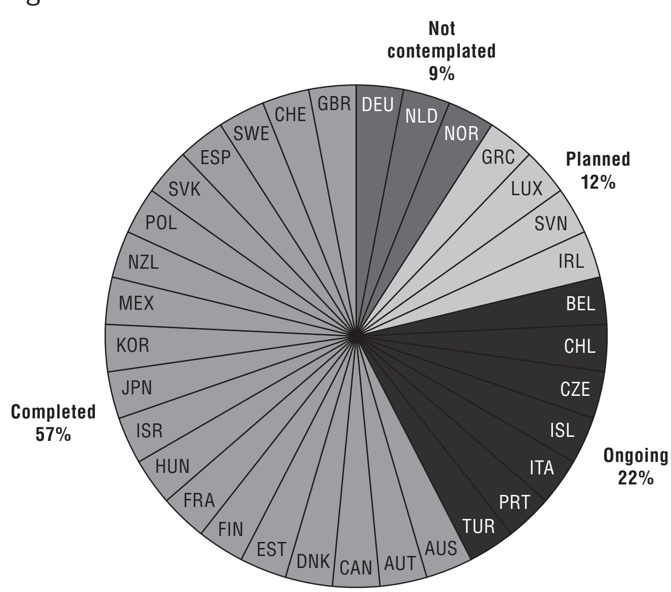
Source: OECD Accruals Survey (2016).

5. Accrual Reforms[18]

5.1. *Status of Reforms*

A majority of countries stated that they have completed their reform programmes (Figure 9).[19] This highlight a major shift in public accounting practices since the 2000s, as only 24% of countries reported using accrual accounting in the first OECD Accruals Survey (2003). However, the objectives and scale of reforms vary significantly: the United Kingdom's reforms involved a transition to accrual for the whole of the public sector and the introduction of accrual budgeting, while France's reforms are aimed at implementing accrual accounting at the budgetary central government level only. In addition, as discussed earlier, the accrual frameworks show a great deal of variations. Another group of countries described their reforms as ongoing, some of them linked to the possible development of European Public Sector Accounting Standards (EPSAS). Few countries have not implemented nor contemplate any accrual reform. The main reasons for this are the lack of political support, concern that the benefits are unlikely to exceed costs (Germany), and satisfaction that cash based budgets and financial reports (with interest budgeted and accounted for on an accrual basis) provide all the necessary information (the Netherlands).

Figure 9. **OECD Countries: Status of Accrual Reforms**



Source: OECD Accruals Survey (2016).

The adoption to accrual accounting was often part of, and intended to facilitate, wider public management reform initiatives. The motivation for reform mentioned most often in the Survey include presenting a fair view of the public finances, assessing the full costs of government operations, introducing or enhancing a performance culture, and modernising public management. Having similar presentation and preparation basis for all fiscal reports (including statistics) is a motivating factor for some countries that have adopted or are transitioning to accrual budgeting in addition to accrual accounting. The government or the MoF sponsored the reforms in a majority of countries. The MoF (often through the budget office or the treasury) were the agencies responsible for the preparation, monitoring, and implementation of the reforms in most countries.

The results of the Survey do not allow evaluating precisely the duration and costs of the reforms. The full implementation of the reform took several years in all countries. Duration however vary greatly: for example, Sweden considers that the reforms took about twenty years to complete, while Estonia completed its reform in two years. A majority of countries have mentioned a ten-year period for completing their accrual accounting reform. Costs seem to vary significantly depending on the scale of the IT systems upgrades and consulting services, but only one country provided detailed information. In New Zealand, the public management reforms as a whole – of which accrual accounting and budgeting was only a part – cost an estimated NZD 160 – NZD 180 million, or 0.1% of expenses over the period of implementation.[20] Some countries noted that the IT systems were upgraded as part of the normal replacement/maintenance cycle – hence did not generate any significant additional operating costs.

5.2. Reform Challenges

Countries seem to have experience a number of common challenges for implementing reforms:

- The identification and valuation of assets and liabilities are considered as the most challenging tasks during the preparatory stage of the reforms. This is understandable because in most cases countries did not have reliable or complete records of assets – particularly non-financial assets – that were owned and identified, let alone the values of such assets. Similarly, the recognition and reporting of civil service and military pension liabilities, PPPs, etc. can present conceptual as well valuation challenges;
- Putting in place new IT systems are presented challenges at the implementation phase, in the bulk of countries. It was noted that the implementation of a new IT system is already difficult enough when the accounting framework remain unchanged. However, the challenges increase exponentially when the accounting basis changes from cash to accrual and the new system is required to support this new framework;
- A number of countries also mentioned difficulties for realising changes in legislation, as these have to be discussed with the political leadership, the preparation of consolidated financial statements and the preparation of financial statements within agreed timetable.

Most governments sequenced implicitly or explicitly the move to accrual accounting. Most governments have taken a realistic view of the time required to implement the reforms. A key strategy was to adopt a phased approach to the reforms in order to manage the challenges, to minimise the risk of failure and maximize the probability of a successful implementation. Some countries (for example, Denmark) also included a pilot phase or limited test-runs, during which lessons would be learnt prior to proceeding with full implementation. In most cases, the balance sheet was populated progressively. For example, in France, individual evaluations of defence assets were established a few years after the first publication of the Government balance sheet.

Effective project management and coordination and strong leadership by the MoF (or another central agency such as the budget office or the treasury) were identified as critical. Many countries also underline the importance of providing sustained training and assistance to implementation units. Guidance and guidelines have also been used in all countries.

The importance of human resources management and capacity building was a common theme. In particular, countries stressed the importance of having staff or consultants with knowledge and experience of accrual accounting, IT systems, and consolidation to address the biggest challenges they faced. Indeed, a number of countries, for example Canada, which successfully implemented a sophisticated accrual accounting framework, indicated that at the time of the commencement of the reforms many finance personnel had never been exposed to accrual concepts. Therefore, training programmes were delivered in all countries, and experts were often hired to supplement the existing skills base.

5.3. *Achievement of reform objectives*

Countries that engage in accruals reform pursue a broad range of objectives. All of them mentioned, as intended benefits, accountability, transparency towards public at large, political and public awareness about the state of public finances, better information on full costs of operations, efficiency of the administration's business processes, more informed decisions about asset and liability management, and producing meaningful figures and financial analysis.

Overall, satisfaction that reforms objectives have been achieved is mixed (Table 3). Ministries of Finance, in around half of countries considered that the expected benefits were achieved; around one third considered that they were partially achieved; and the remaining countries indicated that the achievements could not be assessed yet.[21] However, none of the countries classified any of the intended benefits of the reforms as "not achieved". It is an interesting contrast that, in some countries where what may be regarded as a full accrual accounting framework has already been achieved, Ministries of Finance consider that further improvements should be made.

Accountability and transparency are considered by Ministries of Finance as the main positive outcomes of the reforms. It is indeed undeniable that accrual accounting has made more and better financial information available to the public at large. A number of countries also note that new procedures and IT systems have helped developing the internal control environment.

Table 3. **OECD Countries: Achievement of Reforms Objectives**

	Fully achieved	Partially achieved	Ongoing
Enhancing Accountability	AUS, AUT, CAN, FIN, FRA, ISR, KOR, MEX, NZL, ESP, CHE, TUR	BEL, DNK, HUN, ISL, ITA, POL, SVK, SWE	CHL, CZE, IRL, PRT, GBR
Increasing transparency towards public at large	AUS, AUT, CAN, FIN, FRA, ISR, KOR, MEX, NZL, ESP, SVK, CHE, TUR	DNK, HUN, ISL, ITA, POL, SWE	BEL, CHL, CZE, IRL, PRT, GBR
Producing meaningful figures/ financial analysts for cabinet and/ or parliament and/or citizens	AUS, AUT, FRA, ISL, ISR, KOR, NZL, ESP, SVK, CHE	BEL, CAN, FIN, HUN, ITA, MEX, POL, SWE	CHL, CZE, DNK, IRL, PRT, TUR, GBR
Increasing political and public awareness about the state of public finances	AUS, CAN, FRA, ISR, KOR, MEX, NLD, NZL, SVK, ESP	AUT, CZE, FIN, ISL, ITA, POL, SWE, CHE	BEL, CHL, HUN, IRL, PRT, TUR, GBR
Better information on full costs of operations	AUS, AUT, ISL, ISR, KOR, MEX, NZL, ESP, SWE, CHE	BEL, CAN, DNK, FIN, FRA, ITA, POL	CHL, CZE, HUN, IRL, PRT, SVK, TUR, GBR
More informed decisions on asset and liability management	AUS, AUT, DNK, FRA, ISR, KOR, NZL, ESP, CHE	CAN, FIN, ISL, ITA, MEX, POL, SVK, SWE	BEL, CHL, CZE, HUN, IRL, PRT, TUR, GBR
Efficiency of the administrator's business processes	AUT, CAN, ISL, ISR, KOR, NZL, ESP	BEL, DNK, FIN, ITA, MEX, POL, SWE, CHE,	AUS, CHL, CZE, FRA, HUN, IRL, PRT, SVK, TUR, GBR

Source: OECD Accruals Survey (2016).

Satisfaction with the use of this information by external stakeholders is however limited. In particular:

- A number of Ministries of Finance, including early adopters of accrual accounting and/or budgeting, note that parliamentarians have limited interest in accrual financial information. This suggests that accrual financial statements remain somehow inaccessible to their primary users, and that ministries of finances still have a way to go to demonstrate their use and added-value;
- Information on the full costs of operations is not always available at operational entities or units levels. Where the information is available, tools and methodologies to use it to assess and improve the management of public assets and performance of entities seem to be lacking. Some countries note also that public managers remain accountable mostly, if not only, through the appropriation process, and therefore have limited incentive in using accrual information;
- A majority of countries also note that adoption of accrual accounting had a limited effect so far on improving the efficiency of administrative processes. This could be explained by the fact that expectations with regards to the efficiency of internal audit and quality of accounting data increase with the adoption of accrual accounting, and development of high quality and independent audits.

The use of accrual information for macro-fiscal purpose is uneven. Most of countries that responded to the question on this issue indicated that the accrual information is not used or used only in a limited way for establishing fiscal forecasts. In many countries, the cash budget balance and net lending remain indeed the key fiscal figures, and focus most of the political debate. However, other countries, in particular Australia, Austria, New Zealand and the United Kingdom, underline that efforts for harmonising the accounting basis and coverage of fiscal reports (budget, financial statements, and statistics) have allowed greater usefulness of the accounting data for fiscal analysis, and greater transparency on the state of public finances.

Recent innovations are directed towards making accrual information more user-friendly and useful to budgetary decision making. Noteworthy initiatives include:

- Attempts at reducing the time lapse for establishing the financial statements(for example, Austria), in order to make them available at an earlier stage of the budget process;
- The use of management commentaries, and attempts at simplifying and streamlining the financial reports (for example, the United Kingdom) to make them more user-friendly;
- The use of accrual information to inform citizens and decision-makers on the efficiency of public management (for example, the *Investment Statement*, which measures the Government's performance in managing its assets and liabilities, in New Zealand; or the development of cross government benchmarks for certain costs, in Denmark).

Notes

1. Countries are classified in this category when i) transactions are budgeted or recognised in the financial reports at the time at which the underlying economic event occurs, regardless of when the related cash is received or paid, and ii) assets and liabilities are budgeted or reported in a balance sheet, irrespective of exceptions regarding the reporting or measurement method of some specific assets and liabilities.
2. Countries are classified in this category when some transactions are budgeted or recognised in the financial reports using cash basis, and some transactions are budgeted or recognized under accrual basis, with the final aim to adopt the accrual basis.
3. Countries are classified in this category when transactions are budgeted or recognised in the financial reports only when the associated cash is received or paid, irrespective of their reporting of commitments.
4. The management commentary, which is a common practice in the private sector, provides readers of financial statements with a backwards and forward looking analysis of the entity's financial position, financial performance, and cash flows.
5. In some jurisdictions, all employees, whether employed by the public or the private sector, are entitled to pensions from the state, which are not considered liabilities because the government can change the pension arrangements at any time.
6. For example, in Australia, social benefits do not constitute liabilities, as they are not legal obligations (not legal obligation to pay until a future point in time) and do not represent a constructive obligation (as the government does have an ability to avoid specific payments). This approach is agreed by the Auditor-General.
7. The basic elements of an annual budget are i) a policy statement describing the macroeconomic assumptions on which the budget is based, presenting the fiscal objectives, targets, and the main policy decisions (new programs or savings) of the government; ii) annual forecasts of revenue and expenditure, the fiscal balance, and financing need; iii) legal provisions to authorize or limit the incurrence of expenditure by ministry and/or program, and to implement the policy measures adopted by the budget. In most countries of the Continental tradition, the Budget Act adopted by the Parliament combines all these basic elements. In particular, the Budget Act both forecasts and appropriates money for public policies. Countries of the Westminster tradition have a different approach and make a clear difference between forecasts and the granting of authority to spend. Fiscal forecasts are included, together with a discussion of fiscal policy and government priorities, in a budget statement which has no legal force and is normally debated in Parliament in the form of a vote of confidence (i.e., if the vote is rejected the government must resign). Annual authority to spend is granted through Appropriation Acts (also called "Estimates") or through other laws which permanently appropriate money for specific programs, such as entitlements.
8. They allow authorising, reporting on, and controlling future cash outflows, but are not liabilities. Some countries that use commitments in their budgets have described their budgeting system as "cash and commitment frameworks", rather than cash basis budgeting.
9. In the Survey, the category was entitled "Cash transitioning to Accruals", which did not reflect the actual situation described by most countries.
10. Within these accrual appropriations regimes, cash allocations are made available to the ministries and departments based on their estimated cash requirements, as summarized, for example, in the cash flow statement.
11. Germany and the Netherlands use only commitment appropriations.
12. This is does not mean, though, that comparability between budget and actuals is not possible: budget execution reports are usually comparable with the initial budget.
13. The United Kingdom highlighted its initiative, referred to as the Clear Line of Sight project, to align estimates, budgets and accounts.
14. In international standards, "consolidation" means presenting the assets, liabilities, net assets/equity, revenue, expenses and/or cash flows of public sector entities as if they were a single entity. Consolidation also implies elimination of all transactions and balances between entities that are being consolidated.
15. These practices are not specifically related to accrual accounting, but are necessary and important elements of an accrual accounting framework.

16. International Monetary Fund's Government Finance Statistics Manual or European Commission's European System of Accounts.
17. Such as the standards enacted by the INTOSAI.
18. This section of the OECD questionnaire was not completed by one respondent (United States of America).
19. See Appendix 2, Table 1.
20. Public information is also available for a number of European countries, and a recent study published by EUROSTAT based on a survey of EU Member States estimates that the total cost of such a reform for central government would be around 0.05% of GDP.

    Australia and the UK are among the countries that decided to address this issue by making a strategic decision that the ministries, departments, and other agencies should absorb the costs of the reforms and that no additional funding would be provided. These included the very substantial costs of implementing new IT systems.
21. The assessment of the achievements of objectives may however vary depending on the stakeholders consulted.