Implication of International Public Sector Accounting Standards (IPSASs) on County Financial Management and Reporting

CPA Mike Mbaya

What is IPSAS

- The International Public Sector Accounting Standards (IPSAS) are a series of 32 financial reporting and accounting standards issued by the International Public Sector Accounting Standards Board (IPSASB), which represents more than 160 member bodies in 120 countries.

- IPSAS provides high-quality, independently produced accounting standards, underpinned by strong due process and supported by governments, professional accounting bodies, and international development organizations, representing best practices for governments and not-for-profit organizations.

- IPSAS ideally should replace any Accounting Standards System which were/are being used by any public governmental body around the world.

- IPSAS have not been fully adopted yet around the world but governments are at various levels of Adoption. In Africa the efforts of the Rwandese government have caught the eye and been applauded.

Introduction

- The International Public Sector Accounting Standards Board have established IPSAS for use by governments to tailor financial reporting standards to the public sector context. They provide a framework for all public sector entities other than Government Business Enterprises.

- IPSAS are largely aligned to International Accounting Standards, and differ only where there is a public sector specific issue which warrants a departure. Where no IPSAS is available, entities are encouraged to draw upon the requirements of the relevant International Financial Reporting Standard (IFRS) or International Accounting Standard (IAS) issued by the International Accounting Standards Board.

Introduction

- A statement of compliance with IPSAS should only be made where all requirements of each applicable IPSAS are met. However, there are a number of provisions available during the transitional years of adoption, although such departures should be clearly disclosed in the Accounting Policies of the entity. Some governments may adopt different policies in certain circumstances, and these should be taken into account when considering accounting policies and compliance with the IPSAS.

- A comprehensive Cash Basis IPSAS has also been issued but this would, if appropriate, represent a transitional arrangement only, which is not recommended and is not covered in this guidance.

Objectives of IPSAS

- Better understanding of revenue and expenses and improved management of commitments, risks and uncertainties;
- Increased transparency and harmonization of financial reports and statements across the government system;
- Enhanced prediction of future asset and cash-flow needs; and
- Adherence to the highest international standards of financing reporting— aligned with best practices—that allow for improved consistency and comparability.
- Strengthened accountability towards all stakeholders;
- Strengthened support for results-based management through the provision of comprahensive information on costs;
- Improved management and planning across the Joint Programme due to better accounting practices for income and expenditure;
- Higher standards

Impact of IPSAS adoption

- Applying IPSAS require the introduction of the full accrual basis of accounting, a significant change from the modified cash basis of accounting applied under current government accounting.

- Accrual accounting recognizes a financial event when the underlying economic event has actually occurred—in other words, transactions are recorded when they occur and not when cash or its equivalent is paid or received, which was/is the practice followed under current government accounting.

Shift in IPSAS adoption

- Expenses: Accrual basis accounting entails the recognition of expenses when they occur and when goods and services are delivered and not when disbursements are made.

- Revenue: IPSAS stipulate that revenue be recognized on the basis of signed contractual agreements rather than when cash is received.

- Fixed assets: IPSAS require the cost of assets to be disclosed and capitalized when acquired, including property and equipment, and depreciated over their estimated life.

- Staff-related liabilities: A significant change is the recording of the value of future staff-related liabilities (i.e. accumulated annual leave, termination repatriation grants, after-service health insurance, etc.) that Governments staff have accrued over the period of their service and have not been paid out. In previous financial statements, these types of benefits were shown as an expense only when paid, and the liabilities were only disclosed in the notes.

- Budget: The implementation of IPSAS does not currently impact the preparation of the government budget which continues to be presented on a modified cash basis. As this basis differs from the accrual basis applied to the financial statements, reconciliation between the budget and the principal financial statements is provided in accordance with the requirements of IPSAS.

Current System Vs. IPSAS

Current System	IPSAS
Transactions are recorded on a cash basis when cash is either received or paid.	Transactions are recorded on a full accrual basis when goods or services are received.
Reported expenditures represent disbursements and un-liquidated obligations	Recognition of expenses on the basis of goods and services received.
Inventory is expensed when purchased	The value of inventories at the end of the financial period is recorded as an asset in the statement of financial position
Recognition of income on a cash basis	Revenue is recorded when a binding agreement is signed with no 'subject to' clause.
PPE is expensed when purchased	PPE is capitalized and depreciated over its useful life
Items that are Intangible items are expensed when incurred	Intangible assets are capitalized and depreciated (armotized) over the usefull life period of the asset.

Current System Vs. IPSAS

Current System	IPSAS
Lease payments are recognized as an expense upon payment	Leases are classified into operating and financial lease. A liability and an asset is recognised for finance leases and future lease payments diclosed.
After service health insurance and annual leave liability are reported in the financial statements as notes only.	Full recognition of liabilities and expenses relating to employee benefits in the financial statements.
Annual financial audits	Annual financial audits are required

Accounting for Assets

- **Better Receivables Management**
- Under IPSAS, a receivable is recognized upon signature of a binding agreement. By recognizing receivables when revenue is earned, the government is able to better manage collection on a timely basis.

- **Better Inventory Management**
- Previously the government did not recognize inventories in the Statement of Financial Position. By reporting inventories, the government is able to better understand the extent of inventories held, leading to better stewardship and logistics management (e.g. the use of vaccines by their expiry date).
- Furthermore, by recognizing inventory under IPSAS, the government can conduct a physical verification of all stock on hand. In the process of understanding and valuing its inventory, the government is able to develop a documented account of some locations of assets under its control, and can then implement common procedures across counties for managing these assets.

Accounting for assets

- **Better Management of Property, Plant and Equipment**
- IPSAS requires the governments to recognize assets relating to property, plant and equipment (PP&E). Because the government had not previously recognized PP&E in its financial statements, a central repository containing full PP&E data is unavailable.
- The government could elect to use the transitional provision under IPSAS, which allows it to recognize PP&E for the first time over a period of five years. However, the government should start the task of identifying and recognizing PP&E in its financial statements, resulting in a better understanding of the following:
- PP&E held across the country/county
- Which items of PP&E are owned and operated exclusively by the governments and which relate to common arrangements - specifically land and buildings

Accounting for assets

- **Better Management of Property, Plant and Equipment**

- Which items of PP&E contain financing or operating lease agreements
- Restrictions on the use of PP&E
- The estimated costs of maintaining infrastructure through an annual depreciation charge to PP&E
- By knowing what assets the government owns as well as the remaining useful life of these assets, the government is better able to prepare and plan for upcoming capital requirements.
- The government is also able to recognize the value of in-kind contributions from areas where the use of premises has been given for free.

Accounting for assets

- **Enhanced Awareness of Existing Intangible Assets**
- Historically, the government has not recognized assets that were “intangible” in nature.
- However, IPSAS requires that these assets be recognized if certain criteria are met. The government will need a process of accounting for and understanding what kind of intangible assets exist within it set up, some of these will include patents, copyrights, licenses, and various internally developed and externally acquired software products.
- By understanding which assets meet the definition of an intangible asset, the government is better able to track and control these assets, particularly those assets where there is no physical form.

- **Enhanced Disclosure of Financial Instruments**
- IPSAS requires the government to recognize and disclose the strategies it takes to mitigate its risks and uncertainties, including its hedging strategies, currency exposures and any investment risks.

- By disclosing and recognizing these instruments in the financial statements, users are able to better understand the risk and uncertainties inherent in government operations.

Accounting for liabilities

- **Improved Visibility of Liabilities**
- As a result of IPSAS, the government will have a better knowledge of what it owes. For example, future staff liabilities, which include, Terminal payments including annual leave obligations.

- Better knowledge of existing liabilities supports better management of resources, contributing to improved budgeting and fund-raising in order to ensure that all obligations are met.
- IPSAS will enable governments to better distinguish between assets and liabilities under its direct responsibility as opposed to those that are managed by hosted entities. Several of these entities will now also produce full IPSAS compliant financial statements subject to a separate external audit.

Accounting for revenue & expenses

- **Timely Revenue Recognition**
- With the adoption of IPSAS, revenue is recognized when a binding agreement is signed.
- By recognizing revenue when it is earned, the government is better equipped to understand its revenue inflows, leading to enhanced cash-flow management and forecasting, and a better understanding of balances carried over from one period to the next.
- **Better Expense Management**
- IPSAS requires the recognition of expenses on the basis of the “delivery principle”. Under this principle, expenses are recognized when goods and/or services are delivered rather than when cash is exchanged. Thus, the government will report expenses when they are incurred and when the benefit to it is received rather than when the expense is paid.
- This will help WHO to better understand the cost of operating in the financial period when the activity takes place, leading to improved budget management.

Some immediate challenges of IPSAS

- Although there are various benefits to IPSAS implementation, there are also some challenges that are faced when it comes to IPSAS implementation
- These challenges include:
- **Government -Wide Participation**
- Requirements under IPSAS go beyond financial records. The involvement of many teams (procurement, human resources etc.) and collaboration across locations (Regional Offices, Country Offices etc.) is required for the successful implementation of IPSAS.
- **Training**
- Training of IPSAS to its employees will not be easy for any government . However, changes resulting from IPSAS implementation require that ongoing and focused training is provided to key staff as they report under the new standards.

Some immediate challenges of IPSAS

- **Time and Resources**
- IPSAS requires additional tasks to be completed in preparing and maintaining financial records. These tasks need to be completed each year, within 6 months which is significantly more demanding than in the former process.

- **Bugdet-To-Actual Comparisons**
- IPSAS requires a comparison of budget amounts and the actual amounts arising from the execution of the budget to be included in financial statements. This comparison is to be performed on an annual basis and presents some challenges to governments.

Responsibilities in IPSAS adoption

- The implementation of IPSAS will represent a significant undertaking for most entities. Entities will need to develop a project plan that covers at least the following areas:
- Implementation of new systems:
- Infrastructure to support accounts preparation;
- Compatibility with existing key systems;
- Development of new information systems and internal control mechanisms;
- Staff training.

Responsibilities in IPSAS adoption

- Finance staff training in IPSAS;
- Training of non-finance staff in accounting policies (accruals-based concepts) to ensure cultural change to recognise and record relevant financial data;
- Re-design of key processes and information flows, including financial procedures;
- Management verification of balances and accounts classifications, including appropriate challenge of
- output data prepared by finance;
- Liaison with internal and external auditors.
- Engagement of auditors is crucial to successful change.

Responsibilities in IPSAS adoption

- Entities will be required to prepare annual Financial Statements which give a fair presentation of the financial position, financial performance and cashflows of that organisation.
- Entities and their finance team will therefore need their own assurances that finances and financial systems are in good order, and should ensure that the financial statements are supported and validated by comprehensive reviews before being presented for audit.
- In particular, it is important to consider the information requirements of the various entity stakeholders when considering the extent

.n0 1 341.81 14.33 Tm(ET3)Mnaf12w 3o82()TJETe.it
the

Way Forward

- Double-entry accounting recording system should be operational in all the Counties.
- The present accounting system should be adjusted as outlined above. Some old practices should be discontinued, while new ones introduced.
- Supportive accounting policies should be developed to guide accounting practices in the counties.
- New processes and procedures should be introduced in line with IPSAS requirements.
- The Account Officers should be further trained in depth on the IPSAS, especially when the County adopts the Standards; and other top government officials should be sensitized on the usefulness of the IPSAS for the County Government.
- Each IPSAS (Standard) should be accurately translated into specific policies and procedures.
- Above all, there should be high-level government support for the implementation of IPSAS in the County Government.

Benefits of full adoption of IPSAS

- The Financial Reports would provide comprehensive information for users.
- There would be better estimates of macroeconomic impact of government fiscal policies on the economy.
- Information on outstanding payments or liabilities would be readily available for evaluation and planning purposes.
- Liquidity management would improve in the government's financial management.
- Management of non-financial assets would improve significantly.
- There would be improvement in the accounting for non-financial assets.
- There would be consistency and congruency with other macroeconomic statistical information.

Benefits of full adoption of IPSAS

- Opportunities for manipulation of financial records and public funds would be reduced.
- Financial reports prepared by the government could be compared between one period and another, and with performance of other counties in Kenya and internationally.
- Information on the macroeconomic impact of capital flows would be available.
- There would be improvement in the management of resources by MDAs.
- Information on future commitments would be supplied for monitoring purposes.
- There would be adequate information for the determination of appropriate pricing of government goods and services.
- Access to public sector financial information would be enhanced.
- The financial reports produced by the counties would be recognised by World Bank and other international agencies.

Recommendations to the counties

- The government should make a definite statement on the commencement date for implementing the provisions of IPSAS in the Counties. This will show commitment and political will of the government to embark on fundamental reforms of the State's PFM systems.

- A Working Team should be constituted and a Consultant engaged to coordinate the review process of the present accounting policies and procedures, to comply with provisions of IPSAS; subsequently in-depth trainings on IPSAS will be provided to the Accounts and Audit staff of the counties.
- The Budget Codes and Chart of Accounts should be developed for the County Government and implemented.
- The government should acquire suitable Computer Application Software to start automating its accounting system.
- Desktop and Laptop Computers should be supplied to Account Officers in counties to enable them use basic tools to automate their daily operations and communications. This would result to efficiency and improved productivity.
- Subsidiary accounting records, such as Fixed Assets Register, Accrual Schedules, Prepayment Schedules, Debtors, Creditors, etc. should be introduced immediately in the Counties Public Finance System.

Lessons from other places

- There is need to organise regular Workshops for Account Officers. This would sharpen their skills and keep them abreast with current developments in Public Sector Accounting. It would also create the forum for the Account Officers to work together, thereby promoting team building within the resource groups.
- Most of the Account Officers need to be trained in Computer and Information Technology to prepare them to contribute adequately in the public sector finance reforms programme. Modern financial management is driven by IT, hence there is need to upgrade their knowledge.
- Workshops and training programmes should be planned ahead to give adequate time for preparation.
- There should be post training reviews of performance of the Account Officers to assess the impact of training.

In summary

- The key messages from this guide are:
- The successful implementation of IPSAS will depend heavily on the level of planning and preparation undertaken by entities and any sponsoring organisations;
- A thorough understanding of the entity risks, systems of internal control, and financial transactions is necessary to allow effective application of the IPSAS. This includes the formulation of appropriate accounting policies at the outset that reflect the organisation's circumstances; and
- The disciplines brought to an organisation by the implementation of the standards are important to successful financial management.

Caveat

- This presentation is primarily addressed to accountants of entities who intend to produce Financial Statements under International Public Sector Accounting Standards (IPSAS).
- The purpose of the guide is to provide practical assistance on issues that entities may face in preparation for the implementation of IPSAS.
- Whilst guidance is provided on the application of IPSAS, it is not intended to replace the need for a detailed knowledge of the IPSAS, which is fundamental to the proper implementation of the Standards.

Thank You

- No questions please…….only comments

CPA Mike Mbaya

Tel. 020 04446466 / 020 4443868