

## *Join the leaders in public finance*

### Implementing Accrual Accounting in the Public Sector as part of wider finance reform

PwC Middle East  
Public Finance and  
Accounting Services



# *The climate of public finance reform*

Governments across the world are coping with day to day increasing pressure due to restricted budgets and increased demand for public goods and services. Additionally, as a result of the global financial crisis, public-sector entities at all levels of government are facing unprecedented demands for improvement in the management of public finances.

In response, many of these organisations are undertaking a range of reforms to increase accountability and transparency, whilst also improving operational performance and the Value for Money (VFM) that the general public and individual consumers receive from public-sector services and activities. One essential reform for improving the management of public finance is the implementation of accrual accounting and many governments are choosing International Public Sector Accounting Standards (IPSAS) as the appropriate framework.

PwC is assisting governments implement accrual accounting as the main building block to improving fiscal control and budgeting process.

The IFAC (International Federation of Accountants) which promulgates IPSAS recently issued a letter to the G20 leaders recommending that governments should practice what they preach and follow rules like those set down for public companies.

## *Who has adopted IPSAS?*

*Government bodies such as the European Commission, the United Nations and several governments in the Middle East have implemented IPSAS, or are currently in the process of doing so.*

IPSAS are being adopted by a large number of organisations across the world. Supranational public-sector entities have been at the forefront of the move towards IPSAS. Organisations such as the European Commission, the United Nations and Governments in the Middle East have either already implemented IPSAS, or are currently in the process of doing so.

However, a diverse range of national and sub-national government entities also have projects and processes in place aimed at the adoption of IPSAS, IFRS or an accrual basis of accounting closely aligned with these international standards.

With the United Nations and other international organisations adopting IPSAS as their accounting framework, the number of public-sector organisations announcing their implementation of IPSAS has increased significantly.



# The benefits of implementing IPSAS as part of wider finance reform

*IPSAS is a catalyst to providing high-quality financial statements and, more importantly, improving operational performance.*



## **Enabling sound public-finance management**

The superiority of accrual accounting over cash accounting is now acknowledged by the vast majority of finance and accounting professionals.

By introducing accrual accounting, public entities demonstrate a commitment to improve the use and management of resources, a desire to promote enhanced financial reporting and transparency, plus greater accountability and a pledge to fight fraud and corruption.

Cash accounting, and even accrual accounts based on locally defined financial reporting standards, are no longer sufficient to enable public-sector organisations to respond to the legitimate needs and demands of the citizens they serve. Independent standards are essential for high-quality financial reporting, which in turn is fundamental for developing the levels of accountability and quality decision-making that lead to good governance, transparency and trust.

## **High-quality accounting standards**

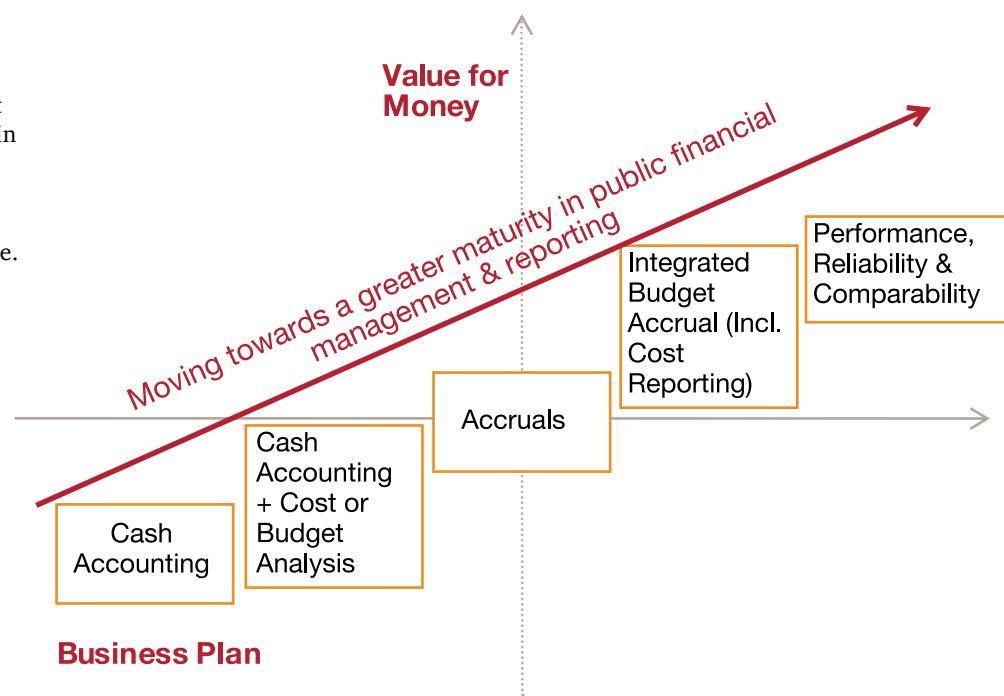
IPSAS are developed by the International Public Sector Accounting Standards Board (IPSASB), which focuses on the accounting and financial-reporting needs of governments and the constituencies they serve. They set out recognition, measurement, presentation and disclosure requirements dealing with transactions and events in the general-purpose financial statements of all public sector entities. The strategy of the IPSASB is, as appropriate, to align the IPSAS with International Financial Reporting Standards (IFRS) issued by the IASB. This ensures that organisations in the public sector that adopt IPSAS have financial reports that are consistent with and comparable to private-sector best practice, while also benefiting from guidance and interpretation for specific public-sector issues such as heritage assets, public grants and revenue from non-exchange transactions.

## **IPSAS as a catalyst for performance improvement**

It is important to acknowledge that implementing IPSAS is not an end in itself, but a catalyst to providing high-quality financial statements and, even more importantly, improving operational performance.

This is true in areas such as fixed assets and inventory management, payroll and the wider field of employee benefits.

In assisting public-sector clients with their IPSAS implementation, we have encountered many challenges, but also helped them reap many benefits.



# What are the challenges

*Implementing IPSAS has an impact on the entire organisation. It is therefore important for organisations to take their time to assess and prepare for the significant changes that will affect their policies, people, systems and processes.*



**Making the change to IPSAS is much more than an accounting exercise. It has an impact on the entire organisation and will affect its policies, people, systems and processes.**

The implementation of accruals accounting requires entities to capture, maintain and control all their assets and liabilities. Where such assets and liabilities have in the past not been recognised, this can place a major burden on not only the accounting functions within an organisation but also on their day to day operations as it typically impacts all functions within the government.

## Policies

One of the inevitable consequences your organisation is facing, when it adopts accrual accounting, is the need for it to review and amend its policies, governance and control structures.

First, financial rules and regulations are affected. A comprehensive accounting manual, possibly supplemented with concise implementation rules, can help your staff quickly adhere to, the new accounting principles and understand the concepts behind the IPSAS standards. Introducing accrual accounting may also require you to revise your budgetary accounting policies, even if budgets remain on a cash or some other basis. Policies for other business processes (e.g. HR, procurement, asset management) may also be affected. Depending on your organisation's governance structure, introducing accrual accounting may additionally have an impact on the work done by your oversight bodies (e.g. the approval and control process surrounding use of public funding).

## People

Accrual accounting is based on the occurrence of economic events, and not merely on cash receipts and payments. Adopting accrual accounting or, for those organisations that already apply it, moving towards IPSAS as the basis for accrual accounting, accrual budgeting or performance –based management requires a significant cultural shift in the mindset of management, staff, regulators, fund providers and other organisational stakeholders.

For this to be successful, it is essential that change management processes, including training, project management, awareness campaigns and organisational reform, are put in place and that they work.

## Systems

Accrual accounting also requires organisations to develop new ways of reporting and communicating financial information. As the focus for public-sector bodies has traditionally lain on budgetary execution rather than wider financial reporting, new data needs will arise when accrual accounting is adopted under IPSAS. In order to capture and analyse the increased accounting data and information, IT systems often need amending. Many public-sector entities use their IPSAS implementation as an opportunity to set up an enterprise-resource planning system or to upgrade their current system.

Having one organisation-wide system that can be used to manage and coordinate all information, resources and business processes means that significant efficiency savings and productivity gains can be achieved.

## Processes

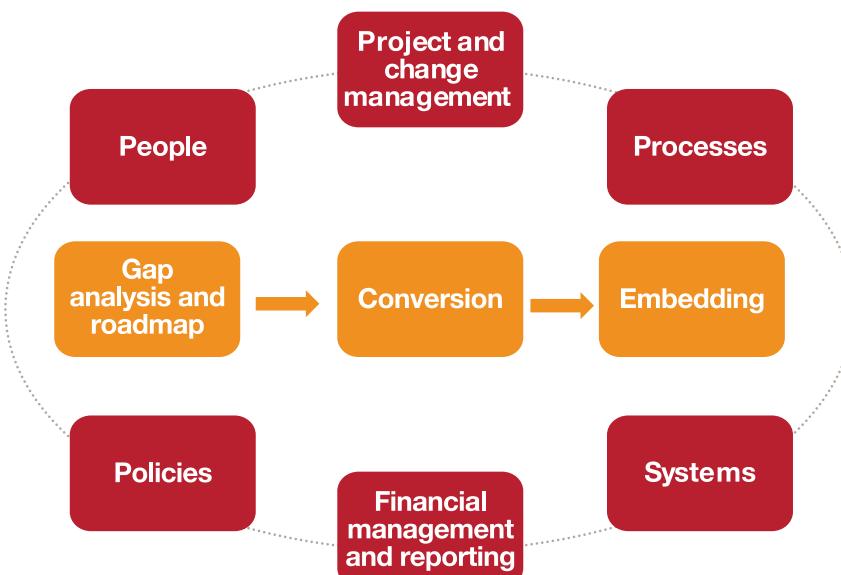
Beyond people and systems, IPSAS adoption also has an impact on processes. Organisations have to enhance existing processes, create new ones and re-examine internal control to ensure risk management processes are effective under the new accounting standards.

Where public-sector entities already utilise local accrual-based financial reporting standards, the challenges of IPSAS implementation are fewer, but they still require careful consideration and management. For example, a number of the standards can lead to significant shifts away from locally-defined accepted practices, especially in areas such as counting for assets, investments and employee benefits.

# Our conversion methodology

Adopting IPSAS is a major undertaking for an organisation, and having a partner that has the necessary knowledge, experience and expertise to manage the change in all these areas is essential.

Our IPSAS conversion methodology typically involves a three-phase approach designed to add maximum value to your organisation. It ensures that IPSAS adoption does not inhibit the achievement of current operational and administrative goals and helps generate significant performance improvement once conversion is achieved.



## Phase One:

### Gap Analysis & Roadmap

The objective of a gap analysis is to gain a detailed understanding of the impact of IPSAS on the organisation, highlight key accounting and reporting issues that need to be addressed, understand which business processes may be impacted by IPSAS, and take an informed decision on how to proceed with the IPSAS conversion. The roadmap allows the organisation to design a detailed project plan, define its needs and estimate the cost of the entire conversion process, including from an information system point of view.

## Phase Two:

### Conversion

The second phase of the conversion methodology involves project set-up, component evaluation and issue resolution, plus the initial conversion. The project set-up is designed to enable the organisation to manage the IPSAS conversion project to a successful conclusion while continuing to run its business or operations effectively. For this purpose, the project management structure is set down, conversion tools are tailored and the project strategy is communicated throughout the organisation.

Component evaluation and issue resolution encompasses establishing IPSAS accounting policies, developing the shell financial statements and implementing the conversion strategy at departmental level. Once IPSAS accounting policies have been documented, adjustments and data requirements identified and reporting-process solutions developed, the organisation is ready to undertake initial conversion.

The initial conversion enables preparation of the organisation's first IPSAS-compliant financial statements and means that an informed decision can be taken on the ongoing conversion strategy. For this, IPSAS reporting process and systems need to be designed, built and tested, IPSAS adjustments need to be calculated, reporting packs completed for required disclosures, and IPSAS results consolidated and analysed. Once completed, the initial conversion provides the organisation with Year 1 IPSAS financial statements, an assessment of the business impacts and a gap analysis of the relevant processes, systems and organisational structure.

## Phase Three:

### Embedding

The final phase is designed to enable the organisation to move smoothly to a new “business-as-usual” operation, using its “new language” comfortably and authoritatively. Embedding the change involves continuing IPSAS training throughout the entity, finalising the accounting manual and chart of accounts, completing systems design, build and test, the design and rollout of new business processes and procedures including internal control and risk management, and modification of budgeting processes. In practice, depending on the needs and time constraints of the project, portions of the work relating to phases two and three may be carried out simultaneously.

Once conversion is completed, IPSAS will be embedded across the organisation, with modified systems, updated controls and procedural documentation, and fully trained staff.

The European Commission implemented IPSAS-inspired accrual accounting standards for the financial year ending 31 December 2005 as part of a major accounting overhaul designed to provide transparency to the financial position of the European Communities. After two years of intensive preparation, the European Commission was able to present the 2005 full accrual financial statements to its oversight bodies.

In this process, PwC assisted the European Commission in a number of key tasks, including:

- Developing accounting rules based on IPSAS and a new chart of accounts, new procedures and manuals;
- Adapting the IT system to support the new accounting rules, and to capture a wide range of information as and when an economic event occurred;
- Training users to apply the new practices and procedures needed to capture the information in a complete, reliable, timely manner; and
- Implementing a quality control project aimed at improving the accuracy of the financial data communicated by each department, and to address the issues identified by their auditors.

Following the successful initial transition to IPSAS, the European Commission is now committed to ensuring that the wider benefits of IPSAS adoption are realised for operational performance.

With our global conversion experience, and regional accounting advisory expertise, PwC has assisted governments in the region in adopting IPSAS as their accounting reporting framework.

PwC has assisted governments in the following key tasks:

- Developing comprehensive accounting manuals based on IPSAS, reviewed and developed charts of accounts to suit the requirements of the new accounting framework;
- Developed accounting conversion manuals for a step by step accounting conversion for all the financial statements areas;
- Helping governments adapt IT systems to support new requirements, such as data gathering between departments and financial statements consolidation;
- Providing training to finance staff ensuring best practices and conversion techniques are understood providing attendees with the ability to implement in practice;
- Supporting the detailed conversions to IPSAS process at a Government Department level; and
- Supporting the Departments of Finance in helping them fulfill their obligations as consolidator of IPSAS compliant financial information.

## Case Studies

IPSAS at the European Commission and various governments in the Middle East



# How PwC can help you

We can offer either assistance on a full conversion process or ad hoc services on request. The following are examples of potential challenges.

## Project and change management

- You need full assistance in your IPSAS conversion process or wish to outsource its entire management to an external partner.
- You need assistance with specific aspects of the conversion process.



## How we can assist

- PwC can provide management of all parts of the IPSAS conversion process for your organisation. Full conversion project management support includes training, technical advice, development of the conversion strategy and all other services necessary to ensure your successful conversion to IPSAS.

## IPSAS accounting advice

- You are uncertain how far your current accounting standards differ from IPSAS.
- You do not have sufficient internal expertise for specific areas that are key to your organisation's IPSAS implementation.
- You need quick, reliable access to a team of experts for ad hoc requests or regular discussions.



- PwC can provide a range of technical support, including services such as gap analysis between current accounting standards and IPSAS, and technical analysis on critical areas that affect your financial statements (e.g. financial instruments, property, plant and equipment, employee benefits, etc.).
- Advice can be delivered as part of an individual engagement or as an ongoing relationship throughout your IPSAS implementation.

## Training and workshops

- You need an overview of IPSAS to understand what implications adopting them may have on your organisation.
- Your financial professionals require individual training on key IPSAS accounting areas.
- You want to facilitate organisational change and increase staff awareness of IPSAS, addressing the benefits and challenges.



- PwC can assist in identifying and providing the right form of training for your people to ensure that implementation of IPSAS is a success.
- From individual technical training sessions in key accounting areas to workshops providing an overview of IPSAS and their implications for an organisation, PwC has a team of trainers who have the skills and experience to transfer understanding and knowledge to your staff.
- Our IPSAS specialists act as workshop facilitators and trainers to public finance specialties across the globe.

## Process and system improvement

- You're looking for advice on the process and information system aspects of the conversion.
- You want to take advantage of the introduction of IPSAS to streamline business processes.
- You want to be certain that changes to your organisation and business processes are effectively translated into the IT environment.
- You aim at high levels of corporate governance and want to ensure the new IPSAS environment complies with your existing regulatory framework.



- Our services include business process reviews, design of risk and compliance frameworks, internal control procedures and manuals.
- Furthermore, PwC can guide your organisation in embedding the changes into your IT environment.

## Financial management and reporting

- You want the additional information provided by IPSAS financial accounting to be easily utilised by management.
- You want to ensure that financial and budgetary accounts are complementary, readily reconcilable, and provide your organisation with a total view of financial management.
- You want to use the enhanced information available from IPSAS to generate operational performance improvements by introducing further reforms such as cost accounting.



- PwC can provide a range of services to assist your organisation improve the quality and credibility of its financial management information and allow reporting to be utilised for compliance and performance improvement.
- This ranges from compliance reviews of whether IPSAS requirements are met in financial statements and annual reports, to the development of cost accounting, billing solutions or other management reporting that will help generate real operational performance benefits for the organisation.

# Who to contact

*Implementing IPSAS has an impact on the entire organisation. It is therefore important for organisations to take their time to assess and prepare for the significant changes that will affect their policies, people, systems and processes.*

For a detailed discussion on how the switch to IPSAS could affect your operations, please contact our Middle East region specialist team:



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Our team is based in the Middle East. They bring with them international experience of major accounting conversion in large and complex organisations including Governments, Multinational Companies and large State Owned Enterprises.

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