



საქართველოს ფინანსთა სამინისტრო  
სახელმწიფო ხაზინა



## Modified IPSAS Step Forward towards Comprehensive Transfer to IPSAS

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## Preconditions of Reforms



- ❖ The Public Sector Accounting reforms is ongoing in compliance with the strategy, approved by the Minister of Finance of Georgia
- ❖ Strategic vision was developed through analysis of the public sector accounting and reporting methodology and assessment of their compliance with international standards
- ❖ Analysis and assessment was conducted with assistance of international experts in the sphere of accounting procedures.
- ❖ **Results of analysis and assessment:**
  - *Entities, funded from the state budget are conducting accounting through modified accrual method*
  - *Budgetary classification was not in compliance with chart of accounts*
  - *Methodology of accounting was not taking into consideration requirements of the budgetary system*



## Preconditions of Reforms



- ❖ Accounting and reporting of public sector entities, having different organizational form was regulated by different normative acts and methodology was not uniform.
- ❖ Accounting was not fully covering budget execution and control over targeted use of budgetary resources was not fully effective
- ❖ **Conclusions:** - *public sector accounting was not in compliance with international standards, while in the private sector IFRS standards were introduced successfully*
- ❖ **Decision was reached** *to implement public sector accounting reform and introduce IPSAS*
- ❖ The above decision was reflected in the accounting system reform strategy



## Preconditions of Reforms



- ❖ There are two alternatives in regard to introduction of IPSAS - **cash and accrual methods**, and we opted towards the **accrual method**
- ❖ **Reasons for choosing above mentioned option:**
  - Elements of accrual accounting method were used in the public sector of Georgia and there is certain experience in given sphere
  - Introduction of cash based IPSAS with further transfer to accrual method would cause:
    - Loss of available information on accruals in regard to assets, liabilities, depreciation and etc
    - Refusal from use of experience of public servants, trained in accrual method accounting and the need for their retraining
- ❖ **Final decision:** **introduction of modified cash basis accounting method during interim period**
- ❖ **Detailed action plan for implementation of the reform was elaborated**
- ❖ **Pilot organizations were selected taking into consideration their specificity**
- ❖ With assistance of international consultants was prepared tentative cost-estimation of implementation of the project at initial stage for the purpose of establishing its cost-effectiveness



## Preconditions of Reforms



- ❖ Was set up permanent consultative body – **The Council of Public Sector Accounting Standards**
- ❖ **Regulations were elaborated, which define purpose, functions and competencies of the Council. Namely:**
  - *Improvement of public sector accounting information and public sector financial management and increase of public trust towards management of public resources*
  - *Elaboration of recommendations and methodological instructions related to introduction of international accounting standards in the public sector of Georgia*
  - *Ensure access to international accounting standard to public sector organizations through official website and other media*

Treasury PFM Reforms



## Preconditions of Reforms



*Trainings for pilot organizations were conducted*

*In pilot organization financial reporting for 2010 was prepared in compliance with new methodology*

*Taking into consideration results of financial reporting methodology for preparation of financial reports through use of modified cash accounting method was improved*

*Budgetary entities prepared financial reporting for 2012 in accordance with this methodology*



Purpose of use of modified cash method during interim period, prior to transfer to accrual method:

Ensure compatibility of financial reporting of budgetary organizations with equivalent GFS 2001 reporting (*Cash method accounting and reporting of budget execution in compliance with GFS 2001*)

Obtaining of additional information through financial reporting (e.g. cash flow)

Expansion of the scope of accounting in the public sector (e.g. accounting of debts)

Development of unified methodology of financial reporting for public sector organizations of different organizational form, which have the right to implement economic activities



## Relevant Regulatory Normative Acts

- The Law of Georgia on Accounting and Audit
- The Budget Code of Georgia

Accounting instructions on "Rules of Reporting by Modified Cash Method"

### Purpose of the law is:

-Definition of legal basis for maintaining of accounting and preparation and submission of financial reports

### According to the law:

-Accounting standards are composed of public sector accounting standards and private sector accounting standards

Public sector accounting standards are rules of accounting and reporting, that apply to budgetary organizations and legal entities of public law.

Public sector accounting standards are defined by the Minister of Finance



## Relevant Regulatory Normative Acts



- ❖ The government of Georgia, taking into consideration the sphere of activities of certain categories of public sector entities, is authorized to require from them to use private sector accounting standards.
- ❖ Public sector entities are authorized to maintain accounting independently, through hired certified or uncertified persons, as well as through procuring such services.

- ❖ According to the Budget Code of Georgia budget execution shall be accounted for through use of cash method and reporting shall be conducted in accordance with Government Finance Statistics GFS 2001 methodology.
- ❖ Public sector entities are authorized to maintain accounting independently, through hired certified or uncertified persons, as well as through procuring such services.



## Modified cash-basis method



Given method is used for preparation of consolidated accounts and includes accounting of those entities, which produce goods and supply services, as well as entities, which are authorized to implement economic activities

According to these rules explanation, recognition and assessment of transactions is admissible.

Modified cash-basis method envisages accounting of economic activities and their reporting through use of accrual, as well as cash method.



## Modified Cash Basis Method



- ❖ Financial reporting is conducted on annual basis, within one month after preparation of annual accounting report, which serves as basis for preparation of financial report.
- ❖ Methodology of financial reporting is not used in the process of preparation of interim (quarterly) reports.
- ❖ Methodology takes into consideration restrictions, established by the law in regard to settlement of accounts with budgetary funds
- ❖ In the event of incompliance with GFS 2001 methodology in the process of preparation of financial reporting through adoption of modified cash basis method, IPSAS definitions, classification and instructions shall have precedence.



## Modified Cash Basis Method



- ❖ **Components of reporting are:**
  - ✓ Financial status report (balance)
  - ✓ Financial performance report
  - ✓ Cash flow report (statement)
  - ✓ Report on capital variance
  - ✓ Planned and actual execution comparison report
  - ✓ Explanatory notes and comments
- ❖ **Reporting on entities includes following information:**
  - ✓ Information on assets
  - ✓ Information on liabilities
  - ✓ Information on capital (i.e. net value) and capital variance; information on revenues and expenditures
  - ✓ Information on cash flow



## Modified Cash Basis Method



Financial reporting can include reporting forms and textual information, that shall be submitted separately, or it can be inseparable part of the budget execution report

### **Financial reporting should contain following information:**

*Whether resources were obtained and used in accordance with planned budget*

*Whether resources were obtained and used in compliance with legal and contractual requirements, taking into consideration financial restrictions, provided for by the legislation*

*Whether organization can continue provision of goods and services of the same volume*

*Define the volume of financial resources, that should be allocated to the organization in future, so that it is able to continue implementation of functions, assigned to it*



## Modified Cash Basis Method



**Taking into consideration specificity of functioning of the budgetary system, economic activities shall be ascribed to the period, when primary documentation was submitted to the accounting service of the relevant organization**

Recognition of revenues and expenditures is conducted on the basis of budgetary classification definitions

In the process of reporting of revenues, they are classified into revenues from exchange transactions and non-exchange transactions

In the balance are reflected only those assets and liabilities, which comply with criteria, defined in budgetary classification and given rules



## Modified Cash Basis Method



Financial status report (balance) is provided in vertical format and the form is filled in accordance with the principle of materiality – i.e. organization must group information on assets and liabilities into material and immaterial (aggregated) indicators

Assets are classified into long term assets and short term assets, as well as financial and non financial assets

Liabilities are classified by their term

Chart of accounts is detailed into cash accounts and their equivalent accounts, as well as other financial assets (payables and accounts receivable)



## Modified Cash Basis Method



- ❖ Activities of budgetary entities are divided into operational (primary) and non-operational (secondary) activities
- ❖ According to the accounting principles in the process of consolidation internal operations between controlling entities and entities subject to control shall be excluded.
- ❖ In the process of assessment of financial status shall be taken into consideration net value of assets and profit and loss indicators (*for entities, who are authorized to be engaged in economic activities*)
- ❖ **Information on financial status (balance) fully covers such issues, as cash or non-cash assets and liabilities, derived from transactions implemented by budgetary funds, non-budgetary funds, donor funding (i.e. third party payments), exchange or non-exchange operations and non-operating activities.**





## Modified Cash Basis Method



- ❖ **Information on financial status (balance)** — *is complete accounting information on a budgetary entity, except for information on financial liabilities in the form of debts and information on financial assets, received from foreign sources*
- ❖ Information on debts and financial assets received from foreign sources, as well as interest accrued on liabilities shall be reflected in the aggregated financial reports, compiled on the basis of data available in the Debt Management Module of the Ministry of Finance and the Treasury
- ❖ Information on financial status should be in compliance with the state budget execution indicators, which include donor funding as well.



## Modified Cash Basis Method



- ❖ One of components of financial reporting is “cash flow reporting”
- ❖ Cash flow is divided into:
  - *Operating activities*
  - *Investment activities*
  - *Financial activities*
- ❖ In the reporting so called “third party payments”, i.e. funds provided by donor organizations for funding of investment projects, which are not channeled to Treasury Accounts, are reflected in a separate column
- ❖ Reporting of cash flow is conducted through **indirect method**
- ❖ Indirect method shall be used prior to finalization of **Treasury General Ledger**



## Modified Cash Basis Method



- ❖ Financial performance and capital variance is calculated:
  - By "net value" – in the event of budgetary funds
  - By „profit and loss” - in the event of non-budgetary funds (i.e. obtained as a result of economic activity)
- ❖ Reports reflect all financial performance results and capital variance, which is reflected in the financial status reporting (balance)
- ❖ By reconciliation of actual spending is obtained information on targeted use of budgetary resources and whether relevant information is fully reflected in the budget execution reports and financial reporting
- ❖ To the reporting shall be attached information on accounting policy and errors, as well as events that occurred after the date of reporting
- ❖ Explanatory notes represent additional information, necessary for better understanding of financial and non-financial reporting (e.g. turnover of non-financial assets), as well as other information, taking into consideration specificity of a budgetary entity



## Obtained Results



- ❖ Financial reporting has improved and became more compliant with international standards
- ❖ Reporting has expanded and covers external and internal debts
- ❖ As a result of cash flow reporting, which at current stage is happening only in centralized manner:
  - ✓ *additional information on public sector entities is obtained*
  - ✓ *Effective assessment of public sector liquidity and the volume of cash flow, as well as better planning of future cash flow is possible*
- ❖ Classification of assets and liabilities into long-term and short-term and their reflecting according to their term allows to improve control over targeted use of budgetary resources and plan future spending more effectively



## Challenges in reporting



### ❖ IPSAS and GFS 2001 provide different definitions for:

- Assets and liability classification
- consolidation and criteria for entities, subject to consolidation
  - *economic organization of financial reporting, where control is the main defining criteria*
  - *Institutional unit for government finance statistics, which has the right to possess assets, undertake commitments and participate in economic activity*
- Realized profit and book profit and loss and other economic flows
- Classification of activities of a budgetary entity for accounting of cash flow

### ❖ Assessment of assets at fair value and charging of depreciation

### ❖ Incompliance of accounting policy with current taxation legislation for financial reporting purposes



## Future plans



Complete transfer to IPSAS accrual method during 2014-2020 through inclusion of relevant **interpretations** in national standards

For the purpose of full harmonization of financial and budgetary accounting and reporting the Treasury General Ledger, the unified chart of accounts and operations reference guide shall become fully operational

Re-evaluation of long term assets and introduction of fair value method at the stage of introduction of international standards

Introduction of training program for public sector certified accountants for the purpose of provision of education in the sphere of international accounting standards

Preparation of consolidated financial reports in accordance with IPSAS accrual basis method.



**Thank you for attention!**

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