

**PEMPAL**

**GLOSSARY OF PUBLIC  
FINANCIAL MANAGEMENT**

**VERSION 1  
APRIL 2011**



# INTRODUCTION

This Glossary is intended to provide PFM practitioners in the PEMPAL region with a glossary and explanation of key terms and concepts. The objective is to enable a consistent approach when using terminology and also to facilitate meaningful translation of the terminology.

The Glossary is divided into two parts:

**PART I** Tabular listing of key terms and brief definitions. Wherever appropriate these are based on the IPSAS definitions

**PART II** A summary explanation of key concepts and related terminology

Where appropriate definitions in Part I are cross referenced to the explanations in Part II

This Glossary is intended to be a resource that develops over time and is contributed to by practitioners within PEMPAL

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# ABBREVIATIONS

CHU	Central Harmonisation Unit
CoA	Chart of Accounts
COFOG	Classification Of the Functions Of Government
COSO	Committee Of Sponsoring Organisations
COTS	Commercial Off The Shelf [software application package]
E AFC	Ex Ante Financial Control
EBF	Extra Budgetary Funds
ESA	European System of national and regional Accounts
EU	European Union
FMC	Financial Management Control
FMIS	Financial Management Information System
GBE	Government Business Enterprise
GFS	(IMF) Government Finance Statistics
GFSM	Government Finance Statistics Manual
GGS	General Government Sector
IA	Internal Audit
ICT	Information and Communications Technology
IFMIS	Integrated Financial Management Information System
IFRS	International Financial Reporting Standard
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standard
IPSASB	International Public Sector Accounting Standards Board
IT	Information Technology
LAN	Local Area Network
MTBF	Medium Term Budget Framework
MTEF	Medium-Term Expenditure Framework
MTFF	Medium Term Fiscal Framework
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PIFC	Public Internal Financial Control
PRINCE	PRojects IN a Controlled Environment
RFP	Request For Proposals
SPN	Specific Procurement Notice
TSA	Treasury Single Account
UN	United Nations
UNSNA	UN System of National Accounts
WAN	Wide Area Network
WB	World Bank

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## PART I – SUMMARISED GLOSSARY OF TERMS

Term	Definition
Accrual basis	See Part II definitions
Accounting basis	See Part II definitions
Accounting policies	The specific principles, bases, conventions, rules, and practices applied by an entity in preparing and presenting financial statements.
Annual budget	An approved budget for one year. It does not include published forward estimates or projections for periods beyond the budget period.
Appropriation	An authorization granted by a legislative body to allocate funds for purposes specified by the legislature or similar authority
Approved budget	The expenditure authority derived from laws, appropriation bills, government ordinances, and other decisions related to the anticipated revenue or receipts for the budgetary period.
Assets	Resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.
Borrowing costs	Interest and other expenses incurred by an entity in connection with the borrowing of funds.
Cash	Comprises cash on hand and demand deposits.
Cash basis:	See Part II definitions
Cash equivalents	Short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.
Cash flows	Inflows and outflows of cash and cash equivalents.
Change in accounting estimate	An adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not correction of errors.
Closing rate	The spot exchange rate at the reporting date.
Comparable basis	The actual amounts presented on the same accounting basis, same classification basis, for the same entities, and for the same period as the approved budget.
Consolidated financial statements	The financial statements of an economic entity presented as those of a single entity.
Construction contract	A contract, or a similar binding arrangement, specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology, and function or their ultimate purpose or use.
Contingent asset	A possible asset that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.
Contingent liability	See Part II
Control	The power to govern the financial and operating policies of another entity so as to benefit from its activities.
Controlled entity	An entity, including an unincorporated entity such as a partnership, which is under the control of another entity (known as the controlling entity).
Controlling entity	An entity that has one or more controlled entities.

Term	Definition
Cost	The amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction.
Currency risk	The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.
Depreciation	See Part II
Economic entity	A group of entities comprising a controlling entity and one or more controlled entities.
Economic life	Either: (a) expected to yield economic benefits or service potential to one or more users; or (b) The number of production or similar units expected to be obtained from the asset by one or more users.
Events after the reporting date	Those events, both favourable and unfavourable, that occur between the reporting date and the date when the financial statements are authorized for issue. Two types of events can be identified: (a) Those that provide evidence of conditions that existed at the reporting date (adjusting events after the reporting date); and (b) Those that are indicative of conditions that arose after the reporting date (no adjusting events after the reporting date).
Exchange difference	The difference resulting from translating a given number of units of one currency into another currency at different exchange rates.
Exchange rate	The ratio of exchange for two currencies.
Exchange transactions	Transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.
Final budget	The original budget, adjusted for all reserves, carry-over amounts, transfers, allocations, supplemental appropriations, and other authorized legislative or similar authority, changes applicable to the budget period
Financial asset	Any asset that is: (a) Cash; (b) An equity instrument of another entity; (c) A contractual right: (i) To receive cash or another financial asset from another entity; or (ii) To exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity; or (d) A contract that will or may be settled in the entity's own equity instruments and is: (i) A non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or (ii) A derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments classified as equity instruments in accordance with paragraphs 15 and 16, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 17 and 18, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments.



Term	Definition
Financial liability	Any liability that is: (a) A contractual obligation: (i) To deliver cash or another financial asset to another entity; or (ii) To exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or (b) A contract that will or may be settled in the entity's own equity instruments and is: (i) A non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or (ii) A derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments classified as equity instruments in accordance with paragraphs 15 and 16, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 17 and 18, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments. As an exception, an instrument that meets the definition of a financial liability is classified as an equity instrument if it has all the features and meets the conditions in paragraph 15 and 16 or paragraphs 17 and 18.
Foreign currency	A currency other than the functional currency of the entity.
General government sector	Comprises all organizational entities of the general government as defined in statistical bases of financial reporting
Government Business Enterprise	An entity that has all the following characteristics: (a) Is an entity with the power to contract in its own name; (b) Has been assigned the financial and operational authority to carry on a business; (c) Sells goods and services, in the normal course of its business, to other entities at a profit or full cost recovery; (d) Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm's length); and (e) Is controlled by a public sector entity.
Intangible asset	An identifiable non-monetary asset without physical substance.
Inventories	Assets: (a) In the form of materials or supplies to be consumed in the production process; (b) In the form of materials or supplies to be consumed or distributed in the rendering of services; (c) Held for sale or distribution in the ordinary course of operations; or (d) In the process of production for sale or distribution
Liabilities	See Part II
Liquidity risk	The risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.
Loans and receivables	Non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than: (a) Those that the entity intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through surplus or deficit; (b) Those that the entity upon initial recognition designates as available for sale; or (c) Those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale.
Loans payable.	Financial liabilities, other than short-term trade payables on normal credit terms
Material	Omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements. Materiality depends on the nature and size of the omission or misstatement judged in the surrounding circumstances. The nature or size of the item, or a combination of both, could be the determining factor.
Monetary items	Units of currency held and assets and liabilities to be received or paid in fixed or determinable number of units of currency.

Term	Definition
Monetary financial assets and financial liabilities (also referred to as monetary financial instruments)	Financial assets and financial liabilities to be received or paid in fixed or determinable amounts of money.
Multi-year budget	See Part II
Net assets/equity	The residual interest in the assets of the entity after deducting all its liabilities.
Net realizable value	The estimated selling price in the ordinary course of operations, less the estimated costs of completion and the estimated costs necessary to make the sale, exchange or distribution.
Non-exchange transactions	Transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.
Operating activities	The activities of the entity that are not investing or financing activities.
Prior period errors	Omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that: (a) Was available when financial statements for those periods were authorized for issue; and (b) Could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements. Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud
Property, plant, and equipment	Tangible items that: (a) Are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and (b) Are expected to be used during more than one reporting period.
Provision	A liability of uncertain timing or amount.
Reporting date	The date of the last day of the reporting period to which the financial statements relate.
Revenue	The gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners.
Transaction costs	Incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability (see [IPSAS 29] Appendix A paragraph AG26). An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial instrument.
Transfers	Inflows of future economic benefits or service potential from non-exchange transactions, other than taxes.

## PART II – DEFINITIONS OF KEY CONCEPTS

### 1. BASIS OF ACCOUNTING

#### Definition

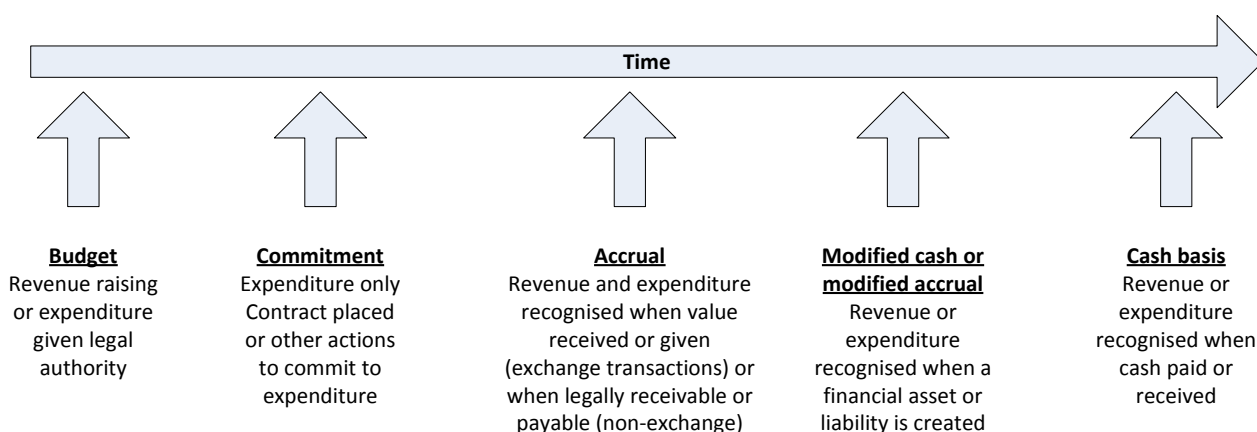
According to IPSAS: “The accrual or cash basis of accounting as defined in the accrual basis IPSASs and the Cash Basis IPSAS”. However, this definition is not explanatory. A better definition is “when revenues, expenditures, expenses, and transfers - and the related assets and liabilities are recognized in the accounts and reported in the financial statements”<sup>1</sup>.

As indicated by the definition IPSAS recognise two basis of accounting as defined below:

- **Cash basis:** a basis of accounting that recognizes transactions and other events only when cash is received or paid.
- **Accrual basis:** a basis of accounting under which transactions and other events are recognized when they occur (and not only when cash or its equivalent is received or paid). Therefore, the transactions and events are recorded in the accounting records and recognized in the financial statements of the periods to which they relate. The elements recognized under accrual accounting are assets, liabilities, net assets/equity, revenue, and expenses.

Although IPSAS only recognise cash or accrual, many (indeed most) countries adopt modified cash or modified accrual accounting. Also, commitment accounting is widely advocated as an important tool for budget management. All accounting basis may be envisioned as points within on a scale as illustrated below.

Figure 1: Basis of Accounting



<sup>1</sup> Washoe County, Nevada Glossary of Terms for Financial Reports

There is no official definition of modified cash or modified accrual accounting. Nor is there any clear distinction between the terms. For the purposes of this glossary, modified cash and modified accrual are treated as being synonymous. A recent article suggested a definition and this is reproduced on the next page.

Commitment accounting is not an accounting base. It is only applied to expenditures and is an important budget management tool. Only by tracking commitment (which often extend several years into the future) can the budget resources already committed or spent be identified. This enables both cash planning and effective budget management.

## Box 1: Definition of the Modified Cash Basis<sup>2</sup>

The Modified Cash Basis of Accounting will recognise transactions only when cash, financial assets or liabilities are paid or received. The Statement of Financial Position (Balance Sheet) will include financial assets and financial liabilities. For the purpose of this definition:

- A financial asset is any asset that is:
  - (a) Cash
    - (i) Cash comprises cash on hand, demand deposits and cash equivalents
    - (ii) Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value
  - (b) An equity instrument of another entity;

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities

- (c) A contractual right:
  - (i) To receive cash or another financial asset from another entity; or
  - (ii) To exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity
- (d) A contract that will or may be settled in the entity's own equity instruments and is:
  - (i) A non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or
  - (ii) A derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments classified as equity instruments in accordance with paragraphs 15 and 16 of IPSAS 28, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 17 and 18 of IPSAS 28, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments.

- A financial liability is any liability that is
  - (a) a contractual obligation:
    - (i) To deliver cash or another financial asset to another entity; or
    - (ii) To exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity
  - (b) A contract that will or may be settled in the entity's own equity instruments and is:
    - (i) A non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or
    - (ii) A derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments classified as equity instruments in accordance with paragraphs 15 and 16 of IPSAS 28, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 17 and 18 of IPSAS 28, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments.

- A payment occurs when there is an outflow of financial assets or an inflow of financial liabilities
- A receipt occurs when there is an inflow of financial assets or an outflow of financial liabilities.

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<sup>2</sup> Michael Parry, International Journal of Government Financial Management, December 2010

## 2. CHART OF ACCOUNTS

The Chart of Accounts is the list of accounts in the general ledger of a double entry bookkeeping system. In a manual accounting system each item in the Chart of Accounts would represent an actual account.

There are several related concepts:

- **Sub-ledger** – also derives from manual bookkeeping. To enable several clerks to work on accounts the ledger was divided into sub-ledgers. For each sub-ledger a “Control Account” is established in the General Ledger. The Control Account always represents the total of the balances in the sub-ledger. Transaction totals are entered in the Control Account periodically (usually daily) and in detail in the sub-ledger.
- **Budget classification** – the coding structure applied to the budget. In most countries the budget codes are identical to the revenue and expenditure codes in the chart of accounts. This facilitates comparison. However in some regions, notably former Soviet Union countries, the tradition is of a budget classification quite separate to the chart of accounts, necessitating bridge tables to enable comparison.

### Chart of accounts in a computerised system

Computerised accounting systems are based on relational database concepts. This enables multiple codes to be assigned to each transaction. Thus analysis can be, for example, by type of revenue or expenditure, organisational entity, geographic area, etc. The different types of analysis are usually referred to as the dimensions of the analysis. There is no theoretical limit to range of analysis (number of dimensions) that is possible, but see below on practical limitations.

Within a computerised accounting system the concepts of double entry remain important. Double entry enables each transaction to be linked to a flow that changes the value of an asset or a liability. In aggregate the flows over an accounting period (the operating statement plus holding gains and losses) link the opening and closing balance sheets.

To enable double entry ledger the accounts that form the general ledger must be defined – the chart of accounts. Usually the Chart of Accounts will be the economic codes. All other codes then exist for analytic purposes but are not part of the general ledger.

#### *Definition of the Chart of Accounts within a computerised accounting system*

- **Narrow definition:** the Chart of Accounts comprises those codes used to complete the double entry bookkeeping system and prepare the Financial Statements
- **Broad definition** – the chart of accounts comprises all codes used to analyse transactions and identify assets and liabilities

The above two definitions are frequently used interchangeably and without adequate explanation.

***Other concepts under a computerised accounting system:***

- **Sub-ledgers** – most computerised systems use the concepts of sub-ledgers as described above, except that the maintenance of control accounts is automated. Sub-ledgers are useful for detailed analysis of a particular category of item not required for the general ledger.
- **Budget classification** – if the budget preparation process is integrated within the same computer application software as the accounting system it is essential that the same codes are used for the budget as for general ledger.

***Limitations on the analytic dimensions within a computerised accounting system***

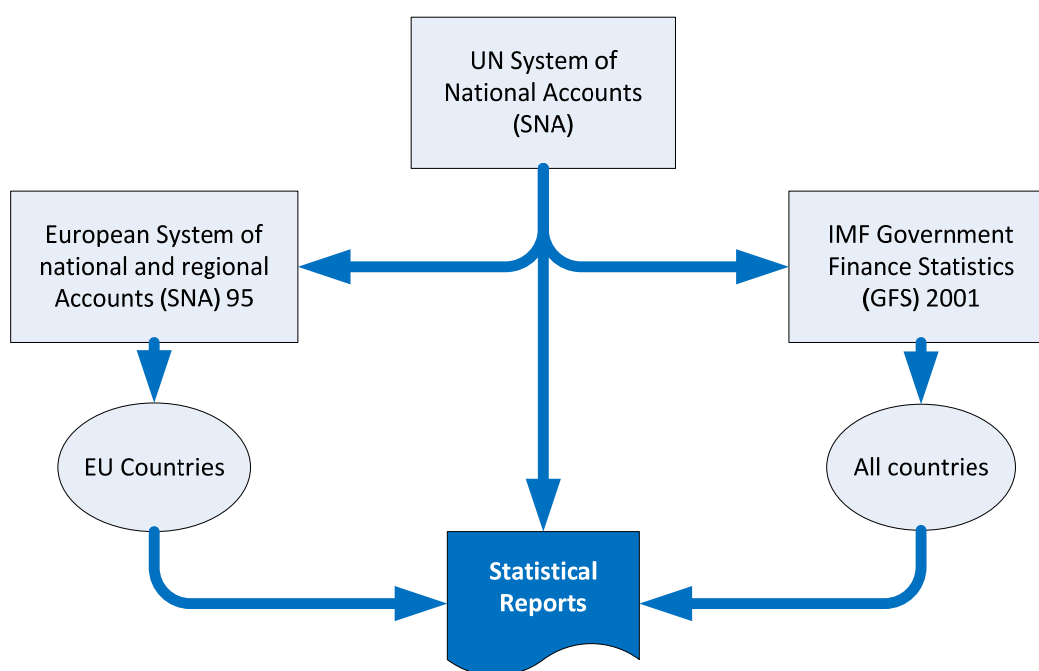
- All Commercial Off The Shelf (COTS) accounting applications will have a designed structure for the chart of accounts and for additional analysis. This will impose limits on the analysis that is possible. More expensive packages tend to have more sophisticated and flexible analytic capability.
- Each transaction must be coded by a clerk. Hence there is a practical limit to the amount of analysis a clerk can code. The more complex the analysis the greater (i) the training requirement, (ii) the time to enter each transaction and (iii) the error rate. These factors must be balanced against the benefits of the analysis.

### 3. STATISTICAL FINANCIAL REPORTING SYSTEMS

Statistical financial reporting systems have been introduced by international bodies to gather information on individual countries so as to be able to provide cross country comparisons on a standardised basis. Three such systems are relevant:

- The UN System of National Accounts (SNA)
- The IMF Government Finance Statistics (GFS) 2001 as set out in the GFS Manual (GFSM)
- The European System of national and regional Accounts (ESA) 95 as set out by Eurostat, the European Statistical office.

Their relationship is summarised in the model below.



#### *The UN System of National Accounts (UNSNA)*

The aim of UNSNA is to provide an integrated and complete system of accounts enabling international comparisons of all significant economic activity within a given country. It does not relate to the Government or any other specific sector but rather to the whole of a sovereign entity – hence the term “national” accounts. Also the UNSNA contains much information other than financial, e.g. the production account, household expenditure account.

Hence, the UNSNA is not directly relevant to public financial management, though much of the financial information within the UNSNA will come from public financial management reporting systems. Therefore, it is important that there is consistency between the definitions used in UNSNA, GFS, ESA and ultimately the classification systems of government accounting. In particular the UNSNA defines a “**Classification of the Functions of Government**” (COFOG) that is used by GFS 2001 and ESA 95.



### **The IMF Government Finance Statistics (GFS) 2001**

The IMF GFS is a comprehensive system for reporting on the activities of the General Government Sector (GGS) within each country. The system is fully described in the GFS Manual (GFSM). Although described as a statistical reporting system it has all of the attributes of an accounting system:

- It adopts an accounting model
- It defines many accounting concepts, e.g. assets, liabilities, revenues, expenditures, etc
- It prescribes reporting formats including an operating statement and a balance sheet.

### **European System of national and Regional Accounts (ESA) 95**

ESA 95 fulfils the same role as GFS but is used instead of GFS for Government financial reporting within Europe. The rules and reporting formats for ESA95 are defined by Eurostat. ESA 95 is consistent with the UNSNA and is largely harmonised with *GFS 2001*. However, whilst definitions of concepts in GFS and ESA95 are the same, differences exist between the two statistical systems<sup>3</sup>. The most important difference is the focus of the GFS system on financial transactions—taxing, spending, borrowing, and lending—while the *ESA 95* focuses on the production and consumption of goods and services.

*ESA 95* consists of a set of macroeconomic accounts, balance sheets, and tables based on a set of internationally agreed concepts, definitions, classifications and accounting rules. It provides a record of the complex economic activities taking place within an economy. Several conceptual differences exist between the *ESA 95* and *GFSM 2001* data. Three of the most significant are the presentation of social security, the treatment of government employer retirement pension schemes, and the consolidation rules for transactions and balances. The last of these three is significant for financial reporting.

Area of difference	GFS 2001	ESA 95
<b>1. Social security</b>	Social security is included as part of the sector that administers the social security scheme, usually central government. Hence they are presented both unconsolidated as a subsector of central government, and also consolidated with the budgetary and extrabudgetary entities to show the consolidated central government.	Social security schemes are a separate subsector and not consolidated in central government.
<b>2. Pension contributions</b>	Contributions and benefits paid under government employer unfunded pension schemes are treated as financial transactions. This requires an imputation of government liabilities related to the unfunded pension schemes, and imputed interest on that liability	treated as contributions and benefits in the current accounts
<b>3. Consolidation</b>	GFS (and IPSAS) consolidation rules require the elimination of transactions between general government units, as well as stocks of assets and liabilities that represent claims by one general government unit on another general government unit. The transactions that can be more easily identified in practice are interest, taxes, grants, and financing transactions.	Flows and stocks between constituent units are not consolidated as a matter of principle. However, consolidated accounts may be built up for complementary presentations and analysis.

Other differences are:

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<sup>3</sup> The explanation in this sub-section is based on “ The Government Finance Statistics Manual 2001 Framework and Its Relationship with The European System of Accounts 1995” on the IMF web site

- ESA95 differs from GFS in the presentation of its reports, and its concepts are more specific and precise
- ESA95 is more rule based than 1993 SNA

### ***Comparison of statistical reporting systems and IPSAS***

The IMF GFS is directly relevant to the design of a Government financial reporting system. However, the GFS are not accounting standards. There are significant differences between the GFS and IPSAS. The IPSASB has published a comparison of the IPSAS, GFS and ESA 95<sup>4</sup>. Some of the most significant differences are summarised in the table below.

<b>Area of difference</b>	<b>Statistical systems</b>	<b>IPSAS</b>
Entity definition	Defines the entity as the General Government Sector and only reports on that sector	Apply to each separate entity within Government and also the whole of government on the basis of control (Note however IPSAS 22 provides for reporting on the GGS)
Basis of accounting	Accrual only (but most countries still report on cash basis)	Accrual or cash basis
Financial reports	Unaudited reports in a prescribed format	Audited Financial Statements which must meet minimum information requirements but without a prescribed format
Concepts such as materiality and prior year adjustments	Not recognised	Fundamental part reporting in Financial Statements
Classification	Prescribed in detail	Not prescribed; any classification acceptable as long as it enables required information in Financial Statements

These differences present a challenge when designing an accounting system to enable reporting under both GFS and IPSAS. However, it should be noted that neither GFS 2001 nor ESA 95 prescribe mandatory rules for the accounting system or chart of accounts; as long as the system can generate the required reports it meets the requirements for statistical reporting.

In deciding which information to use, it is a matter of deciding what you want to know:

- If you want to know how the government is performing financially, you need the IPSAS based full consolidation
- If you want to know the fiscal effects of the financial transactions of the general government sector on the national economy, you need the GFS/ESA95 general government operating result

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<sup>4</sup> "International Public Sector Accounting Standards (IPSASs) and Statistical Bases of Financial Reporting: an Analysis of Differences and Recommendations for Convergence" IPSASB January 2005

## 4. FINANCIAL MANAGEMENT INFORMATION SYSTEMS

Computerised accounting systems for public financial management are commonly referred to as “Treasury Systems” (though strictly such systems do not include line Ministries) or “Integrated Financial Management Information Systems” (IFMIS). In this glossary the term IFMIS is used.

The most comprehensive definition of an IFMIS is contained in the World Bank Treasury reference model<sup>5</sup>. This describes the structure and components of Treasury system and also the basis of a more comprehensive integrated system. A simplified version of the model is set out on the next page.

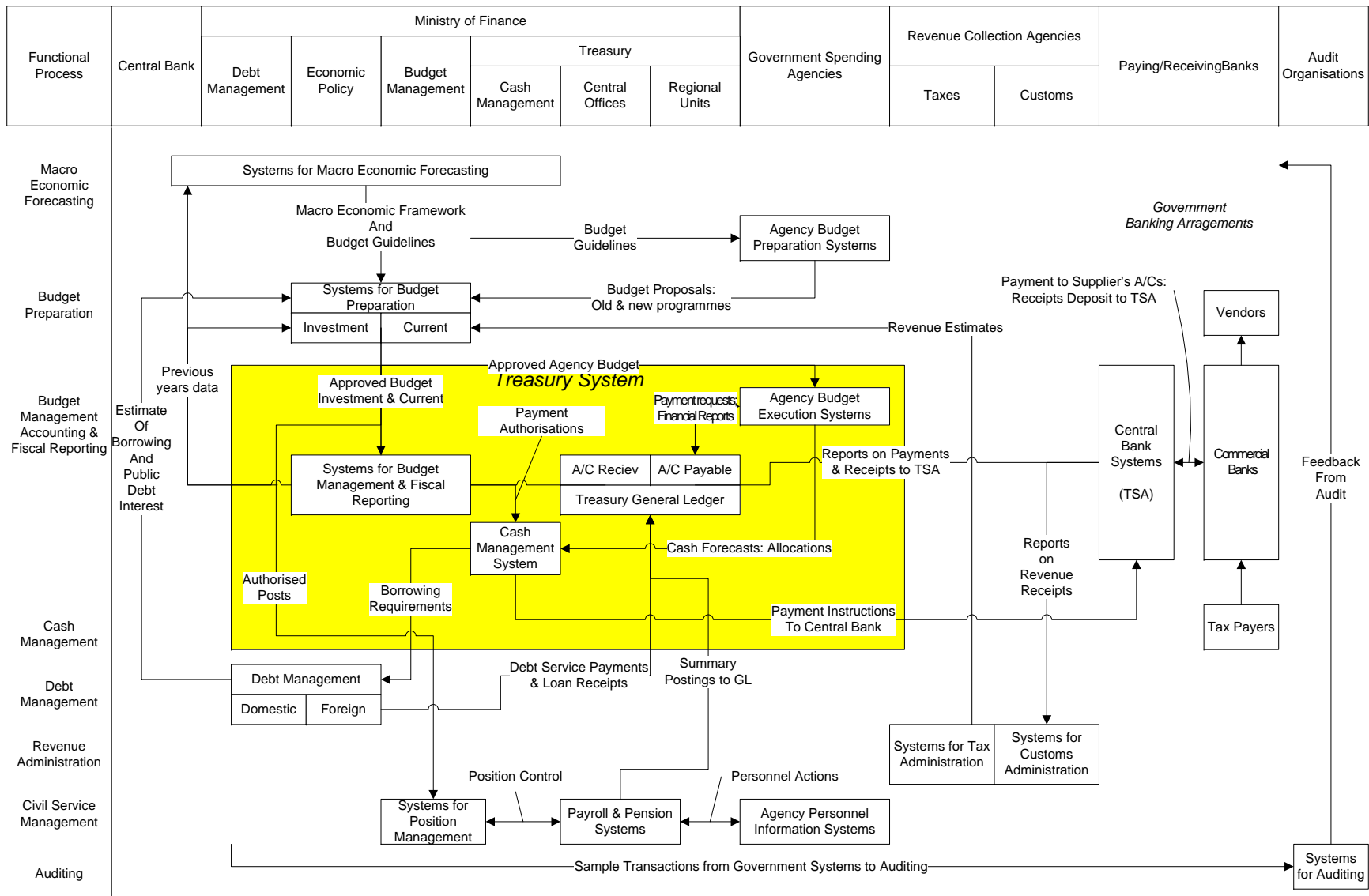
There are a number of important terms that are defined below that have specific relevance to IFMIS. Note that common computer terminology is not included in this glossary as this can be found in any text book.

Term	Definition
Application software	The software to undertake a specific PFM function or group of functions, e.g. accounting, debt management
Bespoke software	See “custom developed software”
COTS	Commercial Off The Shelf application software – package software already developed with most generally required functionality for a particular application. Most may vary from a few dollars to millions of dollars
Custom developed software	Software application developed specifically for one user, e.g. a government accounting system. This is the alternative to a COTS package
Go Live	The stage at which a specific application (COTS or bespoke) has completed testing, is signed off by the customer and actually starts processing data
Integration and interfacing systems	The definition of an integrated system is quite lengthy, but in general it means a system with several different functions but where the user perceives the whole application as a single system.  In contrast, interfacing means that two different systems are able to exchange information with each other. Interfacing may be managed either manually or an automated process.
LANs and WANs	A LAN is Local Area Network – usually within a single building. By way of contrast a WAN is a Wide Area Network connecting physically remote sites.
PRINCE	<u>P</u> rojects <u>I</u> n a <u>C</u> ontrolled <u>E</u> nvironment – a project management methodology developed by a UK Government agency and now available for general use. PRINCE is a complete system with manuals and a certification programme for practitioners. It is designed to ensure that a structured approach is followed for the implementation of complex IT projects that minimises the risk of time or cost overruns or a failure to deliver the required functionality.

<sup>5</sup> “Treasury Reference Model”, the World Bank May 2001

Term	Definition
Procurement (or acquisition) methodology	<p>The methodology used to procure an IFMIS. The World Bank has a specific Information and Communication Technology (ICT) procurement methodology which must be used for World Bank funded procurement and is often used as a model for government procurement. There are two options under the World Bank procurement methodology:</p> <ul style="list-style-type: none"> <li>• Single Stage – procurement is made on the basis of the specification without any scope for amendments and second stage bidding – suitable for small or very urgent procurement</li> <li>• Two-stage – after stage 1 bids requirements can be amended and shortlisted bidders re-bid against amended requirements – the preferred approach for major procurements</li> </ul>
RFP	Request For Proposals
Rollout	The phased implementation of a system across a series of sites
SPN	Specific Procurement Notice – a notice that must be published under WB procurement procedures. It states in detail the proposed procurement and methodology to acquire the bidding documents.
Systems architecture	<p>The overall design of the system, its components and their relationship to each other. This can be sub-divided into:</p> <ul style="list-style-type: none"> <li>• Software architecture – the relationship of the software functions and applications</li> <li>• Hardware architecture – the relationship of the hardware components</li> </ul>
Systems specification	<p>The statement of the detailed requirements against bidders must submit their proposals. This divides into:</p> <ul style="list-style-type: none"> <li>• Technical requirements, e.g. hardware, communications, performance requirements</li> <li>• User requirements – a statement of the financial management functionality required from the system. User requirements further sub-divide into: <ul style="list-style-type: none"> <li>○ Mandatory – essential requirements – if not met then a bid will automatically be rejected</li> <li>○ Desirable – a bid will not be rejected if a desirable requirement is not achieved but the failure will count against the bid in the scoring</li> </ul> </li> </ul>
Test scripts	A test script contains a specific transaction or group of transactions. Both during bidding and subsequent testing the new IFMIS will be required to process the data in the test script to confirm the process and outputs achieve the desired result.

Figure 2: Treasury Reference Model



## 5. ASSETS AND LIABILITY VALUES AND DEPRECIATION

Fundamental to the concept of accrual accounting is the requirement to value assets and liabilities. Changes in the value of assets represent financial flows. These are variously described as:

- Depreciation
- Amortisation
- Holding gains or losses
- Revaluation gains or losses

There is a discussion of the concepts involved in the IPSASB Paper on the Conceptual Framework for PFM Financial Statements<sup>6</sup> This note only defines and explains the important terminology.

### *Methods of valuing assets and liabilities*

There are three approaches to measuring value:

Measurement Basis	Definition	Historical or Current?	Entry or Exit?	Market or Entity-Specific?	Capital Concept
<b>1. Historical cost</b>	Amount paid or liability incurred when asset or liability acquired	Historical	Entry	Entity-specific	Financial capital
<b>2. Market value</b> (Same as Fair Value as defined for IPSAS and IFRS)	The estimated amount for which an asset could be exchanged on the date of the valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently, and without compulsion <sup>7</sup>	Current	May be either	Market	Market value (ability to earn a market return)
<b>3. Replacement cost</b>	The most economic cost required for the entity to replace the service potential of an asset (including the amount that the entity will receive from its disposal at the end of its useful life) at the reporting date	Current	Entry	Entity-specific	Operating capacity
<b>4. Deprival value</b> (Same as economic concept of opportunity cost)	Deprival value is the amount that would just compensate the entity for the loss of an asset.  The deprival model is not an actual valuation base but a criteria for choosing between valuation basis	Current	Entity	Entity specific	Operating capacity

<sup>6</sup> "Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Measurement of Assets and Liabilities in Financial Statements" IPSASB December 2010

<sup>7</sup> "Concepts Fundamental to Generally Accepted Valuation Principles (GAVP)" paragraph 5.2 International Valuation Standards Council

**Notes:**

1. Historical cost means value is based on the amount paid or liability incurred when acquired. On the other hand current refers to the value at the reporting date.
2. Entry basis reflects the consideration payable (or receivable) for the acquisition (or assumption) of an asset (or liability). An exit basis reflects the amount that will be derived from the asset, often from its sale or from its continuing use.
3. A market refers to the value of the asset or liability in an acquisition or disposal to the general market for such assets or liabilities. This will often be different to the value to the specific entity that owns the asset or liability.
4. The capital concept refers to the information provided by the entity balance sheet. Does such value represent the historic financial flows (financial capital), current market value, or the ability of the entity to provide future services? Each measurement base relates to a different concept of capital.

All of the above concepts are derived from commercial accounting where assets are acquired and liabilities incurred in order to generate economic flows. The concepts of replacement cost and deprival value are more difficult to apply where service benefits rather than economic flows are the intended outcome.

***Depreciation and amortisation***

The two terms have the same meaning. They only apply when historical cost or market (+fair) value is used to measure the value of an asset. In such cases the depreciation (or amortisation) is the assumed decline in value of the asset over a period time. It is a method for spreading the cost of an asset over its estimated useful life:

- The annual depreciation is treated as an expenditure in the operating statement
- The accumulated depreciation reduces the value of the asset in the balance sheet
- When an asset is disposed both the original cost and the accumulated depreciation have to be netted against disposal proceeds to establish the gain or loss on disposal, which is also a flow in the operating statement.

***Treatment under IPSAS and statistical systems***

IPSAS allows fixed assets to be valued either at cost or at fair (market) value. Current assets and all liabilities will generally be shown at cost with the exception of amounts denominated in foreign currencies, when current exchange rates at the reporting date will be used.

The treatment revaluation gains or losses under IPSAS is complex and depends on the type of asset or liability. In general, revaluation gains on fixed assets are credited directly to net equity<sup>8</sup>; all revaluation losses and gains on current assets are charged in the operating statement. However, there are a number of exceptions to this generalisation.

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<sup>8</sup> The concept of "Net Equity" for governments and public sector entities is conceptually difficult and is not recognised at all in GFS and ESA95. In British and US based systems it is generally referred to as a Fund, e.g. Consolidated Fund. It is best defined as the difference between net assets and net liabilities.

Under statistical reporting systems all assets and liabilities are valued at market value for every financial report, i.e. annually. Gains or losses on revaluation are treated as holding gains and reported separately to the operating statement in the GFS statement of “Other economic flows”. Under this approach, there is no annual or accumulated depreciation.

Note that in practice the IMF will accept cost less accumulated depreciation as a reasonable surrogate measure for market value. This avoids the need to use different values for GFS and IPSAS reporting.



## 6. TREASURY SINGLE ACCOUNT

A Treasury Single Account (TSA) is a unified structure of government bank accounts that gives a consolidated view of government cash resources. A TSA is a bank account or a set of linked accounts through which the government transacts all its receipts and payments<sup>9</sup>. While it is necessary to distinguish individual cash transactions for control and reporting purposes, this purpose is achieved through the accounting system and not by holding/depositing cash in transaction specific bank accounts. This enables the treasury to delink management of cash from control at a transaction level.

Requirements for a TSA:

- An automated Treasury system make it much more feasible to implement a TSA. Automated transaction processing can enable the analysis and control of transactions without the need for separate bank accounts.
- A legal basis for the TSA to ensure broad implementation across government and also to ensure stability of the system

Three key features of a TSA are:

1. The government banking arrangement should be unified, to enable Treasury oversight of government cash flows in and out of these bank accounts.
2. No other government agency operates bank accounts outside the oversight of the treasury.
3. The consolidation of government cash resources should be comprehensive and encompass all government cash resources, both budgetary and extra-budgetary.

**The benefits of a TSA flow from its objectives:**

- Allows complete and timely information on government cash resources. In countries with IFMIS with adequate interfaces with the banking system, this information will be available in real time.
- Improves appropriation control. The TSA ensures that the MoF has full control over budget allocations, and strengthens the authority of the budget appropriation.
- Improves operational control during budget execution. When the treasury has full information about cash resources, it can plan and implement budget execution in an efficient, transparent, and reliable manner.
- Enables efficient cash management. A TSA facilitates regular monitoring of government cash balances.
- Reduces bank fees and transaction costs.
- Facilitates efficient payment mechanisms.
- Improves bank reconciliation and quality of fiscal data. Lowers liquidity reserve needs. A TSA reduces the volatility of cash flows through the treasury, thus allowing it to maintain a lower cash reserve/buffer to meet unexpected fiscal volatility.

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<sup>9</sup> The material in this section is based on the IMF Working Paper WP/10/143 "Treasury Single Account: Concept, Design, and Implementation Issues" Sailendra Pattanayak and Israel Fainboim, IMF May 2010

### **TSA parameters**

Delineating the boundary of a TSA is important and needs to be carefully considered in light of each country's institutional and legal/regulatory framework

At a minimum, the TSA should cover all central government entities and their Transactions. It has become international good practice to include as many government-controlled trust funds and Extra Budgetary Funds (EBFs) within the TSA as legally possible. However, including public corporations in the TSA is generally not advisable

In many countries donors and external loan providers require the government to manage their funds through separate commercial bank accounts and not through a TSA. However, in line with the donors' commitment under the Paris Declaration to use country PFM systems, the government should encourage official donors to integrate their resources into the TSA to the extent possible

### **TSA Structure**

There are two broad categories of TSA:

- A purely centralised arrangement is one in which all revenue and expenditure transactions of the government pass through a single account, generally maintained with the central bank.
- At the other extreme, a TSA could be virtually operational even though line agencies are allowed to retain separate transaction accounts in the banking system. However, in the latter case, balances in all transaction accounts should be swept into the TSA main account at the end of each day.

The degree of decentralization of a TSA structure is linked to the authority of various entities to access and operate the government bank accounts.

### **Various Types of Bank Accounts under a TSA System**

<b>TSA main account</b>	The Treasury's account with the Central Bank which consolidates the government's cash position. Cash balances in all other linked accounts are swept into this account
<b>TSA subsidiary accounts or sub-accounts</b>	Sub-accounts within the main TSA account. An accounting arrangement to group together a set of transactions and allows the government to maintain the distinct accounting identity or ledger of its budget organizations.
<b>Transaction accounts</b>	Sometimes government bank accounts that are justified for retail transaction banking operations are opened separately and are structured as transaction accounts.
<b>Zero-balance accounts (ZBAs)</b>	Where transactional accounts are necessary, these are generally opened on a zero-balance basis, i.e., end-of-the-day cash balances in these accounts are swept back into the TSA main account
<b>Imprest accounts</b>	Transaction accounts that can hold cash up to a maximum authorized amount and are recouped from time to time.
<b>Transit accounts</b>	Serves as a transit for eventual flow of cash into the TSA main account. Transit accounts might be necessary: (i) for major revenue streams to monitor their collection and remittance by the banking system; and (ii) to facilitate revenue sharing between tiers of government
<b>Correspondent accounts</b>	A separate account is opened for each correspondent. The correspondent entity has real-time information on the balances it maintains in the TSA.

## 7. ECONOMIC ENTITY

The IPSASB definition<sup>10</sup> of a public sector reporting entity is “a government or other public sector organization, program or identifiable activity that prepares general purpose financial reports”. However this definition is not useful if you wish to decide whether an organisation should prepare financial reports.

The GFS is more helpful as set out in the box.

### Box 2: GFS entity definition

An **institutional unit** is an economic entity that is capable, in its own right, of owning assets, incurring liabilities, and engaging in economic activities and in transactions with other entities. Some important features of institutional units follow:

- The ability of an institutional unit to own goods or assets in its own right means that it is also able to exchange the ownership of goods or assets in transactions with other institutional units.
- An institutional unit is able to take economic decisions and engage in economic activities for which it is itself held directly responsible and accountable at law.
- An institutional unit is able to incur liabilities on its own behalf, to take on other obligations or future commitments, and to enter into contracts.
- Either a complete set of accounts, including a balance sheet of assets, liabilities, and net worth, exists for an institutional unit, or it would be possible and meaningful, from both an economic and legal viewpoint, to compile a complete set of accounts if they were to be required.

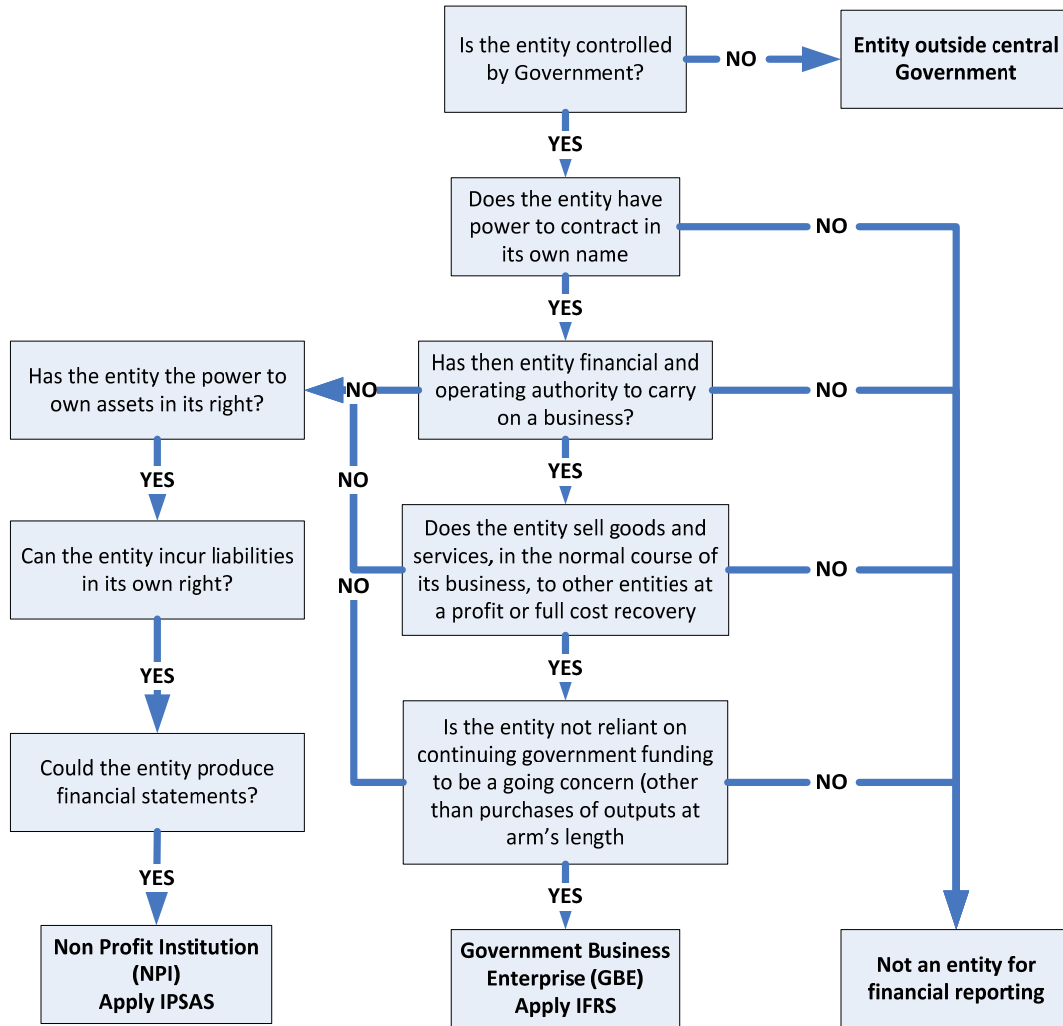
Thus under IPSASB the entity is defined by the production of financial statements. According to GFS an entity has a number of attributes including the ability to produce financial statements. The GFS definition is more useful in identifying entities that should produce financial statements. Thus IPSAS envisage Financial Statements being generated by each entity as well as being consolidated upwards to the whole of government Financial Statements. GFS reports on the other hand are only required for the General Government Sector; ESA95 reports are required for each sovereign entity plus certain regions.

The model below combines the IPSAS decision tree for identifying a Government Business Enterprise with the GFS definition of a Non Profit Institution to identify which entities should produce financial statements under which standards.

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<sup>10</sup> “Conceptual Framework Exposure Draft 1” IPSASB December 2010

**Figure 3: Entity definition**



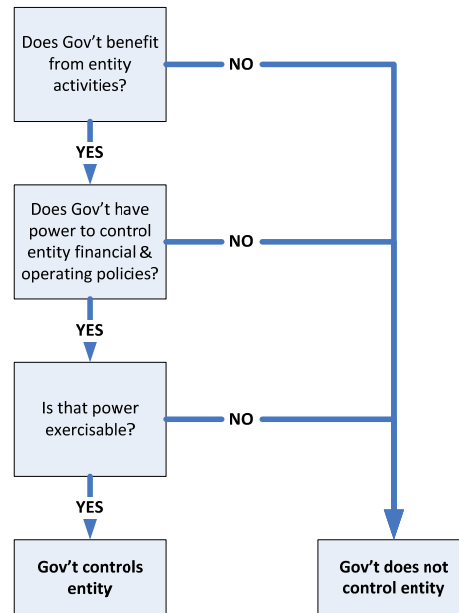
**Whole of government financial reporting**

GFS and ESA95 require the prescribed reports for the General Government Sector (GGS). This is defined in the UNSNA as “consisting of (a) all resident central, state, and local government units, (b) social security funds at each level of government, and (c) nonmarket nonprofit institutions controlled by government units”. Thus the definition is based on administrative units of government.

Note that IPSAS 22 allows consolidated Financial Statements for GGS defined exactly as in the UNSNA. However, the IPSAS 22 reports are in addition to the Financial Statements required on the basis of control (see below).

IPSAS 6 and the Cash Basis IPSAS require consolidation for the whole of government on the basis of control. Control is defined in the model below:

**Figure 4: IPSAS 6 definition of control**

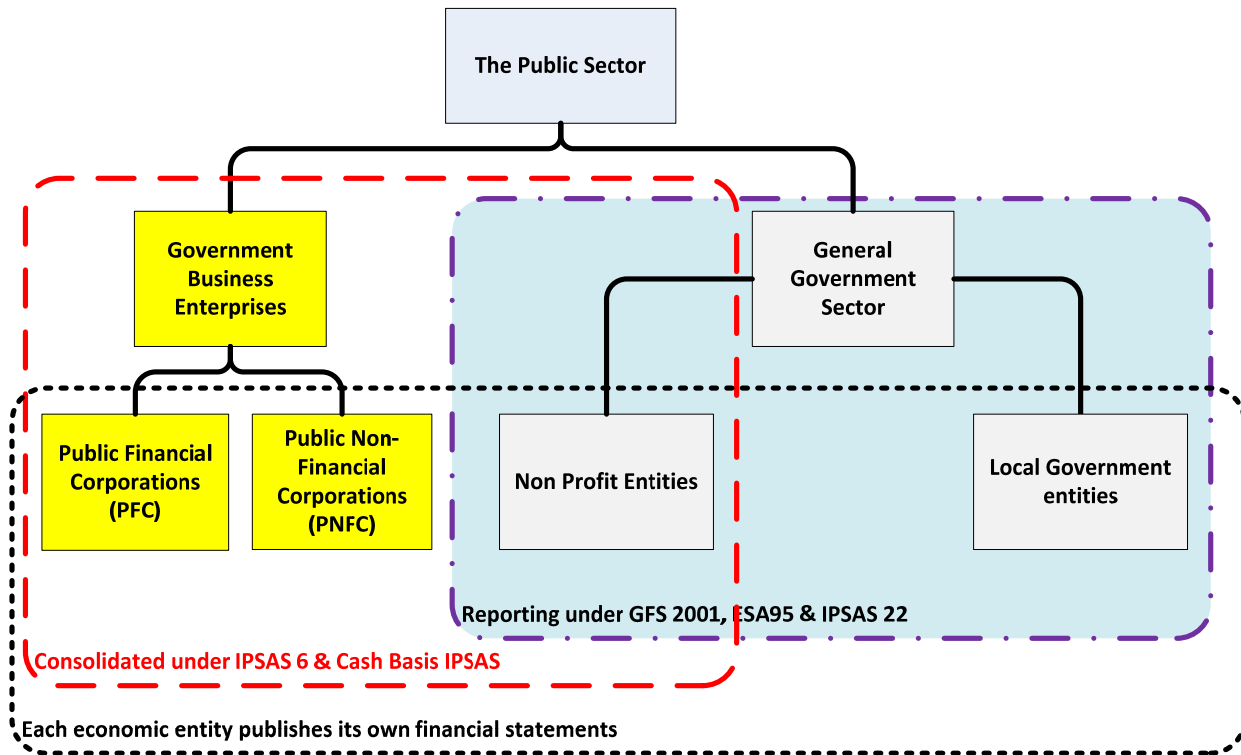


In practice, what this means that consolidated Financial Statements for the whole of Government will usually:

- Include all Ministries, Departments, Extra Budget Funds and Non Profit Institutions under central Government
- Include GBEs - since controlled as defined above
- Exclude local government and Non Profit Institutions under local government - since controlled by locally elected representatives not by central Government.

The differences between the coverage of the GFS, ESA95 and the IPSAS as summarised in the model below.

Figure 5: Government reporting boundaries



Note that under IPSAS 6 (and the Cash Basis IPSAS) consolidation is required of public sector entities with Government Business Enterprises. This creates considerable technical difficulties because of different standards and approaches as between commercial and public sector accounting. If the Government is operating on cash basis accounting then consolidating GBEs operating on a commercial basis with cash based government accounting is extremely difficult and the results of questionable value.

## 8. LIABILITIES AND CONTINGENT LIABILITIES

### Box 3: Definition of liabilities and contingent liabilities (IPSAS)

A **liability** is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.

A **contingent liability** is:

- (a) A possible obligation that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
  - (i) A present obligation that arises from past events, but is not recognized because:
    - (ii) It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or
- (b) The amount of the obligation cannot be measured with sufficient reliability.

These definitions are taken from IPSAS 19. Their meaning is not well understood. Liabilities, provisions, reserves and contingent liabilities are often confused. Note the following points:

- Liabilities are only disclosed in accrual financial statements; under the cash basis liabilities are not recorded
- Contingent liabilities are NOT shown in the balance sheet in accrual financial statements. Nor are they recognised in the double entry accounting system. They are included in the Notes to the Financial statements
- UNSNA, GFS and ESA95 do not include contingent liabilities in their reports.

Hence, for accrual based financial reporting it is critically important to identify actual liabilities as distinct from contingent liabilities and in addition to establish a system for monitoring and reporting contingent liabilities. Although the GFS does not include contingent liabilities, the IMF has recognised their importance as **Fiscal Risk**.

#### *What is included within the definition of liabilities*

Included as liability	Definition
Legal obligations	(a) A contract (through its explicit or implicit terms); (b) Legislation; or (c) Other operation of law
Constructive obligations	(a) By an established pattern of past practice, published policies, or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and (b) As a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

Included as liability	Definition
Provisions	<p>A liability of uncertain timing or amount. A provision shall be recognized when:</p> <p>(a) An entity has a present obligation (legal or constructive) as a result of a past event;</p> <p>(b) It is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; and</p> <p>(c) A reliable estimate can be made of the amount of the obligation.</p> <p>The amount recognized as a provision shall be the best estimate of the expenditure required to settle the present obligation at the reporting date</p>

Note that in accounting terminology there is a distinction between reserves and provisions:

- **Provisions** are as defined above; they are a liability of an entity
- **Reserves** are part of the “Net Equity” of an entity (see the Footnote in the Section of Assets) and are not a liability

### ***Recognising, recoding and managing contingent liabilities***

The term Contingent Liabilities embraces a range of different situations but may be divided into:

- Contingent liabilities that are legally enforceable if and when they arise,
- Contingent liabilities that are not legally enforceable but exist as a matter of practice or expectation – **implicit contingent liabilities**

Examples of legally enforceable contingent liabilities include:

- Pending legal cases against an entity which will result in a penalty if the entity loses the case
- Loan guarantees, e.g. for GBEs, which will be enforceable if the GBE defaults.

Such contingent liabilities are easy to identify. A recoding system needs to be established so that records of all such contingent liabilities can be maintained, estimates made of the likely cost, outcomes recorded and the contingent obligations removed from the records once the outcome is known.

### ***Implicit contingent liabilities***

Implicit contingent liabilities are much harder to recognise – indeed, they may not become apparent until the event arises. The most notable current example has been the contingent liability of governments to support private sector banks. Yet these obligations though unrecognised have been of extreme significance to some countries, e.g. Ireland, Iceland.

Many such implicit contingent liabilities extend beyond PFM to the realm of political decisions. Nevertheless, in establishing a system to manage and record contingent liabilities as far as feasible implicit as well as legal contingent liabilities should be identified and recorded.



## 9. PUBLIC INTERNAL FINANCIAL CONTROL

Public Internal Financial Control (PIFC) is the overall financial control system performed internally by a Government or by its delegated organisations, aiming to ensure that the financial management and control of its national budget spending centres (including foreign funds) complies with the relevant legislation, budget descriptions, the principles of sound financial management, transparency, efficiency, effectiveness and economy. PIFC comprises all measures to control all government income, expenditure, assets and liabilities. It represents the wide sense of internal control. It includes but is not limited to Ex Ante Financial Control (EAFC) and ex-post Internal Audit (IA)

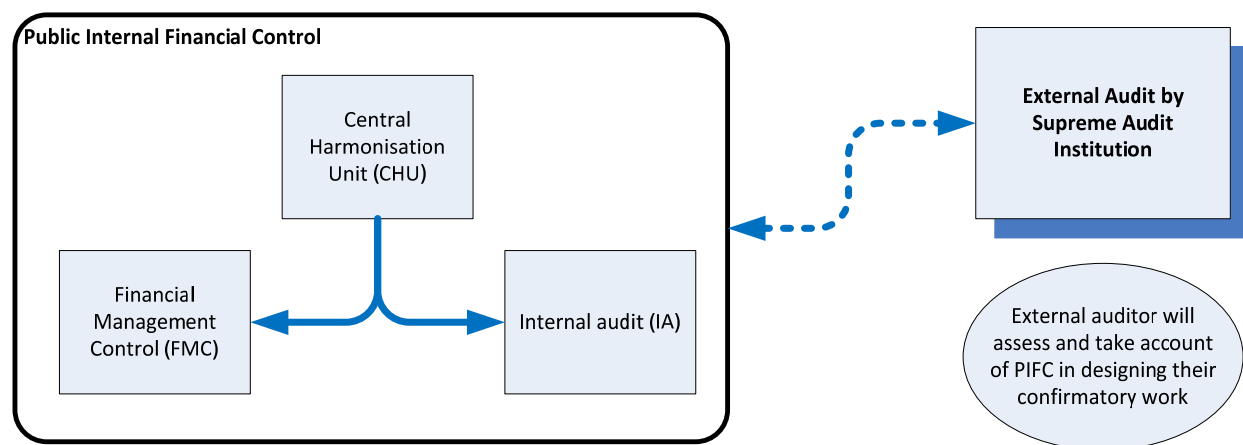
The PIFC model was developed by the European Commission for its own needs and later considered as part of the *Acquis Communautaire* to be transposed into the legal framework of all new EU Member States. The model reflects implicitly the so-called COSO<sup>11</sup> model under which most internal control systems, in both the public and private sector are now being developed. Amongst other things, this model highlights the importance of a two-way (top-down and bottom-up) control system based on the establishment of a sound control environment.

The main international standards for Public Internal Financial Control are the INTOSAI Guidelines for Internal Control in the Public Sector and the EC IIA Position Paper on Internal Audit in Europe. The Association of Internal Auditors issues International Internal Audit Standards

The concept of Public Internal Financial Control is a three-component system that comprises three sets of tools aimed at providing Public Managers with a **Harmonised and Comprehensive System** that enables and promotes **Managerial accountability** and its **subsequent control**.

The components of PIFC and their relationship to external audit are summarised in the model below.

Figure 6: PIFC and external audit



Note the difference between audit and control:

- **Audit** involves investigation and reporting.
- **Control** involves actions (which may be based on audit reports) to manage and correct failures or weaknesses that have been identified.

<sup>11</sup> COSO stands for “Committee Of Sponsoring Organizations » of the Treadway Commission (US, 1985)

### ***Risk management***

The concepts of risk management are the foundation of PIFC. **Risk management** is defined as a process effected by an entity's legislative body, management and other personnel, applied in strategy setting and across the entity, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.

### ***Central harmonisation Unit (CHU)***

It is essential to have in place a central structure – referred to as the Central Harmonisation Unit (CHU) – that is empowered to manage the development of PIFC.

The CHU is responsible for developing and promoting internal control and audit methodologies on the basis of internationally accepted standards and best practice and for co-ordinating the implementation of new legislation on managerial accountability (financial management and control systems) and internal audit. The CHU is best placed in the Ministry of Finance.

In summary the CHU:

- Coordinates activities of PIFC
- Central direction
- Training and technical support to PIFC

### ***Financial Management Control***

Otherwise known as Internal Control may be defined as follows:

#### **Box 4: Internal Control**

A process, affected by an entity's legislative body, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

1. Effectiveness and efficiency of operations
2. Reliability of financial reporting
3. Compliance with applicable laws and regulations

Ex ante financial control (EAFC) is the set of control activities prior to carrying out financial decisions relating to appropriations, commitments, tender procedures, contracts (secondary commitments), and related disbursements and recovery of unduly paid amounts. Such decisions can only be taken after the explicit approval of the ex ante financial controller.

EAFC is sometimes also called "preventive control". This is the narrower meaning of financial control. If described as EAFC there can be no ambiguity.

Each public manager is responsible for establishing and maintaining adequate financial management and control (FMC) systems to carry out the tasks of planning, programming, budgeting, accounting, controlling, reporting, archiving and monitoring.

### ***Internal audit***

The Institute of Internal Auditors definition is as follows:

*Internal audit is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.*

More concretely, it is the functional means by which the managers of an entity receive an assurance from internal sources (including internally subcontracted sources) that the internal controls are achieving their internal control objectives. It will cover, inter alia, Financial Audits, System Based Audits, Performance Audits and IT Audits. It has most of the characteristics of external audit except that it finally reports to the management and therefore can never have the same level of independence as external audit.

## 10. MULTI YEAR BUDGET

The term “Multi Year Budgeting” embraces a range of concepts and different terms. The table below identifies some of the common terminology and the general meaning. Note that there are no absolute definitions, and the same terms are often used with different meanings.

**Table 1: Terminology of multiyear budgeting**

Name	Abbreviation	Usual meaning
Multi year (or medium term) Budget Framework	MTBF	A budget that extends over more than one year, e.g. 3 years
Medium Term Expenditure Framework	MTEF	Usually used to refer to an approach to budgeting that integrates an MTBF with programme and output based budgeting
Medium Term Fiscal Framework	MTFF	A medium term fiscal forecast as the basis of a an MTBF
Programme Budgeting	-	Budgets are built around programmes with specific goals and targets (in contrast to traditional budgeting based on administrative structures)
Output budgeting	-	A budget focussed on delivering outputs (or outcomes) rather than input based budgeting
Input based budgets	-	Budgets where the focus is on the amount spent rather than the outputs to be delivered

Recently many countries have moved to implement an MTEF approach to the budget, using the term in the broad sense described above.

### **MTEF**

A MTEF rests on three pillars:

1. The top-down multi-year projections of resource envelope targets (what is affordable);
2. The bottom-up multi-year cost estimates of sector programs (what has to be financed with a focus on performance);
3. The institutional (politico-administrative) decision making process to integrate the above two pillars (making the necessary trade-offs).

The table below summarises the stages of an MTEF.

**Table 2: The Six Stages of a Comprehensive MTEF**

Stage	Characteristics
Development of Macroeconomic/Fiscal Framework	Macroeconomic model that projects revenues and expenditure in the medium term (multi-year)
Development of Sectoral Programs	Agreement on sector objectives, outputs, and activities Review and development of programs and sub-programs Program cost estimation

Stage	Characteristics
Development of Sectoral Expenditure Frameworks	Analysis of inter- and intra-sectoral trade-offs Consensus-building on strategic resource allocation
Definition of Sector Resource Allocations	Setting medium term sector budget ceilings (cabinet approval)
Preparation of Sectoral Budgets	Medium term sectoral programs based on budget ceilings
Final Political Approval	Presentation of budget estimates to cabinet and parliament for approval

Source: *PEM Handbook* (World Bank, 1998a: 47-51).

The goal of the MTEF approach is to link goals with available resources through a multiyear budget process. The MTEF provides the “linking framework” that allows expenditures to be “driven by policy priorities and disciplined by budget realities” (World Bank, 1998a: 32). If the problem is that policy making, planning, and budgeting are disconnected, then a potential solution is an MTEF. Given that this disconnect between policy making, planning, and budgetary processes is a common condition of country governance, the MTEF has increasingly come to be regarded as a central element of PFM reform programs.

However, a number of recent studies have called into question the extent to which MTEFs achieve their goal. Problems include:

- Lack of linkage between the MTEF and budget processes, so that the MTEF becomes a planning process that is delinked from the actual resource allocation in the budget
- Failure to establish an integrated approach that links the three elements described above so that the MTEF fails in its central goal of linking resources, policies and allocations.
- The MTEF becomes an extension of the budget without any real change in the process of resource allocation.

### ***Budget reporting and IPSAS 24***

IPSAS 24 and the Cash Basis IPSAS both require that the Financial Statements include a report comparing the original and revised budget with the actual outturn. The actual requirements are as set out in the box below.

### **Box 5: Budget Comparison IPSAS 24**

The comparison of budget and actual amounts shall present separately for each level of legislative oversight:

- (a) The original and final budget amounts;
- (b) The actual amounts on a comparable basis; and
- (c) By way of note disclosure, an explanation of material differences between the budget for which the entity is held publicly accountable and actual amounts,

This is a mandatory requirement for all Financial Statements whether on the cash or accrual basis.

The term “comparable basis” means that the figures must be on the same accounting base. Thus, in the budget is cash based and the Financial Statements accrual based, then one of the two sets of figures must be adjusted to a common basis. Normally this will involve modifying the accrual accounting information to show the information on a cash basis. This can present problems for automated accrual accounting systems.

Also note:

- Original budget is the initial approved budget for the budget period
- Final budget is the original budget, adjusted for all reserves, carry-over amounts, transfers, allocations, supplemental appropriations, and other authorized legislative or similar authority, changes applicable to the budget period.