



Public Sector Accounting System - A Conceptual Analysis

Abhishek N.* and Divyashree M. S**

ABSTRACT

Public sector accounting is the system of accounting that involves recording and maintenance of books of accounts by the government authorities on their financial performance. There are three categories of organisations normally working in any environment: public, private and non-profit concerns. Each of these organisations are working on a different motive, for instance private sector organisations run for making more profit for their long-existence, public organisations or governments work for socio-economic sustainable development of the country, where as NGOs are for rendering the services to the society at large. If this is the reality, it is clear that the financial transactions of each of these organisations are different from each other. So it is not possible to record their transactions as per single accounting standard. Hence, it is necessary to have different accounting standards applicable to these organisations individually. Government accounts must be available to the public in a transparent manner. To ensure this, it is necessary to have standards which are applicable to public sector to account for their financial transactions. The present paper is intended to analyse the public sector accounting system at the global level and in Indian.

Keywords: *Public sector accounting; Cash basis; Accrual basis; IPSASs; IGASs.*

1.0 Introduction

Public sector accounting is the system of accounting that involves recording and maintenance of books of accounts by the government authorities on their financial performance. The pivotal characteristics of traditional method of public sector accounting were mainly based on single-entry book-keeping, recording financial events on cash basis. But over the period of time public sector accounting is transformed with

*Corresponding author: UGC-SRF Scholar, Department of Studies in Commerce, University of Mysore, Mysore, Karnataka, India. (Email: abhishekalmighty93@gmail.com)

**Assistant Professor, Government First Grade College, Bilikere, Mysore, Karnataka, India. (Email: divyakala.ms93@gmail.com)

different modern methods of recording and disclosing the financial affairs of the public sectors i.e., accrual system with the help of well accepted accounting standards (García, 2014). The improvement can be done in government financial statements by developing International Public Sector Accounting Standards and which is the international accounting harmonization project undertaken by the International Federation of Accountants (IFAC, 2008) There are three categories of organisations that are normally working in any environment: public, private and non-profit concerns. Each of these organisations are working on a different motive; for instance, private sector organisations runs for making more profit for their long-existence, public organisations or governments work for socio-economic sustainable development of the country, whereas NGOs are for rendering the services to the society at large. If this is the reality it is clear that the financial transactions of each of these organisations are differs from each other. So it is not possible to record their transactions as per single accounting standards so it is necessary to have different accounting standards applicable to these organisations individually. Public sector accounting is the system of accounting which supports the government to record the information about their financial affairs so as help to shape its monetary and fiscal policies. The government accounting system has the following composition:

- Documentary evidence for financial transactions
- Bank accounts through which payments and receipts are handled
- Accounting records such as cash book, ledgers etc.
- Accounting Procedures and controls
- Aggregated accounting data
- Internal accounting reports
- External financial statements
- Staff

Apart from the above mentioned components of government accounting system also have some sub-accounting systems which are:

- General ledger
- Payroll
- Payables
- Receivables
- Assets and liabilities including cash management

1.1 Role of ICAI in harmonizing the public sector accounting

The Institute of Chartered Accountants of India (ICAI) is not only involving in setting accounting standards for private sector but it also involved in setting the accounting standards for government accounting also. It has issued various accounting standards for public sector machineries such as local bodies such as Municipal Corporation and others. while finalizing the accounts of such machineries the accounting authority should verify whether all the guidelines contained in the public sector accounting standards are followed or not.

Nowadays we can observe countries of the world are more or less interdependent and to recognize the government itself at the international level in the financial matters it is necessary to shift from cash basis of accounting to accrual basis of accounting. Accrual basis of accounting will help in recognizing, measuring and disclosing the various financial elements such as assets, liabilities, revenues, Income more objectively. This benefit is realized by the government of India and now it is putting more effort in making its accounting system more advanced so as to meet the global standards. For supporting government's agenda it is necessary to have the support from academicians, researchers and professionals who are more involved in this regard. On the other hand Government accounts must be accountable to the public in a transparent manner. To ensure this there is necessary to have the standards which are applicable to public sector to account their financial transactions so the present paper is intended to analyse the public sector accounting at the global and Indian scenario. The next part of the paper is organized as review of literature, objectives, discussions and conclusions.

2.0 Review of Literature

This section of the paper deals with analysing the existing literature on the current research topic to identify the untouched area in the context of Indian scenario.

Lapsley (1988) analysed various concepts of public sector accounting, including current developments and areas of neglect. The highlighted one important development is the application of current research methodologies in management accounting to the internal accounting of public sector institutions. The study also identified a major area of neglect by public sector accounting researchers are that of the financing of public sector institutions.

Newberry (2015) found that Australia's public finance legislation reinforces the need for public accountability, but through delegated regulatory powers terms such as accountability and public accountability are undergoing subtle reinterpretation. The study observed the main issue is whether IFRS should apply to all governments, and

whether government departments should be viewed as not publicly accountable and therefore permitted reduced disclosures in their published financial reports.

Bracci et al, (2019) analysed the role and impact of accounting within the fragmented field of public value theory literature. The study found that the lack of empirical research and the limited number of papers on accounting for the creation of public value means that accounting scholars need to address 'theoretical stagnation' to achieve a deeper understanding of how to govern the public value creation process.

Jayasinghe et al., (2015) found that the rapid development of public sector accounting, accountability and auditing in emerging economies creates the theoretical and empirical challenges because of the different ways in which public sector reforms and changes are understood and enacted within institutions.

Senarath and Ukwatte (2015) have analysed the reasons why Sri Lanka adopted International Public Sector Accounting Standards (IPSAS) recently. Their study found that the public sector reforms and the shift from cash based accounting to accrual based accounting in the public sector have been strongly affected by the global pressures imposed by international organisations such as International Public Sector Accounting Standards Board and the World Bank . The results of the study shows that the dysfunctional impact of globalisation in the public sector accounting standards as there are major structural issues which are yet to be solved. Further there are increasing dilemmas over whether the move to accrual based accounting is worth the costs and the additional risks involved.

3.0 Research Gap

By the analysis of existing literatures it is found that studies have largely focused on the operational mechanisms of public sector accounting and emphasize that there is need of research for the implementation of accrual system to the public sector. So, the present study is intended to conceptually analyse both cash and accrual basis of public sector accounting in the global and Indian context.

4.0 Objectives

From the analysis of research gap study have framed following objectives:

- To conceptually analyse the cash and accrual based public sector accounting system.
- To examine the International Public Sector Accounting Standards setting process.
- To examine the public sector accounting system in Indian context.

5.0 Methodology

The present study is conceptual in nature and conducted based on secondary data collected through published sources such as newspapers, research articles, websites etc.

5.1 Basis of accounting for public sector

There are mainly two basis of accounting of financial transactions: one is cash basis and another one is accrual basis. It is most advisable to the public sector to follow the accrual basis of accounting. Because on cash basis it is impossible to account for significant liabilities such as pension to employees, loans and assets, property, plants etc., and also it is not possible to follow the prudence principle of accounting. To avoid this problem the IPSASB encourages public sector entities to adopt the accrual basis of accounting. The accrual basis of accounting improves financial management and increase transparency which results in more comprehensive and accurate view of a government financial position.

5.2 Issues involved in accrual based accounting in the public sector

System of both cash accounting and accrual accounting can be seen in the public sector accounting. In the initial stages, the accounting model was considered as most suitable for the public sector. Its main intension is on compliance with rules and regulations. The main issue in cash system of accounting is that it makes little or no information regarding the liabilities that an organisation will be required to meet in the future. Besides this, it does not recognize the benefits which can be obtained from purchased assets over a period of time. More over the financial reports do not give complete information to financial managers and other stakeholders (decision makers). But traditionally, most of the countries still adopt cash accounting to provide periodical balance sheet information.

Accrual accounting is that system of accounting where the transactions are identified as the underlying financial event occurred without considering the time of the related cash receipts and payments. So, in this system revenue recognition is done when income is earned and expenses are recognized when liabilities are incurred or resources are used. In cash system of accounting revenues are considered to be earned and expenditure to be incurred only when cash is received or paid.

Accrual accounting maximizes the public management efficiency and can be achieved with minimal cost for the society.

5.3 Benefits of accrual based accounting

Financial position under accrual system of accounting, the information relating to entities financial position and current assets and liabilities are known through preparation of balance sheet. This required for the public entities to make required decision about the liability of financing the provided services plan for the future funding requirements of asset maintenance and replacement, decide on the repayment of existing liabilities etc., this enables entities to manage cash position and financing requirements efficiently and effectively. More importantly accrual system stresses on financing decisions on net assets or equity which in turns make entities to take a long-term view when making crucial financing decisions.

Financial performance under accrual system of accounting income statement is prepared where complete information regarding revenues and expenses are provided. The income statement aids governments to focus management by results and also management of resources. Information regarding revenues is necessary because to assess the impact of taxation on the government's fiscal position and the requirement of borrowings in the long-term likewise, knowing about expenses is very much necessary because to assess revenue requirements, the sustainability of existing programmes, and the estimated cost of proposed activities and services.

Cash flows cash accounting is not fully neglected in accrual accounting because cash management is an integral part of accrual based accounting and financial management framework. Statement of cash flows is necessary because to identify separately the cash receipts and payments relating to operating, investing and financing activities. The conventional accrual based accounting systems supports cash based accounting and reporting and also tries to provide very comprehensive information on current and certain projected cash inflows and outflows. This helps in efficient cash management and as result aids in preparation of cash budgets effectively.

Reporting and budgeting, the main motto of accrual based reporting is to meet the various needs of wide range of users in making economic decisions by providing that financial information which is understandable, relevant, reliable, accurate, complete and comparable. It widely includes non-cash information which is not possible in cash system of reporting. for instance, re-valuations, write-offs , pension liabilities and consumption of assets through depreciation etc., are some important non-cash transactions which are possible to incorporate in cash system but can find place in accrual system and better can be provided. The financial reports which are produced by entities have to depend on the budget forecasts to show any variances between actual results and the budgeted results. In some cases, the budget becomes more financially important than the financial statements.

5.3.1 Additional benefits

By the analysis of New Zealand's accrual system of accounting following benefits are evidently observed:

- Improved cash management
- Elimination of idle cash balances.
- Better accounting for and management of accounts receivables.
- Better management of assets.
- Ensuring recovery of cost for services provided.

5.4 Disadvantages of accrual based accounting

Accrual system of accounting throws following hurdles to the entities.

- Accrual system involves very high costs related to developing of accounting policies, establishing accounting systems, identifying and valuing existing assets, purchase of software and pilot testing, developing required skills, providing financial information training for preparers and users etc.,
- Accrual system is framed to measure financial performance only which is apt for private sector but sometimes considered as meaningless concept in the public sector.
- In public sector maintenance of public assets is given more importance than providing information on their value.
- No role of finance staffs in budgetary control because they play their role only when cash paid, but non-financial managers and suppliers play their role and decide before cash is paid when invoices are issued.
- The understanding of government accounts prepared as per accrual system of accounting demands greater professional judgement by both the preparers and the auditors of final accounts.
- Compared to accrual system of accounting, cash based accounting more simpler and objective.
- The users of financial reports should have strong ground knowledge about the principle of income, revenue, expenses, assets and liabilities in order to make economic decisions based on the information provided in the reports prepared as per accrual system of accounting.

6.0 Global Context of Public Sector Accounting

In order to strengthen the accounting profession at the global level, International Federation of Accountants (IFAC) was found on October 7, 1997 in Munich, Germany.

The federation provides structure and processes to support the operations of International Public Sector Accounting Standards Board (IPSASB). IPSASB develops accounting standards and guidelines to the public sector entities. The main duties and responsibilities of IPSASB is to develop high-quality standards in auditing and assuring public sector accounting, ethics and education especially for professional accountants and supporting their adoption and use. The overall operations of the IPSASB are facilitated by IFAC. In addition IPSASB also receives institutional support from the following international organisations:

- a) Asian Development Bank
- b) The Chartered Professional Accountants of Canada
- c) The New Zealand External Reporting Board
- d) The Governments of Canada and New Zealand

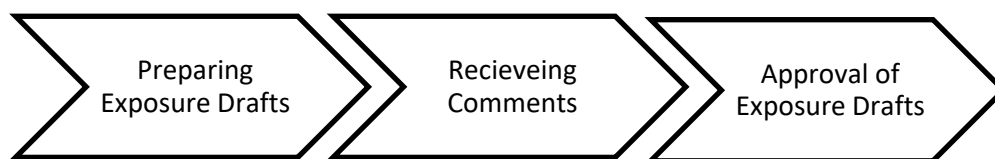
IPSASB works with certain objectives which are for “Strengthening Public financial management and knowledge globally through increasing adoption of accrual-based International Public Sector Accounting Standards” through:

- Developing high-quality public financial reporting standards.
- Developing other publications for the public sector; and raising awareness of the IPSASBs and the benefits of their adoption.

6.1 Process involved in developing IPSASBs

The due process involved in setting IPSASBs is very systematic, well-structured and provides the great opportunity to interested parties like preparers and users to participate in the process and offer their individual views on the standards to be developed. This process is indicated in Figure 1:

Figure 1: International Public Sector Accounting Standards Development Process



Source: Compiled by author

6.1.1 Preparing exposure drafts(ED)

The exposure drafts of IPSASs are developed by task force or by project advisory panel. Exposure drafts are also prepared through consultation paper which examines and explores the subject in detail and provides the basis for further discussion,

development and policy development. For the public opinion regarding ED the board provides open and finite comment periods.

6.1.2 Receiving of comments

The comments made by the public regarding ED are duly received and are publicly made available on the IPSASBs Website. The board re-develops the draft of standards for the further review and comments if changes are made to the ED after analysing and discussing the responses.

6.1.3 Approval of exposure drafts

The approval draft is done by voting mode. To approve the draft at least two-third of IPSASB members approves the exposure drafts, re-exposure drafts and IPSASs.

7.0 Public Sector Accounting System in Indian Scenario

Accounting system of maintenance by government in India is totally based on rules, which means all the financial transactions must be recorded and maintained based on accepted rules. This rule based accounting follows cash basis of accounting. The maintenance of accounting of government is follows the provisions of Government Accounting Rules, 1990, this rules is made under the Article 150 of the Constitution of India. Article 150 emphasizes that the accounting of central and state government must be maintained as per the format given by the president of India in consultation of CAG i.e., Comptroller and Auditor General of India. CAG has set the GASAB that is Government Accounting Standards Advisory Board with the support of Central Government to align the government accounting system with the international emerging trends. The emerging international trends in government accounting are good governance, efficiency and transparency in public spending and fiscal prudence. The main goal of GASAB is that to develop Indian Government Accounting Standards (IGASs) to improve the quality of governmental accounting and reporting to enhance the quality of decision making and public accountability.

GASAB work for the achievement of two independent objectives which are:

- Improving the existing cash basis of accounting.
- To support the government in shifting from cash basis accounting to accrual basis of accounting.

Cash basis accounting standards are developed by GASAB which are popularly known as Indian Government Accounting Standards (IGAS) and standards for accrual

basis are developed under the nomenclature of Indian Government Financial Reporting Standards (IGFRS).

8.0 Government Accounting Standards

The list of IGAS and IGFRS is presented in Table 1. It is necessary for the government to maintain books of accounts under IGFRS i.e accrual accounting basis along with IGAS i.e., cash basis.

Table 1: List of Indian Government Accounting Standards

S. No.	IGAS	IGFRS
1	IGAS-1: Guarantees given by Governments: Disclosure requirements	IGFRS-1: Presentation of Financial Statements
2	IGAS-2: Accounting and Classification of Grant –in- Aid	IGFRS-2: Property, Plant and Equipment
3	IGAS-3: Loans and Advances made by Governments	IGFRS-3: Revenue from Government Exchange Transactions
4	IGAS-09: Government Investments in Equity	IGFRS-4: Inventories
	IGAS-07: Foreign Currency Transactions and Loss or Gain by Exchange rate variations	IGFRS-5: Contingent Liabilities(other than guarantees) and Contingent Assets: Disclosure Requirements
5	IGAS-10: Public Debt and Other Liabilities of Governments: Disclosure Requirements	

Source: GASAB

Apart from this GASAB planned for developing accounting standards on:

- Standard on Chart of Accounts (uniform object head of classification)
- Events after reporting date
- Disclosure of information on General Government Sector
- Presentation of budget information in financial statements
- Transfer of funds from Consolidated Fund of India to Public Deposits
- Suspense and Remittance heads
- Standard on cash balance
- Incomplete capital works

- Accounting for Subsidies in government
- Off-budget borrowing

If government accounting standards are developed in respect of these transactions then Indian government accounting system will be compatible at the international standards.

GASAB also gave chance for academicians, researchers and public for offering their new ideas for improving the present government accounting system. The interested parties can submit their proposal to GASAB.

9.0 Conclusion

India is having multiple government systems. The multiple government system operates in different states in a different manner. They are for under taking socio-economic sustainable welfare activities. To undertake these activities it has earn revenue and spend the same on the society in which it is working. The amount of revenue earned and the amount of revenue spent to the society must be accounted in a systematic manner. For this purpose it is necessary to have some accounting and reporting standards which are compatible at the global standards. The global public sector accounting is totally based on accrual accounting basis which follows prudence principle of accounting. However, in Indian context, governments are accounting more on cash basis. From a few years India has also made the effort to initiate accrual system but it is not yet fully implemented at global standard. So the present study concludes that it is necessary to have commitment from accounting professionals, academicians, researchers to make India's public sector accounting come to a globally acceptable level and to ensure the accountability and transparency in governments' financial events and thereby strengthen fiscal system of the country.

9.1 Limitation and Future Research

The major limitation of the study is that it is in conceptual in nature and it has not analysed the government accounts in an empirical manner. This area, therefore, can become an opportunity for future research.

References

Bracci, E., Papi, L., Bigoni, M., Deidda Gagliardo, E., & Bruns, H. J. (2019). Public value and public sector accounting research: A structured literature review. *Journal of Public Budgeting, Accounting & Financial Management*, 31(1), 103-136.

García, F. M. (2014). Developments and challenges in public sector accounting. *Journal of Public Budgeting, Accounting & Financial Management*, 26(2), 345-366.

International Federation of Accountants. (2008). Handbook. New York, NY.

Lapsley, I. (1988). Research in public sector accounting: An appraisal. *Accounting, Auditing & Accountability Journal*, 1(1), 21-33. Retrieved from <https://doi.org/10.1108/EUM0000000004618>.

Jayasinghe, K., Nath, N. D., & Othman, R. (2015). The public sector accounting, accountability and auditing in emerging economies: Insights, gaps and some new ways forward. In *The Public Sector Accounting, Accountability and Auditing in Emerging Economies*, 15(1), 1-6.

Senarath Y.P., & Ukwatte, S. (2015). The new public financial management (NPFM) and accrual accounting in Sri Lanka. *The Public Sector Accounting, Accountability and Auditing in Emerging Economies*, 15, 7-50. DOI: 10.1108/S1479-356320150000015002

Newberry, S. (2015). Public sector accounting: Shifting concepts of accountability. *Public Money & Management*, 35(5), 371-376. DOI: 10.1080/09540962.2015.1061180.

Weblinks

<https://cpfga.icai.org/wp-content/uploads/2017/11/Government-Accounting-System-in-Developed-and-Developing-Countries.pdf>

<https://www.ipsasb.org/public-sector/about-ipsasb>

<https://www.thehindubusinessline.com/news/education/Government-accounting-%E2%80%94-accrual-is-the-way-to-go/article20657641.ece>