

Chapter 11. REPORTING

A. REPORTING

1. Objectives of reporting¹

Traditionally, reporting was aimed at showing compliance with the budget. While this function is met in countries with a parliamentary tradition and adequate audit capacity, in other countries, improving compliance remains the priority challenge. Nevertheless, transparency and accountability call for wider scope of reporting.

A budget reporting system should provide a means of assessing how well the government is doing. Ideally, therefore it should answer following questions:

- *Budgetary integrity.* Have resources been used in conformity with legal authorizations and mandatory requirements? What is the status of resources and expenditures (uncommitted balances and undisbursed commitments)?
- *Operating performance.* How much do programs cost? How were they financed? What was achieved? What are the liabilities arising from their execution? How has the government managed its assets?
- *Stewardship.* Did the governments financial condition improve or deteriorate? What provision has been made for the future?
- *Systems and control.* Are there systems to ensure effective compliance, proper management of assets and adequate performance?

Reports are an important instrument for planning and policy formulation. For this purpose, they should provide information on ongoing programs and the main objectives of government departments. Reports can also be used for public relations and be a source of facts and figures. They give an organization the opportunity to present a statement of its achievements, and to provide information for a wide variety of purposes.

Reporting must take into account the needs of different groups of users including: (i) the Cabinet, core ministries, line ministries, agencies, and program managers; (ii) the legislature; and (iii) outside the government, individual citizens, the media, corporations, universities, interest groups, investors, and creditors.

According to surveys carried out in several developed countries,² all users need comprehensive and timely information on the budget. The executive branch of government needs periodic information about the status of budgetary resources to ensure efficient budget implementation and to assess the comparative the costs of different programs. Citizens and the legislature need information on costs and performance of programs that affect them or concern their constituency. Financial markets need cashbased information, etc.

2. Principles of reporting³

Reports prepared by the government for internal and external use are governed by the following principles:

- *Completeness.* The measures, in the aggregate, should cover all aspects of the reporting entity's mission.
- *Legitimacy.* Reports should be appropriate for the intended users and consistent in form and content with accepted standards.
- *User friendliness.* Reports should be understandable to reasonably informed and interested users, and should permit information to be captured quickly and communicated easily. They should include explanations and interpretations for legislators and citizens who are not familiar with budgetary jargon and methodological issues. Financial statements can be difficult for nonaccountants; where possible, charts and illustrations should be used to improve readability. Of course, reports should not exclude essential information merely because it is difficult to understand or because some report users choose not to use it.

- *Reliability.* The information presented in the reports should be verifiable and free of bias and faithfully represent what it purports to represent. Reliability does not imply precision or certainty. For certain items, a properly explained estimate provides more meaningful information than no estimate at all (for example, tax expenditures, contingencies, or superannuation liabilities).
- *Relevance.* Information is provided in response to an explicitly recognized need. The traditional function of year-end reports is to allow the legislature to verify budget execution. The broader objectives of financial reporting require that reports take into account the different needs of various users. A frequent criticism of government financial reports is that they are at the same time overloaded and useless.
- *Consistency.* Consistency is required not only internally, but also over time, that is, once an accounting or reporting method is adopted, it should be used for all similar transactions unless there is good cause to change it. If methods or the coverage of reports have changed or if the financial reporting entity has changed, the effect of the change should be shown in the reports.
- *Timeliness.* The passage of time usually diminishes the usefulness of information. A timely estimate may then be more useful than precise information that takes longer to produce. However, the value of timeliness should not preclude compilation and data checking even after the preliminary reports have been published.
- *Comparability.* Financial reporting should help report users make relevant comparisons among similar reporting units, such as comparisons of the costs of specific functions or activities.
- *Usefulness.* Agency reports, to be useful both inside and outside the agency, reports should contribute to an understanding of the current and future activities of the agency, its sources and uses of funds, and the diligence shown in the use of funds.

d. Special and general purpose reports

A distinction between special purpose reports, prepared to meet specific needs, and "general-purpose financial reports, prepared for a large public,⁴ can help to define the presentation and the mode of dissemination of the reports. For example, reports needed to monitor budget implementation are special-purpose reports while financial statements should be considered as general-purpose reports. However, the distinction is partly subjective and depends on the country context. Many governments have special reporting requirements , e.g., environmental reporting (resulting from environmental audits) or retirement fund reporting (for pension policy), and the like. This type of reporting is becoming more frequent as governments face the need to respond to pressures from various interest groups.

3. Budget execution reports

a. Budget implementation management

For managing budget execution the following reports are needed:

- Daily flash reports on cash flows. These reports should distinguish inflows and outflows, but it is better for cash flow forecasting to have a breakdown of expenditure and revenue by broad economic categories (at least weekly).
- Monthly reports on budget execution based on the budget classification system. These reports must specify:
 - Initial appropriation;
 - Revision appropriation (if any);
 - Amount apportioned;
 - Commitments, expenditures at the verification stage, payments, or (at least) arrears and payment;

b. Appropriation Account

In a majority of countries, an annual appropriation report (or budget enforcement report) is generally submitted to the audit office and the legislature. This report is essential, but is insufficient to provide information on fiscal sustainability and performance and should be only one element of the reporting system. In many developing countries, the production and the publication of the annual report takes at least a year, making it useless for external users. Moreover, taking into account time needed to audit these accounts, preliminary information on budget execution must be available and published no later than two months after the end of the budget period.

4. Financial reporting

Financial Statements, as currently defined, fit better an accrual accounting system than a cash accounting system. However, regardless of the accounting system, certain minimum reporting requirements should be met in any country. Sample tables for each of the reports discussed below are shown in annex X.

a. Minimum financial reporting requirements

Whatever the accounting system, the objective should be to produce the following reports, and therefore to keep appropriate accounting books or ancillary registers:

1. *Consolidated accounts.* The government should publish an analytical report on consolidated financial operations of the government. This report should be prepared in accordance with GFS standards, complemented with accrual information for debt, information on expenditures at the verification stage, and information on arrears. This report consists of three tables showing the government financial operations for (i) central government; (ii) local governments; and (iii) general government. Financial information for “funds” should be consolidated into the accounts of the relevant level of government. The report should cover at least two fiscal years to allow comparisons. Box 33 shows the main elements to be included in the government consolidated accounts.

Box 33
Elements to be Included in the Government Consolidated Account

Cash basis

Revenues, broken down into broad categories;

Grants, including grants-in-kind and debt remission;

- Non interest expenditures;
- Interest;
- Capital expenditure broken down by financing source (i.e., domestic, project loans and grants);
- Lending minus repayment. preferably to divided between gross lending, repayments, no sales of assets, rather than shown as net lending;
- Deficit on a cash basis;
- External financing (project loans, other loans, amortization, debt rescheduling);
- Domestic financing (central banks, commercial banks, nonbank lending)

Commitment basis

- Wages and salaries;
- Other goods and services, preferably at the verification stage;
- Capital expenditures, preferably at the verification stage;
- Interest on an accrual basis;
- Deficit on a commitment basis;
- Flows of arrears (domestic and external), including any undelivered orders on a separate line;
- Adjustment for project loans (drawings less expenditures).

Either in the tables or as a memo item to show, when practical:

- Breakdown of expenditure between true capital expenditures and current expenditures;
- Breakdown of expenditures between the recurrent budget, the capital budget, and funds.

Some developing countries do not prepare the consolidated accounts of the government on a consistent accounting basis. When preparing a financial program with the IMF, they gather data from budget monitoring reports, from the central bank, extra budgetary information, etc. Outflows and inflows estimated in such a manner cannot be balanced. As a result, the consolidated accounts show a gap, which is often hidden under the catch-all heading of arrears.

This information should be derived from the government accounts. When extra-accounting elements are introduced in the consolidated table, they should follow a double-entry procedure should be followed. For example, if arrears for utility consumption are estimated from data not recorded in the government accounts, they should be posted both as expenditure and as arrears.

2. *Statement on stock and flows of domestic arrears.* This report separates arrears to the private sector from arrears, to subnational government entities and to the non government public sector.
3. *Summary report on the execution of the government expenditure program.* This report covers expenditure from the budget and funds by broad function and programs (if any). It should distinguish between current and capital expenditures, show previous years for comparison, and give estimates for the following year if the country prepares multi year estimates. The report should cover at least two fiscal years to allow the user to make comparisons. It should include a narrative statement on government expenditure policy.

A consolidated report should be prepared for (i) the central government; (ii) local governments; and (iii) the general government. All tables or memo items required for comparison with the annual budget report and other reports (e.g., local government execution budget and funds reports) should be annexed to this report.

In a country with an arrears problem, this summary statement should be produced for both cash payments and expenditures at the verification stage.

4. *Report on medium-term external debt.* The report on the medium-term external debt should include the following statements:
- * Debt outstanding and disbursed (DOD) for medium-term external public debt, classified into the following categories:
 - DOD without arrears, with interest arrears, and with principal arrears;
 - Directly contracted debt and guarantees;
 - Broad categories of creditors (e.g., Multilateral Institutions; Commercial Creditors);
 - Broad categories of beneficiaries of guarantees (e.g., industrial state enterprises; agricultural enterprises);
 - Debt instruments (loans and other obligations).
 - * Objections of public debt service for the next five to ten years, distinguishing:
 - Directly contracted debt, and guaranteed debt, by broad category of creditor;
 - Projections on both an accrual basis and cash basis for partly rescheduled debt;
 - New borrowings;
 - Rescheduling over the period.
5. *Report on short-term borrowing.* The format of this report depends on the level of development of the financial markets in the country. Depending on the composition of its debt and on the organizational arrangements within the country, the report can be consolidated with the report on medium-term debt or prepared separately.
6. *Report on grants.* This report should show donor pledges, disbursements (from the donor's point of view), and estimated of receipts (see discussion below).
7. *Report on lending and on-lending.* This report shows loans contracted, interest and principal payments over the period, and stock and flows of arrears by major

category of beneficiary. It should include a narrative on any problems met in collecting payments from debtors, and assessment of future risks.

8. *Statement on forward commitments.* In fulfillment of accountability to the legislature, the report on forward (multi year) commitments should show forward commitments and the projected payment schedule by function/program and line ministry/agency.
9. *Statement of cash flows.* Like a normal commercial bank monthly statement, this statement shows flows of cash revenues and cash payments, and opening and closing cash balances. It covers all government cash and bank accounts, and is normally produced directly from government accounts.
10. *Statement of tax expenditures.* It is desirable to give estimates on tax expenditures by sector/function and type of tax concession.
11. *Statement of other liabilities and other contingent liabilities.* If possible, in addition to the debt reports, this statement could be prepared to show other liabilities and contingencies, such as pension liabilities, insurance contingencies.
12. *Statements on physical assets and investments for selected sectors/programs.* For the infrastructure sector, it can be useful to produce statements showing the most significant assets, the investment made on an accrual basis (i.e., the increase in physical assets which can be very different from expenditures), and maintenance, including deferred maintenance. This statement can be included in the report on development expenditures mentioned in section 6 below. Generally, other statements of assets concern the internal management of the agencies or are inputs to the preparation of performance indicators.

b. Financial statements under an accrual accounting system⁵

Accrual accounting systems allow the preparation statements that give a much more complete view of the financial situation of the government, and a consistent and comprehensive framework for preparing the reports mentioned in the previous section.

Moreover, financial reports prepared by ministries and agencies on the basis of full accrual accounting can be used in assessing their performance.

An accrual accounting system commonly entails the preparation of the following financial statements:

- *Financial position statement (or balance sheet)*. The statement of financial position includes details of all recognized assets and liabilities. The balance of assets less liabilities is the net worth.
- *Financial performance statement (or Operating statement)*. Under full accrual accounting the statement of financial performance includes details of all recognized revenues and expenses, and the operating deficit. To avoid confusion, it is essential that the deficit on an accrual basis be compared to the deficit on a cash or commitment basis. Adequate caution must be given to the report users on this crucial issue to avoid giving a misleading assessment of the macroeconomic situation.
- *Statements of movements in net worth*. This statement links the statement of financial performance to the statement of financial position and explains movements in the opening and closing balances.
- *Statement of cash flows* (see discussion in A.4.a).

Notes to the financial statements should provide as much detail as needed to interpret the statements correctly and also a statement of accounting policies

These statements must be complemented with the reports mentioned in paragraph E.4.a above for the fields that they cannot cover or do not detail sufficiently (e.g., commitment, contingencies, tax expenditures, details on debt and borrowing).

d. *Coverage of financial reports within the government*⁶

Financial reports should cover all government entities. Fund accounting poses a problem in many countries. As explained in chapter 2, these funds include both independent funds and special accounts managed by the Ministry of Finance or the Treasury. When fund accounting is not consolidated line by line, the revenues and expenditures of the government are inflated by transactions between funds, which constitute instead a mere transfer within the government sector. Moreover, under accrual accounting, when revenues attributed to a fund are greater than its expenditure, the excess revenue is included as a liability on the government's books, while any excess of deficiency of expenditure appears as an asset⁷. When, these funds, in the aggregate, have significant financial imbalances, the financial position of the government can be seriously distorted.

Whether extrabudgetary funds are or are not justified in a particular country, there is no reason to exempt them from the accounting and reporting obligations to which all other government entities are subject. All funds and accounts of all entities of the government must be consolidated. To make this consolidation possible, the chart of accounts of government entities and the economic and functional classification of their budget must fit a common set of accounts and classification determined at the central level (the general ledger discussed earlier).

Good financial reporting is required for accountability. However, the allocation of resources is made through the budget process, and implementing a sound financial reporting system for existing extrabudgetary funds will in no way strengthens the case for their retention.

e. *Nongovernment public entities*

While the scope of the budget is limited to the government, as defined in chapter 2, a broader scope should be considered for financial reporting. Entities controlled or owned by the government should produce regular financial reports. The accounts of entities carrying out business activities should be on a full accrual basis, and their financial statements should be those required under accrual accounting. These accounts

should be consolidated by the government and published. Such information is needed by the public and for policy making, notably subsidies, the financing capital expenditures of public enterprises, on-lending, etc.

Some countries have adopted the concept of “the government financial reporting entity,”⁸ i.e., the set of entities, transactions, and activities for which the government is accountable and that are to be covered by government financial reports. Criteria for defining the boundaries of the entity are financing, ownership and control. Control is the criterion that is more consistent with the objective of financial reporting, since government should be accountable for the resources and entities it controls, regardless of government financing or degree of ownership. However, this criterion requires a greater element of subjective judgment.

Rules for identifying the government entities that must produce financial statements are established either via legislation (as in Bangladesh, Taiwan, France, and Italy) or through accounting principles, such as the notion of control and the existence of users for which the information will be useful (as in Australia and New Zealand).

5. Departmental reports⁹

Departmental reports show the activities of line ministries and government spending agencies, and give important information for deciding the intersectoral allocation of resources. If they are available before the start of budget preparation (which is desirable), they can be useful in preparing the initial budget ceilings. In some countries, these reports are discussed in legislative committees and made public.

There is no standard presentation for a departmental report. Ideally, it should include the following elements:

- Major issues in the sector;
- Goals of the department and policies to meet them;
- Programs and activities of the department;
- Fiscal performance and financial statements;
- Estimated expenditures in future years;

- Performance indicators;
- Other relevant information, e.g., tax expenditures in the sector.

6. Development/Investment expenditures reports

The system of reporting on investment expenditures depends on the organizational arrangements. In any event, the presentation of investment expenditures in a unified report or as an identifiable part of a departmental report is systematically required in aid-dependent countries and generally desirable in other countries. Reports on development/investment expenditures should show, by program/project:

- Actual expenditures at the verification stage (not only the cash payments) during the fiscal year ;
- Actual expenditures of the previous fiscal year;
- Estimate costs of ongoing programs/projects for the three or four assignment years.

In a small country, investment expenditures are presented by project. In a large country, this report should be presented by program. However, ongoing projects of national importance and significant size should be identified. For each project, the report should indicate: (i) annual projected costs over a period of three to four years; (ii) total costs; and (iii) the balance required to complete the project after the three or four year period.

In addition, accrual-based information on the progress of projects is important, especially in transport, communication, energy and public works, where payment schedules do not necessarily coincide with physical implementation. For large infrastructure projects, the increase in asset value can be presented, along with the indicators of physical progress. For programs, performance indicators can be measured as well, particularly in the social and agriculture sectors. (issues related to performance measurement are discussed in chapter 15.)

Information on projects financed with external loans should be presented at the verification stage. Information on financing presented in the government account is

based on disbursements. No matter how efficient the system of data collection within the country, there is always a time-lag between drawings from loans and verified expenditures, and the length of the time-lag depends largely on the procedures of the lender. Because the difference between drawings and expenditures may be large, these data must be compared the difference and explained. Drawings and expenditures made from special funds must also be required.

In principle, grants-in-kind should be reported at the time when these are received. Discrepancies with information from donors should be identified and explained. In practice, however, many aid-dependent countries rely on information from donors to estimate expenditures financed grants-in-kind. This often leads to mixing cash-based information from some donors with commitments or “pledges” from other donors. A better monitoring of grants is needed in most aid-dependent countries. Except when special disbursement procedures have been established, this monitoring should be done at the project level, the only level where expenditures financed with grants can be reliably estimated. Even then, data from donors must be collected and compared with the data from the projects.

B. MAIN ISSUES AND DIRECTIONS IN REFORMS

1. Main Issues

a. Accounting systems

Accounting and reporting systems are crucial for budget management, accountability, and policy decision making.

For financial reporting, accounting systems are classified into the following categories:

- Cash accounting, which focuses on cash flows and cash balances. Provided that it is supplemented that it is complemented by an adequate system for recording commitments and reporting on arrears, cash accounting can fit expenditure control needs.

- Modified cash accounting, which includes a complementary period for recognizing end-of-year payments.
- Modified accrual accounting, which covers liabilities and financial assets. Modified accrual accounting gives a complete framework for registering liabilities and expenditures;
- Full accrual accounting, which is similar to the accounting systems of commercial enterprises. Accrual accounting gives an appropriate framework for assessing full costs and performance and also for registering all assets and liabilities. However, it has tough implementation requirements.

a. *Accounting: Minimum Requirements*

Whatever the basis of accounting, the accounting system should have the following features :

- Adequate bookkeeping procedure, systematic recording of transactions, adequate security, and systematic comparison with banking statements;
- Recording of all expenditure and revenue transactions in the accounts, according to the same methodology, including, notably, expenditures from funds and autonomous agencies, and foreign financed aid (see chapter 3);
- A common set of classifications for expenditure into functional and economic categories (see chapter 2);
- Clear and well-documented accounting procedures;
- Regularly produced statements (see section on reporting below);
- System for tracking the use of appropriations (budgetary accounting, at each stage of the expenditure cycle (commitment, verification, payment));

- Clear procedures and full disclosure of operations made below the line or through liability accounts.

b. Reporting System

The reporting system must be designed to fit the needs of the different report users (the public, budget managers, policy decision makers, etc.). Minimum reporting requirements include:

- Budget management reports showing all movements in appropriations and line items (allotments, supplementary estimates, virements, etc.);
- Accountability reports to the legislature,
- Financial reports: consolidated accounts of the general government, statement of arrears, report on debt and contingent liabilities, and report on lending;
- Reports assessing budget policy, and
- Departmental reports.

2. Accounting and reporting improvements

a. Immediate actions

In a majority of developing countries, it is necessary first to focus on the following:

- Implementing a commitment register and an ancillary book for outstanding payments, countries that monitor only payments and more generally, implementing a comprehensive budgetary accounting system and register

expenditure at each stage of the expenditure cycle. Budget execution reports must show expenditures at each stage of the expenditure cycle.

- Developing a dept accrual accounting system if none exists, and preparing comprehensive reports on debt.
- Consolidating fund operations (if any) and ensuring that all government entities submit reports based on the same set of classification must be set up.
- Recording contingent liabilities, and preparing and publishing statements of these liabilities.

b. Further improvements

Further steps should include:

- Implementing of a modified accrual accounting system, to have a comprehensive framework for reporting on liabilities, and systematic recording of contingent liabilities.
- Publishing financial statements.
- Implementing asset registers, at least for the categories of assets that need to be carefully monitored.

Box 34**Canada's Awards for Excellence in Annual Reporting by Public Corporations**

In 1993, the Auditor General of Canada announced a five-year award program for Excellence in Annual Reporting by Crown Corporations. The award is intended to recognize corporations that have prepared exemplary annual reports as accountability documents and to encourage and guide Crown corporations in improving corporate reporting. It is a response to the growing recognition throughout the public and private sectors, in Canada and elsewhere, of the importance of more information on corporate performance in enhancing accountability. Improved performance reporting is especially important in the case of state enterprises wholly-owned by Crown corporations because they deliver a mix of public policy and commercial objectives.

In times of fiscal restraint and deficits, performance reporting becomes even more important. Information on financial results alone does not adequately address the full range of stakeholders' interests and information requirements. While Crown corporations are distinct legal entities, they are accountable to Parliament through the responsible minister. More attention needs to be given to providing more comparable and consistent information on parliamentary funding. The establishment of annual award for Crown corporations will encourage greater accountability to Parliament among these corporations through improved reporting.

The Auditor General Awards for Excellence in Annual Reporting by Crown Corporations are given on the basis of four main factors: excellence in reporting both financial and operational performance; provision of clear, relevant, and meaningful objectives that can serve as indicators for measurement and reporting; emphasis on the corporate environment and the risks inherent in operations; and discussion of future directions and plans.

An assessment was carried out during the year to determine whether the award program had a positive impact on the corporations' performance reporting and whether it would be worthwhile to continue the program. The corporate plan summaries and annual reports of a number of Crown corporations for years 1 and 4 were compared to determine whether the reporting had improved and Crown corporations were consulted to determine whether the program had a positive impact on their performance. Almost 80 percent of the corporations in the sample were found to have improved their reporting performance.

A majority of the respondents in the survey likewise believed that the program should be extended and expanded to include other agencies, corporations, and departments. The award program has developed in these corporations a sense of pride, and a competitive spirit, and has focused more attention on the quality of reporting. One respondent commented, "Although we were fortunate enough to win the award in 1994 to 95, this has not stopped us from continuing our efforts each year to improve and hopefully, to win again."

Source: William Radburn

c. *Accrual accounting*

If (and only if) the previous actions has been implemented, the government can consider implementing a full accrual accounting system and a financial reporting system based on accrual accounting. Taking into account their implementation requirements, the systems could be implemented gradually, beginning with agencies with a greater need for full cost assessments. Cost measurement systems must be developed for this purpose.

¹ Drawn from Office of Management and Budget, Objectives of Federal Financial Reporting Statement of Federal Financial Accounting Concepts, Statements no. 1 and no. 2, 1993; and Liekerman, What are the Rules for Financial Reporting?" in D. Henley & Liekerman, et al., "Public accounting and financial control, Chapman and Hall, 1993.

² For more detailed survey results see Premchand, 1993.

³ Drawn from Premchand, OMB; and Liekerman, op. cit.

⁴ See, for example OMB, op. cit.

⁵ See PSC of IFAC, "Financial Reporting"; and Premchand, op. Cit.

⁶ The term government in this paragraph refers to any government authority which can be the central government or a local government.

⁷ IFAC "From cash to accrual: the Canadian experience in *Perspectives on accrual accounting*,

⁸ See "The government financial reporting entity", IFAC.

⁹ See Premchand and Liekerman, op. cit.