

****Please note that this is an early early/first stage draft.***



The accounting of projects by implementing agencies under IPSAS
Challenges and Insights

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5/13/2011

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1 Introduction

Several public sector entities across the globe are in the process of transitioning to either cash based or accrual based IPSAS. Our focus in this paper is on the implementation challenges arising from, possible ‘grey areas’ in the accrual based IPSAS for dealing with the appropriate accounting treatment of projects carried out on behalf of clients, donors and beneficiaries (figure 1 illustrates various stakeholder relations extant in the case studies drawn upon in this study). The key challenges the public sector entities are facing is to account for projects they implement for or on behalf of beneficiaries, based on transfers done by donor agencies and/or clients.

The drive for accrual based accounting in the public sector has been ongoing for nearly two decades. The implementation of IPSAS (or other authoritative and recognized accounting standards) is often seen as an integral part of public sector entities’ quest to strengthen governance.¹ The convergence to accrual accounting within the public sector is often understood within the broader context of wanting to strengthen efficiency and thus New Public Management (NPM). United Nations Educational, Scientific and Cultural Organization (UNESCO) has in the context of their implementation of IPSAS emphasized that since public entities “manage public funds, these organizations have to operate with demonstrable integrity and professionalism (see Aggestam, 2010). By providing a more uniform, transparent and commonly accepted standard, IPSAS helps public entities to meet this requirement” (UNESCO, 2008, p.1). Nevertheless, despite numerous governments and other public sector entities embracing accrual accounting, a number of studies have criticized such reforms of accounting systems in the public sector.

It is well recognized that there are numerous challenges involved in the implementation of accrual based IPSAS and it is also acknowledged that the literature debates the whether accrual accounting is really an appropriate accounting method in the public sector. The focus of this paper though is that of looking at the accounting specific questions that arise when accounting under accrual based IPSAS for public sector entities that implement projects on behalf of donors/clients.

Questions most commonly are:

- Do the project funds which have been transferred by the donor agencies have to be recognized or disclosed, if so under what basis?
- Will the accounting treatment be different if the funds are transferred to an account of the implementing agency versus an account under the name of the beneficiary, if so what are the differences?
- Under what circumstances do the assets acquired, constructed and managed by the implementing agency have to be recognized or disclosed by the implementing agency?
- Is the funding of the project and the risk and rewards associated by the projects managed by the implementing agency relevant for the accounting treatment under IPSAS?

¹ IFAC Study 13 on ‘Governance in the Public Sector: A Governing Body Perspective’ highlights the need for good governance in the public sector (IFAC, 2001). Study 13 draws on the empirical research by Kaufman et al. (1999) pointing to extant evidence on the strong causal relationship between good governance and better development outcomes (p.1).

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- What other issues from a management or accounting perspective are relevant to be considered when managing projects on behalf of a beneficiary.
- How do these transactions have to be classified: as transfers, exchange or non-exchange transactions? And what are the common accounting challenges facing implementing agencies classifying the transactions?

In this paper the accounting issues of several implementing agencies will be highlighted and discussed.

Based on different identified revenue streams and operating activities the accounting issues will be listed and a discussion on accounting solutions which are IPSAS-compliant will be given. **Through this analysis the paper argues that there are grey areas in the IPSAS pertaining to accounting for projects.** [check?]

2 International Public Sector Accounting Standards

The mission of the International Federation of Accountants (IFAC) is *'to serve the public interest, strengthen the accountancy profession worldwide and contribute to the development of strong international economies by establishing and promoting adherence to high-quality professional standards, furthering the international convergence of such standards, and speaking out on public interest issues where the profession's expertise is most relevant'*. The IFAC, in pursuing its mission, established the International Public Sector Accounting Standards Board (IPSASB).

The IPSASB is formed to develop and issue under its own authority the International Public Sector Accounting Standards (IPSASs). The objectives of the IPSASB are *'to serve the public interest by developing high quality public sector financial reporting standards and by facilitating the convergence of international and national standards, thereby enhancing the quality and uniformity of financial reporting throughout the world.'*

The IPSASB develops IPSASs which apply to the accrual basis of accounting and IPSASs which apply to the cash basis of accounting.

Interestingly, the IPSASB revised its cash-basis standard (Financial Reporting under the Cash Basis of Accounting') with supplemental information regarding Recipients of External Assistance.

2.1 Multilateral Organizations

The Development Assistance Committee (DAC) of the Organization for Economic Cooperation and Development (OECD) has recognized aid groupings to enable assessments of national contributions to development. Funding to multilateral institutions for use in specific countries or for specific purposes is classified as 'bilateral aid'. Funds are classified as 'multilateral aid' where the individual donor does not control the use or disbursement of pooled funds. Multilateral aid is de facto undertaken by multilateral

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organizations, however they can also undertake bilateral aid, e.g. if a government directly transfers funds to the multilateral entity.

A multilateral organization is usually established by intergovernmental agreement and are independent of the interests of any single country member or recipient government. Multilaterals have a strong comparative advantage in realizing their universal objectives, because of the global reach of their operations, unique legitimacy, breadth and depth knowledge and expertise.

Multilateral organizations have typically their own policies and have their own governance arrangements. Individual members, governments, have rights (such as voting power) and duties (such as to contribute), but only alongside all other members. Priorities between members may be different based on characteristics (such as population figure and GDP) or contributions of the member countries.

In its reports, the National Audit Office of the United Kingdom concluded: *‘Whilst multilateral aid figures derived using DAC definitions are necessary for international reporting purposes, the lack of readily available information on total funding to each multilateral raises accountability and management issues. It means DFID’s total funding to individual multilaterals is not visible to taxpayers and other interested parties. It also means DFID may not exploit the full power of its total contribution to each multilateral. And funding decisions may not be set in the context of DFID’s overall portfolio, and as a result are often considered in a piecemeal way.’*

Based on its research the National Audit Office came with the following recommendations regarding accountability by multilateral organizations and recommendations for the funding government¹:

- Increase the focus of monitoring and evaluation on development results and push multilaterals that score weakly in this area to improve.
- Require managing teams to produce monitoring reports, or ensure that the multilaterals’ own monitoring systems can provide the government with the evidence from which progress against objectives can be monitored.
- Government managing teams should monitor and evaluate their own performance in the partnership.
- Make payments only when the multilateral has demonstrated progress and the need for more funds.

The Public Sector Committee of IFAC, predecessor of the IPSAS Board formulated in its Study Report 13ⁱⁱ one of the following conclusions: *‘Governing bodies of public sector entities need to publish on a timely basis an annual report (including financial statements), presenting an objective, balanced and understandable account and assessment of the entity’s activities and achievements, and of its financial position and performance and performance prospects.’*

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2.2 The dilemma

To us the following is key to the dilemma of our paper: How to account for multilateral aid by the reporting to all stakeholders, in a transparent and unbiased way?

Based on the issue of accountability and transparency required by stakeholders of a reporting multilateral entity, we will try to answer the following questions:

- Do the project funds which have been transferred by the donor agencies have to be recognized or disclosed, if so under what basis ?
- Will the accounting treatment be different if the funds are transferred to an account of the implementing agency versus an account under the name of the beneficiary, if so what are the differences ?
- Under what circumstances do the assets acquired, constructed and managed by the implementing agency have to be recognized or disclosed by the implementing agency?
- Is the funding of the project and the risk and rewards associated by the projects managed by the implementing agency relevant for the accounting treatment under IPSAS?
- What other issues from a management or accounting perspective are relevant to be considered when managing projects on behalf of a beneficiary.
- How do these transactions have to be classified: as transfers, exchange or non-exchange transactions? And what are the common accounting challenges facing implementing agencies classifying the transactions?

3 Relevant literature

Whilst the literature and the standard setting work through the IPSASB has recognized that accounting for Public-Private Partnerships (PPPs) has entailed grey areas – not much work has been addressed to discuss best practices for accounting for fee earning projects between public sector entities (public-to-public partnerships).

4 Method

Case studies to examine why and how [x] number of organizations have dealt with arriving at accounting decisions for accounting for projects.

The paper the examines the accounting solutions to arrive at a conclusion on the appropriateness of such solutions.

4.1 Case descriptions

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4.1.1 Case Organisation 1.

Business model: Renders services for public sector and private sector clients. The services entails construction work (i.e. construction roads in Afghanistan). The majority of construction work is done through sub-contracting, but there are cases where the public sector service provider is the sole provider of the construction work. In addition to construction work the organization renders non-construction services, an example is running election programmes.

Determination of type of revenue: Exchange vs. Non-exchange

Construction contracts

Treatment of PPE

Accounting challenges and analysis

- Intro. To structure of analysis
- Revenue:
 - o Exchange vs. non exchange
 - o Net vs. gross (agent – principal)
 - o Identifying critical revenue streams
 - Construction contracts
 - Rendering of services
 - Procurement of goods
- PPE?
- Links between revenue and PPE
- Cash?
- Other?
- Summarized analysis

4.1.2 Case organization 2.

4.1.3 Case organization 3.

5 Analysis

- Refer to powerpoint presentation
- Agent versus Principal: IFRS VS IPSAS guidance

6 Conclusions

Accountability information provided by multilateral organizations will in our opinion add to the cost effectiveness and efficiency on aid funds transferred and results achieved, as per defined goals.

- Will combine literature review and accounting analysis...

The IPSAS Board should develop more guidance and in our opinion a separate standard on donor reporting. This new IPSAS would cover the specific issues related to donor reporting. Apart from financial information, also sufficient attention would be required on non-financial information. To date, the minimum requirements of disclosure of non-financial information is limited in the IPSASs.

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Literature

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Websites

<http://www.ifac.org/PublicSector>

Notes

ⁱ Department of International Development, (2005), *Engaging with multilaterals*, National Audit Office., page 19.
ⁱⁱ International Federation of Accountants (IFAC), Public Sector Committee, *Governance in the Public Sector: A Governing Body Perspective – International Public Sector Study 13*, August 2001, ISBN 1-887464-68-9, page 18.

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Figure 1 Funding relations and operations of an agency 6