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PUBLIC SECTOR ACCOUNTING

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CHAPTER 1
APPROACHES TO PUBLIC SECTOR ACCOUNTING AND REPORTING IN EUROPE

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SUMMARY

This chapter aims to provide both a context and a foundation for the book. Thereby it introduces important terms used throughout the module and differentiation of contents. By deriving a roadmap, it serves as a guidance through the different chapters and points out connections between lectures and the overall structure of the textbook.

After reading this chapter, readers will know about the relevance of public sector accounting as a field of study, the current public sector accounting developments in the EU, the reasons for differences in public sector accounting between countries and the key terms used in public sector accounting.

KEYWORDS

Public sector reporting, accounting concepts, harmonization, EPSAS

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1. Introduction and background

Public sector accounting (PSA) and reporting internationally have undergone severe reforms during the last decades.[1] Within these reforms there has been the change from cash to accrual accounting.[2] However, the extent of reforms and thereby also the implementation of accounting systems and norms, differs considerably between governments on an international scale. This is a problem particularly striking for the European Union (EU), as the European Commission (EC) needs to rely on statistical data about e.g. financial debt of its member states. For these statistics, the reference is the European System of National and Regional Accounts (ESA), which is accrual-based and uses double entry bookkeeping. However, the accounting systems in the member states range from pure cash-based systems, combinations of cash- and accrual-based accounting, modified accrual accounting to accrual accounting.[3] In addition, the accounting systems even differ between the different levels of government within one country. Thus, there is a risk of inconsistent data being reported to the EC.

There are various reasons for the differences in PSA and reporting norms across countries.[4] Firstly, countries differ in their legal and juridical system. This refers for example to the extent of power that central governments have. In some countries, like Germany, the central government is not legally entitled to enforce accounting reforms at the municipal level, but only the state governments, in which the municipalities are located. As such, the central government alone would not be able to enforce harmonized accounting norms even in its own country. Secondly, the organization of the public sector differs. Some countries have a centralised state (such as France) and others run a federal system (such as Germany). Depending on the country, federal states can have an own right to determine their

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[1] See e.g. Manning and Lau (2016), pp. 39 ff., in: Bovaird and Loeffler (2016).

[2] For example, in Europe, see Brusca et al. (2015), p. P. Xiii.

[3] See EY (2012) and Brusca et al. (2015) for an overview. The terms are explained in Chapter 3 of this textbook.

[4] See for the following eight reasons: Jorge et al. (2011) with reference to Brusca Alijarde and Condor (2002), Brusca Alijarde and Benito López (2002).

accounting system. Differences in the accounting traditions may thirdly lead to differences in specific objectives of governmental financial reporting. Whereas in the Continental European countries accountability is the utmost objective, in Anglo-Saxon countries typically decision usefulness takes a centre stage. Differences in these objectives determine different accounting norms. Depending on divergent views about the principal users of financial reporting as a fourth point, the reporting contents can be different. One example is the difference between standards of the Governmental Accounting Standards Board (GASB, i.e. the accounting norms for US local government) and the International Public Sector Accounting Standards (IPSAS) Board. Whereas the citizenry is seen as the main user in the GASB Framework (there is not only focus on financial terms, but also on contents about economy, efficiency and effectiveness), IPSAS focus on service recipients and resource providers, hence suggesting a more general, financial perspective.

Fifth, the type and extent of financial resources suppliers may influence the type of information and reporting needed in order to assess financial wellbeing and the ability to repay debt. Important external financiers such as the World Bank or the International Monetary Fund (IMF) do indeed influence the accounting norms that their governmental borrowers use. As sixth and seventh reasons, national institutions can play a role in differences. Stimuli towards or resistance against reforms of governmental accounting may come from regulatory bodies such as financial regulation authorities or competition authorities or professionals such as accounting profession bodies. A final main reason are differences in the political and administrative environment. Whereas European Continental countries have a strong culture of administration and the Rechtsstaat, a so called rule of law, Anglo Saxon countries rely on common law. This leads to differences in the number of individual circumstances that have to be addressed by accounting norms and standards.

In order to reduce differences in PSA and reporting, the EC strives for harmonization of the heterogeneous accounting systems of its member states by the adoption of European Public Sector Accounting Standards (EPSAS). The EPSAS project arose as a response to the financial and

economic crises beginning in 2008 and the reliability problems that became apparent with the public debt data (and other fiscal data to monitor fiscal discipline) delivered to the EC by some EU member states. Thus, in 2011, the European Council passed a set of measures to reform the Stability and Growth Pact and to provide greater macroeconomic surveillance. The so-called 'Sixpack' contains 5 regulations and 1 directive. Directive 2011/85/EU refers to requirements for budgetary frameworks of the member states. Overall, this directive claims for more homogeneity of the budgeting rules among the member states. In one article of this directive, the EC was requested to assess whether the IPSAS would be suitable for adoption in all member states. In effect, this could lead to an overall harmonisation of public sector reporting in the EU. In a review of the suitability of IPSAS, the EC came to the conclusion that "IPSAS standards represent an indisputable reference for potential EU harmonised public sector accounts"[5], but need some adjustments so that these "would be suitable as a reference framework for the future development of a set of European Public Sector Accounting Standards".[6]

As a consequence, the EC instructed its statistical office Eurostat to undertake such an assessment of IPSAS. Thus, the Eurostat EPSAS Task Force has been founded in 2012 and is still in place. In 2013, the Task Force EPSAS Governance was created by Eurostat with the aim to exchange views with the member states' authorities. The topics were: possible future governance arrangements and underlying key principles of EPSAS. The Task Force should assist Eurostat in developing a model for the EPSAS governance structure.[7]

This was followed by the creation of the Task Force EPSAS in 2014. Again its aim was to exchange experiences with authorities of the member states. The focus of this group was the analysis of IPSAS with respect to difficulties of adoption in the EU, the analysis of how to reduce difficulties for small public entities and the discussion on the implementation of

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5 EC (2013), p. 7.

6 EC (2013), p. 8.

7 Weyland and Nowak (2016), p. 114.

standards. In order to establish a more permanent forum concerned with the development, introduction and operation of EPSAS, both task forces were completed in 2015 in favour of the creation of the EPSAS Working Group. This is a technical expert group consisting of representatives from the member states, international advisors and Eurostat staff. The Working Group meets twice a year, being supported by three EPSAS Cells. Two were set up in 2015: one on First Time Implementation and a second on Governance Principles. A third cell on Standards Principles is working since 2016. In addition, the Eurostat Task Force gets feedback from public consultations and EPSAS issue papers that are compiled by members of accounting profession.[8]

As the EU plans to develop EPSAS with IPSAS as a reference, public entities or governments that opt for a voluntary use of IPSAS until 2020 currently receive financial support by the EU. The period of 2020-2025 was indicated by the EU as a transition to EPSAS, leading to a homogeneous EU-landscape of PSA and reporting. However, this implies that the EPSAS implementation project is completed and a legal basis for the adoption in the EU member states has been found. To date, an impact assessment[9] is being completed to discuss different scenarios of the bindingness of the EPSAS pronouncements. More details on the EPSAS background and development are provided in the chapters 6 discussing the challenge for harmonization and 14 providing an EPSAS outlook.

The remainder of this chapter will derive a map through the book by explaining important terms with respect to European PSA and by highlighting on which concepts this book will focus on. Section 2 starts with identifying the reporting units, whereas Section 3 discusses sources of PSA. The different types of accounting are addressed in section 4. On which geographic focus this book will draw, is explained in Section 5 with more specific explanations of PSA standards in the EU in Section 6. Finally, different reporting units are explained (Section 7) and a conclusion with a roadmap is provided (Section 8).

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[8] Weyland and Nowak (2016), p. 114.

[9] See EC (2019), p. 6.

2. Scope of reporting units

In order to narrow down the content of this book, the public sector needs to be differentiated from the private sector. This chapter draws on the differentiation of ESA, i.e. the statistical system of the EU. According to its internationally recognized definition, the public sector consists of all institutional units resident in one economy that are controlled by the government. The private sector consists of all other resident units (ESA 1.35). Therefore, the concept of control is the first criterion to distinguish the public sector. Control is defined as the ability to determine the general policy or programme of an institutional unit (ESA 1.36).[10]

Second, a differentiation between market and non-market activities is considered to distinguish between public sector entities belonging to the general government sector and the corporations sector. A market activity has the following conditions, which do not have to be met perfectly (ESA 1.37):

(1) Sellers act to maximise their profits in the long term, by selling goods and services freely on the market;

(2) Buyers act to maximise their utility given their limited resources;

(3) Effective markets exist where sellers and buyers have access to, and information on, the market.

Thus, the public sector consists of the general government and public corporations, both being controlled by the government. Public sector corporations are distinguished between non-financial and financial corporations with e.g. the central bank belonging to the latter type. However, only general government units are in the focus of this chapter. Government units are legal entities established by a political process, which have legislative, judicial or executive authority over other institutional units within a given area. Their principal function is to provide goods and services to the community and to households on a non-market basis and

[10] Further details in relation to the definition of control can be found in the ESA guidelines.

to redistribute income and wealth (ESA 20.06). The general government is classified further, into four levels of entities.

The **central government** subsector includes all administrative departments of the state and other central agencies whose competence extends normally over the whole economic territory, except for the administration of social security funds (ESA 2.114). On a lower level, the **state government** subsector consists of those types of public administration which are separate institutional units exercising some of the functions of government (e.g. education, road infrastructure), except for the administration of social security funds, at a level below that of central government and above that of the governmental institutional units existing at local level (ESA 2.115). As a third subsector, the **local government** includes those types of public administration whose competence extends to only a local part of the economic territory, apart from local agencies of social security funds (ESA 2.116). Finally, the **social security funds** subsector includes central, state and local institutional units whose principal activity is to provide social benefits and in which, by law or by regulation, certain groups of the population are obliged to participate in the scheme or to pay contributions; and for which general government is responsible for the management of the institution in respect of the settlement or approval of the contributions and benefits independently from its role as supervisory body or employer (ESA 2.116).

This book focuses on public entities of central, regional or state and local government. In the following and throughout the book, these are referred to as **public sector entities**.[11] These have specific characteristics that distinguishes them from private sector entities. On the one hand, public sector entities have sovereignty that is, depending on the structure of government, ultimately controlled by politicians who hold power and responsibility in the legislative and executive systems. On the other hand, public sector entities seek for the production of public goods and services, which can also lie in the redistribution of income or the regulation of industries. In order to raise financial resources, public sector entities hold

[11] Although, at times, strictly speaking, one would need to refer to government entities.

the power to tax. As public goods and services are often delivered for free, governments entities do not strive for profits but for recovery of their costs.[12] These differences also lead to adjustments compared to private sector reporting as e.g. the aim of the units differ and there are potentially different stakeholders.[13] Also different sources of PSA information have been developed, which are explained in the next section.

3. Sources of PSA information

PSA information can be derived from different sources. A selected list of accounting sources is shortly introduced in the following: (1) Budgeting, (2) Budgetary accounting and reporting, (3) Financial reporting, (4) Management accounting, (5) Sustainability and Integrated reporting and (6) Government financial statistics.

(1) Budgeting: Government sector entities are organizations ultimately controlled by politicians. A major responsibility of politicians refers to their authority to establish a budget. The budget is an estimation of expenditures/expenses to provide public goods and services, to suppress public needs, as well as the estimated revenue to cover those expenditures/expenses. Usually the budget is established for one to two years. However, besides being merely a plan, the budget also serves as an authorization by the deliberative body (such as elected politicians) to the executive body, for any expenditure which is later on undertaken by the public entity's administration. Therefore, the budget is formalized by law. It is therefore also made publically accessible, so that citizens in general can inform themselves about how resources are spent and which public services are planned to be delivered. However, mainly, the budget is used by managers of the administration, the politicians and legislative overseers. Especially due to its legal bindingness, the budget is central in PSA and reporting.

[12] Jones and Pendlebury (2010), pp. 2 f.

[13] See e.g. Pallot (1991).

Therefore, budgeting and budgetary accounting will be discussed in more detail in Chapter 4 of this book.

(2) Budgetary accounting and reporting: After the budget has been approved, in the respective budgetary year the actual payments and receipts (and/or expenditures and revenues) are documented, i.e. accounted for, and compared with the previously agreed annual budget. The budgetary reports provide information about the extent to which the budget has been realized, therefore the information is made publicly available. The statements such as budget out-turn reports (comparing budgets planned and spent), financial balance sheets and explanations of significant variances, are used by public managers, politicians, legislative overseers and also citizens. Budgetary reports are produced at least annually, however mostly also supplemented by quarterly or monthly reports.

(3) Financial accounting and reporting: Besides a comparison of planned *versus* actual budgetary figures at the reporting date, public sector entities can also prepare an overview of the resources, i.e. assets and sources of finance (liabilities & net assets), as well as an overview of the resource consumption and creation, i.e. expenses & revenues; cash in- & outflows, during the reporting period. The documents thereby produced on an annual basis are called financial statements which are composed by, e.g., a balance sheet (disclosing assets and liabilities), income statement (comparing revenues and expenses) and cash flow statement (showing cash inflows and outflows from three activities (operations, investing, financing – see also Chapter 9). As such, compared to the budget and budgetary reports, financial reporting information can deliver further relevant accounting information such as reliable accounting measures in the form of net costs for services provided, assets and liabilities.[14] Conceptually, by deducting assets from liabilities the net assets are derived, which differ to some extent from the concept of equity that is known in the private sector. Still, the fundamentals of accounting are the same in both sectors,[15] if based on accrual accounting and double entry bookkeeping. Nonetheless,

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[14] Jones and Pendlebury (2010), p. 115.

[15] Jones and Pendlebury (2010), p. 30.

as Lüder (2011) asserts, financial accounting, reporting and auditing "is not mainstream and only a few scholars are working in this field" in most countries.[16] Due to this reason, and particularly because the main reforms of PSA and reporting internationally, in the last years, has centred on financial accounting and reporting,[17] and also the EPSAS project only covers this source of accounting information, the focus of most chapters in this book is on financial accounting and reporting.

(4) Management accounting: In the public sector management accounting and control is traditionally structured around budgeting,[18] however its functions go beyond pure budgeting because the information delivered is more detailed and user-oriented. Management accounting refers to the calculation of the resource consumption (costs) of organizational units or product/service units for control or pricing purposes. Statements produced on a monthly or quarterly basis are, e.g., costing systems or cost allocation sheets which refer to single product or service units or organisational units, but can also cover the entire organisation. In contrast to budgetary or financial reporting, management accounting is basically for internal users such as public managers, administration, politicians, and legislative overseers. A further difference to financial reporting is that management accounting information may, besides past information, also contain future information, e.g., in the form of cost forecasts or replacement costs.

(5) Sustainability and Integrated Reporting:[19] Both of these approaches of reporting are alternative approaches compared to traditional financial reporting as these cover also non-financial information. Both, Sustainability Reporting and Integrated Reporting address organizational stakeholders and contain past, but also future-orientated information in the form of strategy reporting. Both approaches not only concentrate on

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[16] Lüder (2011), p. 5, in: Jones (ed.).

[17] In particular, also because budgeting has a strong legal basis in each country and thus international accounting standard setting bodies focused on financial accounting and reporting (Jones and Pendlebury, 2010, p. 85).

[18] Jones and Pendlebury (2010), p. 85.

[19] Performance reporting, another source of PSA information is not introduced here.

the reporting entity itself, but also cover how the entity interacts with its environment, society and governance. Therefore, Sustainability Reporting aims at delivering an overview of an economic, environmental and social performance of an organization, whereas Integrated Reporting can be seen as a wider approach to report on organizational public value creation during a reporting period. Integrated Reporting is about representing clearly and concisely how a public entity creates and sustains public value (e.g. public welfare), taking into account economic, social and environmental factors (IIRC, 2013) by reporting financial and non-financial information in an interconnected way. Reasons for Integrated Reporting and how it can be prepared in the public sector are addressed by, e.g., Cohen and Karatzimas (2015), Oprisor et al. (2016) and Katsikas et al. (2017). With respect to the extent of reporting, Sustainability and Integrated Reporting go beyond what is covered by General Purpose Financial Statements, a term that is introduced later in this section.

(6) Government Financial Statistics: In contrast to the reporting approaches introduced above, Government Financial Statistics (GFS) do not only focus on single entities, but cover a total economy (e.g., region, country or group of countries) and report on all of its sectors (i.e. households, corporations and governmental entities). The aim of GFS is to deliver a systematic and detailed description of a total economy, its components and its relations with other total economies, building on an (internationally compatible) accounting framework. For the EU, the ESA 2010 is relevant, whereas on an international level, the System of National Accounts of the United Nations (SNA 2008) is used. Differences between ESA and SNA lie especially in their presentation. Accounting measures of GFS are, e.g., the net worth of a total economy (stocks of assets deducted of liabilities), its Gross Domestic Product (i.e. the sum of value added (gross)) and the value added of an industry (sum of incomes generated in an industry). Conceptually in the ESA, the demand for any product or product group has to equal its supply from within or outside the economy. Primary users of GFS information are politicians, statisticians, managers, oversight bodies (such as the EC) and the main statements produced are institutional sector accounts using an input-output framework. In the EU,

GFS requirements have also driven the call for harmonizing PSA across the member states (as the latter provides input for the former) and thus the EPSAS project. GFS will be explained in more details in Chapters 6 and 7.

With respect to sources of PSA information, not only the different approaches to accounting play a role, but also the scope of reporting. In this notion, the terms General Purpose Financial Statements (**GPFSs**) and General Purpose Financial Reports (**GPFRs**) have been coined, which play a key role and therefore are explained in the following and depicted in Figure 1.1[20].

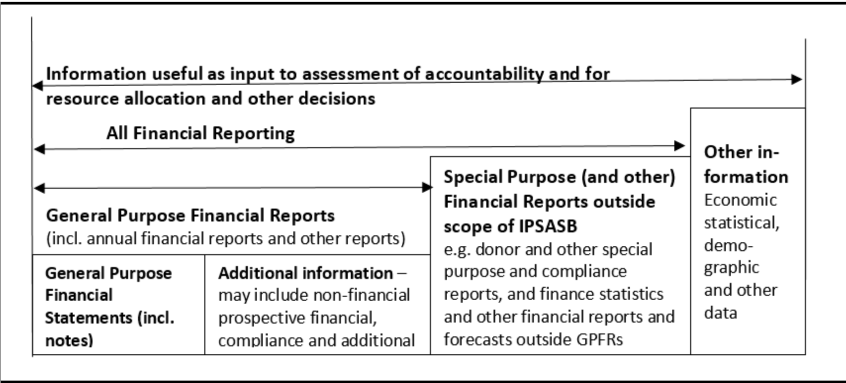

Figure 1.1: Scope of reporting depending on information needs of users

In the preface of the IPSASs, GPFRs are defined as "financial reports intended to meet the information needs of users who are unable to require the preparation of financial reports tailored to meet their specific information needs."[21] In a consultation paper for the Conceptual Framework in 2008, the IPSASB aimed to distinguish GPFRs from GPFSs and other reporting concepts. Typically, GPFSs contain financial information about financial position, financial performance and cash flows[22] and are often accompanied by narrative information in the notes. GPFRs go beyond GFFSs and include additions such as non-financial prospective financial information, compliance information and additional explanatory material.

[20] IPSASB (2008), 1.14 Figure 1.

[21] Preface 9, IPSASB (2018), p. 14.

[22] IPSASB (2018), CF 2.17.

Thus GPFRs encompass the annual financial reports and other reports. For example, the IPSAS pronouncements also entail non-binding Recommended Practice Guidelines (RPGs) with voluntary additional non-financial information.

Despite of financial reports that are not tailored to meet specific information needs, also Special Purpose Financial Reports and other reports can be prepared, for those users that have the authority to demand specific reports for their information needs. Such reports could be e.g. donor reports, compliance reports, finance statistics and other financial reports and forecasts outside GPFRs. Special Purpose Financial Reports are outside the scope of IPSASs (see chapter 9). Together, GPFRs and Special Purpose Financial Reports form the concept of 'all financial reporting'. As also the IPSASB (2008, 1.15) states, GPFRs "may not provide all the information users need for accountability, decision-making or other purposes". Thus, in an extension of all financial reporting, the entirety of information that is "useful as input to assessment of accountability and for resource allocation and other decisions", as well as other information such as economic statistical, demographic and other data, can be included into the reports.

In the following, this book will focus on GPFRs and primarily will introduce financial accounting and reporting, as well as budgeting and budgetary reporting to some extent.

4. Accounting systems and techniques

As already indicated in Section 3 and when addressing the reforms in PSA, there are different systems of accounting in place, which will be introduced in this section and more thoroughly are explained in particular in Chapter 4. Thereby, a distinction is made between single entry and double entry bookkeeping as well as cash accounting and accrual accounting systems.

With respect to transactions recording techniques, one can distinguish between single entry and double entry bookkeeping. In general, bookkeeping is defined as recording of financial impacts of economic

transactions or events of an organization. Using the **single entry bookkeeping technique**, each transaction is only recorded once. Mostly, the transactions recorded are based on the inflows and outflows of cash. Advantages of single entry bookkeeping relate essentially to the simplicity of the system, which however comes with the disadvantages of risking lack of comprehensiveness and coherence.

In contrast, by using **double entry bookkeeping**, for each transaction there are at least two related recordings, balancing between each other. This leads to the advantage that an income statement and a balance sheet can be derived from the accounting data as assets and liabilities are recorded. However, the system is much more complex and requires extended knowledge for its use.[23] The relevance of double entry bookkeeping for PSA has been much debated in literature[24] and its history and reference to persons such as Luca Pacioli will be explained in Chapter 2. A basic principle of double entry bookkeeping is that for each transaction at least a debit entry on one account and a credit entry on another account is to be recorded. The system is closed so that all accounts must balance. Over an accounting period, the monetary value of debit entries must equal the monetary value of credit entries. Table 1.1 provides an overview of the changes of debit and credit entries depending on the types of accounts.

Groups of accounts	Debit entries (D)	Credit entries (Cr)
Assets accounts	Increase ↑	Decrease ↓
Liability accounts	Decrease ↓	Increase ↑
Capital or equity (net assets) accounts	Decrease ↓	Increase ↑
Revenues accounts	Decrease ↓	Increase ↑
Expenses accounts	Increase ↑	Decrease ↓

Table 1.1: Principles of double entry bookkeeping

Regarding the timing of the recognition of revenues and expenses. in general, cash accounting and accrual accounting are distinguished. For

[23] Van Helden and Hodges (2015), p. 57.

[24] See e.g. Soll (2014).

cash accounting, revenues and expenses are only recognized when the receipt/payment occurs. Thus, in its pure form, cash accounting does not allow for the recording of assets and liabilities. As such, the system has been criticized for not being transparent with respect to financial implications of economic events. In contrast, when using **accrual accounting** revenues are recognized in the period earned and expenses in the period in which these are incurred, regardless when they are received/paid.

Often, single entry bookkeeping is combined with cash accounting systems and, particularly in the public sector, used for budgeting and budgetary accounting.[25] In the public sector of German-speaking countries, a system called cameral accounting that also uses the combination of single entry bookkeeping with cash accounting has evolved and is partially also still in place (e.g. at central level). Cameral accounting will be addressed in more details in Chapters 2 and 4.

To illustrate the differences between cash and accrual accounting, the following example can be used: On 15.11.20X0 a public entity delivers services, worth 10,000 EUR. At the same date, the service recipient receives a bill but does only pay in cash in the next year, on 01.02.20X1. In a cash-based system, a revenue will only be accounted for together with the cash when the payment is received, so on 01.02.20X1. Thus, the revenue is not shown in the year t0, in which the service was delivered. In contrast, when using an accrual-based system, the revenue is already recorded on 15.11.20X0 together with accounts receivable. Thus, the revenue falls in the year 20X0. After the payment, cash is accounted for and the accounts receivable are cleared. As such, both systems lead to a different timing recognition and reporting of revenues and expenses. This is particularly the case for the purchase of non-current assets and their depreciation which is only recorded in an accrual-based system.

Besides a strict distinction between cash and accrual accounting, also modified regimes are in place in many countries, which are further distinguished between the public and private sector. Thus, according to the extent of use of accrual accounting, Lande (2011) distinguishes

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[25] Bergmann (2009), p. 66.

four types of accounting systems.[26] In a **modified cash accounting system**, only monetary (e.g. cash-based) assets and liabilities are accounted for. Thus the list of assets only contains cash and cash equivalents and loans and investments of the year. This system is currently prevalent in the Netherlands and at the central state level of Germany. A **modified accrual accounting system** is more developed, because assets also cover receivables, and liabilities also encompass payables. Thus, financial assets and financial liabilities are accounted for. **Accrual accounting at the public sector level** means that most assets and liabilities are accounted for as this is the case in the public sector of Austria, Finland, Sweden, the UK and for the EC. In general, in the EU, **full accrual accounting** is used for the private sector. This means that enterprises have to account for all their assets, including intangible assets, and all liabilities, including provisions. However, exemptions from full accrual accounting may exist, e.g. for smaller companies, or building on the legal form of the company, as in the case in Germany.

Throughout this book, both main bookkeeping techniques and both accounting regulation regimes will be addressed, despite a focus on double entry bookkeeping and accrual accounting.

5. Geographic focus

With respect to the geographic focus drawn in this book, the authors decided to concentrate on the countries of the partners of the DiEPSAm project (i.e. this book authors' affiliations) and, to a wider extent, also on the EU due to its underlying EPSAS project. The strategic partners of the DiEPSAm project represent diverse national PSA traditions and can therefore contribute with contradictory and alternative approaches to create an enriched European society. Thus, in the book a transnational and comparative approach is sought for. Subsequently, the public sector financial accounting and reporting systems in the following countries are

[26] See Lande (2011), p. 17 for details.

introduced: Austria, Finland, Germany, Portugal and the United Kingdom (UK). It needs to be stressed, that the brief descriptions only cover financial but not budgetary accounting. Also it needs to be distinguished between the government levels: Finland, Portugal and the UK have two government levels (central and local), whereas in Austria and Germany there are three levels of government (central, state and local).[27]

In Finland, Portugal and the UK, both at the central and local government level, accrual accounting systems are in place. In Austria and Germany, the systems are heterogeneous at the different levels of government. Of the three levels of government in Austria, to date only the central government has fully switched to accrual accounting. At the regional and local government levels there are diverse systems in place. However, there is a transition procedure going on to accrual accounting, which will come into force at the regional level from 2019 onwards and at the local government level from 2020 onwards. In Germany, the most diverse systems are currently in place. In general, there is an option to choose between modified cash and accrual accounting at central and state level. However, currently the central government uses modified cash as well as twelve of the sixteen federal states, so only four federal states decided to use accrual accounting. Instead, at the local level, most federal states (twelve) enforced accrual accounting for the municipalities comprised within them.

As such, where applicable, the book will draw on comparative studies between Austria, Finland, Germany, Portugal and the UK and also will shed light on the EPSAS project in the EU.

6. PSA standards in the EU

As outlined in the introduction, currently the EC, authorizing via the Eurostat, aims to harmonize PSA in Europe. Thereby, EPSAS are to be developed that might use the IPSAS as a basis of reference. However,

[27] See Brusca et al. (2015) for detailed descriptions of the accounting systems.

potentially, with respect to the accounting norms to be used for the EU member states, there are different options to consider.

On the one hand, there are the internationally accepted accounting standards produced by private standard setting bodies. However, on the other hand, private standard setting bodies do not have the power to enforce their norms into any national accounting system. Therefore, these accounting standards can either be used voluntarily by reporting units, or mandatorily by endorsement in each country individually. For the private sector, the International Financial Reporting Standards (IFRS) released by the IASB are widely used. IFRS are used as a basis of reference for the IPSAS released by the IPSASB, being adjusted to the public sector context.

Despite a voluntary use or adoption of international accounting standards, of course also national or local standards can be in place that have to be mandatorily used by resident reporting units. For private sector entities, in many countries there are national commercial codes. These often also serve as a basis of reference for PSA norms. As such, some countries have their own accounting regimes for the public sector or they adjust IFRS or IPSAS to be used in the public sector. Examples of the countries involved in the DiEPSAm project are: Finland and Germany that adjusted their national commercial code for the public sector; Portugal and Austria that use modified IPSAS; and the UK that primarily adapted IFRS directly. Therefore, the question remains – which set of norms has superior suitability for serving as an EPSAS basis.

This book aims to shed light on different accounting standards such as IPSAS, potential EPSAS, but also national systems in the partner countries, to provide comparative transnational insights.

7. Reporting units

With respect to financial accounting and reporting, also the reporting unit needs to be considered, i.e. the boundaries according to which one entity is distinguished, and the extent of reporting economic transactions.

Typically, **financial statements** and consolidated financial statements are distinguished.[28] Accordingly, financial statements concern the individual public entity only. If a public entity holds interests in subsidiaries, these are shown as a financial asset. However, if a public entity has close and strong economic relationships with other entities, financial statements do not clearly depict the financial performance and financial situation of that public entity, if e.g. liabilities have been outsourced together with an asset. Therefore, in contrast to financial statements, **consolidated financial statements** combine all entities under control of a public entity. By applying consolidation methods, holdings, liabilities and groups transactions are combined within one statement. Consolidated financial statements are the content of Chapter 12, whereas consolidation methods and reporting will be addressed in Chapter 13.

More recent concepts, such as **whole of government accounting**, follow the statistical treatment by creating an economic entity that entails all public sector entities in one country. As such, the financial statements cover all government entities and all entities that are controlled by the government (see Section 2 of this chapter for a definition). Therefore, the approach is much broader than consolidated financial statements. Countries using this approach are New Zealand and the UK.[29] Whole of government accounting will be addressed in Chapter 12 in more details.

8. Conclusion

This chapter aimed to present key terms of PSA and reporting and in doing so, also to narrow down the content of the book. As PSA in Europe is currently still very heterogeneous, professionals and academics in Europe face tremendous challenges.[30] In particular, there will be a large need for university graduates and practitioners that are knowledgeable in PSA and

[28] Bergmann (2009), pp. 161 ff.

[29] Bergmann (2009), pp. 157 ff.

[30] Adam et al. (2019).

that are aware of the differing PSA systems across Europe. In order to account for this development, this book concentrates on PSA in Europe. The key terms used and the linked concepts are presented in Table 1.2 below. The topics that this book addresses in the following chapters, are faded out in grey.

<table>
<tr><td rowspan="2">Scope</td><td colspan="6">Public sector</td><td colspan="2" rowspan="2">Private sector</td></tr>
<tr><td colspan="3">General government</td><td colspan="3">Public corporations</td></tr>
<tr><td>Sources of PSA information</td><td>Budgeting</td><td colspan="2">Budgetary accounting and reporting</td><td colspan="2">Financial accounting and reporting</td><td>Management accounting</td><td>Sustainability and Integrated Reporting</td><td>Government Financial Statistics</td></tr>
<tr><td rowspan="2">Types of accounting</td><td colspan="4">Bookkeeping technique</td><td colspan="4">Timing of recognition</td></tr>
<tr><td colspan="2">Single entry</td><td colspan="2">Double entry</td><td colspan="2">Cash accounting</td><td colspan="2">Accrual accounting</td></tr>
<tr><td rowspan="2">Geographic focus</td><td rowspan="2">Inter-national</td><td rowspan="2">Europe</td><td rowspan="2">EU</td><td colspan="5">Selected EU countries</td></tr>
<tr><td>Austria</td><td>Fin-land</td><td>Germany</td><td>Portugal</td><td>UK</td></tr>
<tr><td rowspan="2">Accounting standards</td><td colspan="2">International standards</td><td colspan="2" rowspan="2">EU Standards EPSAS</td><td colspan="4">National standards</td></tr>
<tr><td>IFRS</td><td>IPSAS</td><td>IFRS-based</td><td>IPSAS-based</td><td colspan="2">Own regime</td></tr>
<tr><td>Reporting unit</td><td colspan="4">Separate financial statements</td><td colspan="4">Consolidated financial statements</td></tr>
</table>

Table 1.2: Roadmap of topics presented in this book

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Discussion topics

- Reasons for harmonization in public sector accounting and reporting
- Cash accounting and accrual accounting: What suits the public sector better?
- Accounting regimes for the public sector: Internationally accepted standards vs. local norms