Government Accounting

Making Enron look good

Ian Ball and Gary Pflugrath

Introduction

> Unconsolidated can mean unseen. Greater visibility, on the other hand, holds out the hope that something might be done to address the underlying issues. The transparency drive in UK government accounting managed to avoid exacerbating sovereign debt jitters this month; maybe it can be a genuine asset in the longer term. (*Financial Times* 2011a)

On the day after the UK government finally issued its first 'Whole of Government Accounts (WGA)', at least one media commentator recognised the significance of the event. The transparency and accountability associated with preparing and publishing accounts, on an accrual basis, for the entire government did not 'spook' markets at a time of great uncertainty; rather it may have had a positive effect. Critically, there is recognition that transparent, robust, accrual-based financial reporting by governments may assist in addressing 'underlying issues'. In its *Global Financial Stability Report* (April 2011), the International Monetary Fund (IMF) recognised the importance of strengthening sovereign balance sheets, and the need for 'improved governance of fiscal decision making, including through independent monitoring of targets and enhanced transparency over

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accruing obligations and contingent liabilities' (International Monetary Fund 2011, p. 35).

Such enhanced transparency, and the reporting of accruing obligations and contingent liabilities, are fundamental features of a strong accrual-based financial reporting framework for the public sector. By contrast, governments with poor accounting practices are unable to make fully informed decisions about the allocation and use of scarce resources, and thus are handicapped in solving the problems posed by the sovereign debt crisis. Practices that result in comprehensive and reliable reporting of the performance and position of the government, and that are audited, enhance accountability and transparency, and are essential to solving the problems exposed and highlighted by the sovereign debt crisis. New and revised fiscal treaties – at least those discussed to date – are necessary but not sufficient. While enhanced, robust public-sector financial management would not solve the crisis, it is clear that the problems presented by the crisis will not be solved without it.

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In the early part of this century large corporate failures such as Enron, Worldcom and Parmalat resulted in swift government action to remedy identified shortcomings in the financial reporting and assurance of publicly listed companies. More stringent reporting and disclosure requirements were introduced, including legislative measures such as the Sarbanes-Oxley Act (SOX) in the United States, which – in the context of already robust reporting requirements – imposed detailed requirements for the assessment of internal controls over financial reporting. Stricter independence requirements were mandated for auditors, who were also subject to much closer scrutiny and inspection by government regulators. Many measures outlined in this legislation provided a template for government action around the world. In part because of SOX's extra-territorial effects, the key elements of the legislation were largely replicated – adopted with modifications to suit local conditions – in many jurisdictions around the world.

These measures were aimed at restoring confidence in capital markets, which had been dealt severe blows by the misreporting of corporates and the associated audit failures. However, it is a lack of confidence in government debt markets that currently confronts investors, and potential investors. Significant rollover risk – the risk that a country may not be able to refinance or roll over its debt – exists for many governments, as the gross borrowing needs of OECD governments alone for 2012 reaches $11.5 trillion (*Financial Times* 2011b). The IMF notes that weaknesses in sovereign balance sheets are having a direct impact on the private sector and investors, through higher country risk premiums and the fears of write-downs on government debt holdings (International Monetary Fund 2011).

In response to the loss of confidence in capital markets earlier this century, governments sought to establish a high bar for reporting and disclosures by private-sector entities. There is an obvious hypocrisy in that when it is their own accounting at issue, governments are taking little serious action to address the problem. This raises the question ‘Why are governments that impose such stringent reporting requirements on others – in the private sector – not prepared to impose similar disciplines on themselves?’ The answer lies in the incentives facing politicians and public servants.

Public choice theory, or the economics of public choice, may help explain the behaviour of politicians and public servants in this respect:

> … public choice, like the economic model of rational behavior on which it rests, assumes that people are guided chiefly by their own self-interests and, more importantly, that the motivations of people in the political process are no different from those of people in the steak, housing, or car market. They are the same human beings, after all. As such, voters ‘vote their pocketbooks,’ supporting candidates they think will make them personally better off; bureaucrats strive to advance their own careers; and politicians seek election or re-election to office. Public choice, in other words, simply transfers the rational actor model of economic theory to the realm of politics. (Shughart II 2007)

This theory suggests that politicians and public servants do not always act in the public interest. Indeed, it may help explain why governments do not want transparency, why they do not want anyone else setting their financial reporting standards, and why ministries of finance generally do not advocate for better accounting (Ball 2011a).

The need for better reporting

If current arrangements for public-sector financial management provide incentives for politicians and voters to behave in ways that are arguably contrary to the general public interest, efforts should be made to redesign the institutional arrangements to achieve better long-term alignment between the interests of decision-makers and the general public. Actions taken by many governments during the global financial crisis have caused that crisis to 'morph' into a sovereign debt crisis. While some actions by governments were clearly necessary to stem financial sector contagion risk, and to guard against systemic meltdowns, not all governments were fully aware of the implications of the decisions they were making. Simply, they did not have financial management systems and processes adequate to the task. Of course, in at least one situation, the accounting and reporting by a government was not merely deficient, but also fraudulent. In the case of Greece it seems that self-interested politicians and public servants were keen to ensure that an accurate picture of the country's finances was not made available. While changing reporting arrangements and processes will not of itself ensure that fraudulent reporting is eliminated, implementing a system that is based on a structured, robust framework permits reported information to be audited – that is, it allows independent assurance about the reliability of the information presented, and whether it is free from material misstatement.

As well as being aware of how decisions impact their constituencies, governments need to be cognisant of the responsibility they have to protect those who have invested in public debt. The advent of global markets means that governments are accountable to investors in government bonds, who come from many parts of the globe. A global market will operate more efficiently, and will engender greater confidence, if investors operating in that market receive accurate, detailed information about the specific government or governmental organisation in which they are investing. Only in circumstances where such investments are actually risk-free might the detailed information arguably not be required – though, as we have learned, the risk-free assumption is a dangerous one.

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Sovereign debt defaults and 'haircuts' taken by investors in public debt over the years, when combined with recent events in Europe and the downgrade of the US government, make it abundantly clear that government debt cannot be considered 'risk free'. Indeed far from it. Table 1 shows a list of 24 countries that had sovereign debt restructuring agreements between 1990 and 2005, prior to the current crisis. Private-sector organisations must provide detailed, audited financial reporting and disclosures to banks and credit providers so appropriate risk premiums and the price of borrowing can be determined. Once the 'risk-free' assumption can no longer be made, investors in public debt require similar detailed information from governments, and for the same reasons.

It cannot seriously be disputed that more accurate, robust information can improve the decision-making of governments. With better accounting governments will, at least, be more fully aware of the implications of decisions they make; and even when difficult decisions need to be made – such as 'bailing out' banks and providing economic stimulus packages – the full impact of those decisions (including the impact on the government's own balance sheet) can be more accurately anticipated. Also, investors in public debt can make more informed investment decisions, and ensure that the price of debt more accurately reflects the economic reality presented by governments.

Arguments against enhanced public-sector financial reporting, disclosure and financial management typically involve arguments that superior methods are either not available, or come at a prohibitive cost. The former is patently untrue for governments that continue to use traditional, cash-based methods of accounting; while the latter can be countered – perhaps

Table 1: Countries with sovereign restructuring since 1990 (agreement date)

Algeria (07/1996)
Argentina (04/1993, 04/2005)
Brazil (04/1994)
Bulgaria (06/1994)
Chile (12/1990)
Cote d'Ivoire (03/1998)
Croatia (07/1996)
Dominican Rep. (08/1994, 05/2005)

Ecuador (02/1995, 08/2000)
Mexico (05/1990)
Morocco (09/1990)
Nigeria (12/1991)
Pakistan (12/1999)
Panama (05/1996)
Peru (03/1997)
Philippines (12/1992)

Poland (10/1994)
Russia (08/2000)
South Africa (09/1993)
Ukraine (04/2000)
Uruguay (05/2003)
Venezuela (12/1990)
Vietnam (12/1997)
Serbia & Montenegro (07/2004)

Source: Cruces & Trebesch (2010)

with a little more effort – through careful examination of the costs of making, and of not making, such improvements. The unexpected costs of poor decision-making and fraudulent reporting are currently being felt in not-so-uncertain terms.

‘Traditional’ and ‘modern’ methods of government accounting

Citizens and investors deserve more reliable and complete financial information, and greater transparency and accountability, from governments. The costs of not doing so are just too high. The Chairman of the International Accounting Standards Board noted that ‘without transparency, neither can there be trust or accountability’ (Hoogervorst 2011). Governments that employ traditional cash-based public-sector accounting cannot be transparent; their reporting necessarily presents only part of the total picture. Traditional methods of government accounting – cash-based accounting, or at the best an inadequate form of accrual accounting – are simply insufficient to allow governments to discharge accountability to the public, or to permit investors and potential investors to make fully informed decisions. Better accounting practices are required. Once it is accepted that government debt is not ‘risk free’, risk premiums must be determined, and that requires information.

The cash-based accounting of many governments basically involves the reporting of cash inflows (e.g. cash received from taxation receipts, interest earned on investments, proceeds from sale of assets) and cash outflows (e.g. spending on government programmes, interest on borrowing, lending, asset purchases, public-sector salaries and wages). One of the main deficiencies with the cash-based approach is that it does not distinguish between the economic characteristics of transactions. The sale of an asset, giving rise to a cash inflow, is treated in the same manner as cash raised through taxation. Likewise, government lending – a cash outflow – is treated the same as the payment of public-sector salaries. However, it is on the cash basis that most governments prepare and present their annual budgets, which become headline economic news. The difference between these inflows and outflows is reported as the budget surplus or deficit, and becomes the centrepiece of reporting, analysis and debate. Of course, where deficits exist governments must borrow money to close the shortfall. These borrowings – government or public-sector debt – also become headline news, and become a key way in which many countries, and governments, are assessed.

It would be folly to suggest that these types of cash-based measure are not important. They are. How can any business survive without knowing its cash position, inflows and outflows, borrowing requirements, and liquidity position? However, it is also clear that an important element of reporting is missing. Put simply, what is missing is the value of all physical assets, and non-debt liabilities. These are amounts that can be determined only when an accrual-based accounting system is used. The need for accrual-based public-sector accounting is recognised by the European Parliament. In its *Report on the proposal for a Council directive on requirements for budgetary frameworks of the Member States* in May 2011, the Parliament's draft legislative resolution includes: 'Member States shall have in place public accounting systems, applying the accrual basis of accounting and comprehensively and consistently covering all sub-sectors of general government as defined by Regulation (EC) No 2223/96 (ESA 95). Those systems shall be subject to independent control and audit' (European Parliament 2011)

It is perhaps surprising that there is such strong support remaining for government budgets being on a cash basis. Almost everywhere else, the accrual basis is seen as necessary to an understanding of economic reality. That is, without knowing the effects of a set of decisions or actions on an organisation's assets and liabilities, revenues and expenses, one cannot fully assess their impact. Yet government budgeting systematically ignores non-cash consequences, such as the accumulation of liabilities associated with public service pensions. There is broad recognition of the importance of the accrual basis in nearly all aspects of government accounting; the exception being where it relates to looking at governments' budgets and fiscal positions.

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This cash-based focus continues despite the fact that two key government reporting arrangements – the United Nations System of National Accounts (SNA) and IMF Government Finance Statistics (GFS) – promote the use of accrual-based reporting. Clearly, there are few strong incentives for governments to prepare accrual-based reports using these frameworks. Many commentators talk of sovereign balance sheets, which are generally references to the balance sheets prepared using the GFS or SNA. However, these balance sheets typically are not the same as balance sheets that an accountant would describe. As well as basic differences between the manner in which transactions and items are reported and disclosed in the GFS (and SNA) and in accepted high-quality financial reporting frameworks, the GFS (and SNA) does not provide a consistent basis of comparison between countries.[1]

Differences in reporting between the GFS and a high-quality financial reporting framework include several items that are excluded from GFS reporting, on both the assets and liabilities sides of the balance sheet. The GFS Manual (International Monetary Fund 2001) notes that weapons (e.g. missiles, rockets, bombs) are not treated as assets and therefore, by extension, warships, submarines, military aircraft, tanks, missile carriers are not reported as fixed assets. An accountant, using a robust accrual-based financial reporting framework, and considering the conceptual bases upon which assets are defined, would generally consider weapons to be assets – either fixed assets where they have a life of greater than one year and for which future economic benefits will accrue (e.g. a rifle), or as inventory, the balance of which is adjusted through use (e.g. bullets, bombs). Similarly, warships, aircrafts and other items that clearly have a life of greater than one year would be reported as fixed assets. The costs of fixed assets are allocated over a period of time identified as the asset's useful life. GFS reporting also differs from high-quality financial reporting frameworks utilised by accountants, for intangible fixed assets (e.g. computer software). The difference relates to the conceptual definition of an asset, with the GFS Manual noting that the government must establish ownership rights. It is generally accepted in accounting that control, rather than strict legal ownership, is a defining feature of an asset.

On the liability side of the balance sheet, an item that presents major problems for many governments – and is often cited as a primary reason for many governments not wanting to adopt full accrual-based accounting – relates to the reporting of pension liabilities. The GFS Manual notes that 'No liability is recognized in the GFS system for government promises to pay social security benefits in the future, such as retirement pensions and health care. All contributions to social security schemes are

[1] Progress is being made towards greater consistency between the reporting requirements under GFS and SNA, and reporting requirements using IPSASs. A project to update the GFS is currently under way.

treated as transfers (revenue) and all payments of benefits are also treated as transfers (expense)' (International Monetary Fund 2001, p. 129). This contrasts with the reporting of liabilities in an accrual-based accounting system, which requires the reporting of liabilities as soon as an obligation exists – in the case of retirement pensions for public servants the obligation would generally be a legal one – and which results in the future outflows of economic benefits.[2]

In relation to making comparisons between countries, Table 2 highlights some of the more obvious problems in using the IMF GFS. There are differences between countries in the basis of recording, with the method of recording being described as, variously, non-cash, accrual, or accrual with some items on a cash adjusted basis. Assets and liabilities are valued differently by different countries, while the boundaries of government – for reporting purposes – differ.

Table 2: Summary of key accounting practices used in International Monetary Fund government finance statistics in 2011

Accounting practices (countries adopting those practices)

Basis of recording	• **Non-cash basis** (Australia; Netherlands; United Kingdom) • **Accrual basis** (United States; Chile) • **Non-cash basis, but with some items on cash adjusted basis** (France; Germany) • **Not reported** (New Zealand)
Valuation of assets and liabilities	• **Market/fair value, where available** (Australia) • **Market price** - ***fixed and financial assets***; **Face value** – ***loans and bonds*** (New Zealand) • **Market value** – ***financial assets and liabilities*** (France; Germany; Netherlands; United Kingdom) • **Book value/historical cost** – ***financial assets and liabilities*** (United States) • **Current prices, net of depreciation** – ***fixed capital assets*** (United States) • **Not reported** (Chile)
Units of general government included in reporting (exceptions)	• No extra-budgetary units e.g. government agencies included (United States) • No social security funds included (Australia; United Kingdom)
Based on **information received** in:	• **2008** (Chile; France; New Zealand) • **2009** (Germany; Netherlands; United Kingdom) • **2010** (Australia; United States)

Source: www.elibrary-data.imf.org

[2] Currently, in most instances, intangible assets are not recognised under GFS. However, a project is under way to update the GFS Manual, which is expected to see a recognition requirement included. Also, in relation to employee pension liabilities, requirements are to be included in an updated GFS Manual that are in line with IPSASs.

The inclusion in SNA balance sheets of certain items (e.g. pension liabilities, intangible assets) – which are normally included in a balance sheet by an accountant – is dependent on the application of International Financial Reporting Standards (IFRSs) or International Public Sector Accounting Standards (IPSASs). Balance sheets prepared under the IMF GFS or SNA are currently not ideally suited for measuring and reporting governments' financial performance and position, although typically they are used for this purpose. Inconsistencies in the manner in which the statistics are prepared, and the exclusion of items accountants would typically include in a balance sheet, suggest that a better system could be used.

It seems a relatively straightforward exercise to remedy the reporting deficiencies of governments: introduce a robust accrual-based financial reporting framework. To do so requires two important things: (i) the existence of such a framework; and (ii) the will by politicians to make the decision to improve government transparency and accountability, and therefore enable greater scrutiny of their decision-making. While the former exists – in the form of IPSASs – the incentives provided to politicians in most countries mean that the latter is very difficult to achieve.

IPSASs are developed and issued by the International Public Sector Accounting Standards Board (IPSASB), an independent standard-setting board supported by the International Federation of Accountants (IFAC). The board uses IFRSs as the basis for IPSASs, modifying the IFRS only where the specific circumstances of the public sector require a modification to be made. As such, IPSASs comprise a suite of standards that requires the preparation of a complete set of accrual-based financial statements.[3] While these standards are used as the basis of reporting for a growing number of countries – including Switzerland, Spain, South Africa and Austria – accrual-based reporting has been adopted in several other countries, such as Australia, New Zealand, the UK and Canada. Australia and New Zealand – two countries that have utilised accrual-based accounting for the public sector for nearly two decades, and the latter of which has recently announced the adoption of IPSASs – are consistently regarded as two of the world's leading countries in terms of public-sector financial reporting, disclosure and financial management. Indeed, it is no

[3] There is also a cash-based IPSAS, which is not widely adopted. Governments reporting on a cash basis typically do not aim to be tied to a framework for reporting as strict as cash-based IPSASs.

coincidence that Australia and New Zealand are the two top-rated countries in the Sovereign Fiscal Responsibility Index issued by the Stanford Institute for Economic Policy Research (Stanford University 2011).

It would be easy to suggest that enhancing public-sector financial management is an unattainable, idealistic goal. However, the experience of New Zealand over the last two decades provides a positive example of how the development and implementation of an appropriately designed financial reporting framework can significantly assist governments in their decision-making during times of stress. While robust financial reporting and financial management are not the only reasons for the country enduring the recent global economic and financial crises reasonably well, having them in place meant that the New Zealand government was able to make decisions based on good financial information, and be more confident of the consequences of those decisions. The country strengthened its net worth position from a negative position 20 years ago, to around 10% of gross domestic product (GDP) at the start of the century, and to the equivalent of nearly 60% of GDP just prior to the global financial crisis – the effects of which reduced its net worth to GDP ratio to something over 50%. Although the recent global financial crisis caused net worth to decline, the robust position developed in the preceding two decades permitted the New Zealand government to continue to make fiscally responsible decisions (Ball 2011b). In New Zealand, accrual-based systems are used for budgeting, forecasting and appropriations. Accrual-based reports of fiscal position are prepared on a monthly basis, which keeps fiscal performance and position in the public eye on a continuing basis and acts as a constraint on political decisions. Monthly reporting also allows for timely corrective actions and adjustments to be made.

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Tough decisions were made by politicians in countries like Australia and New Zealand some decades ago to introduce the systems of public-sector reporting, disclosure and financial management that currently exist. In certain respects, these decisions were ‘courageous’, given the incentives that were present at the time, and that are present in most countries now; incentives that mean long-term considerations that are often in the public interest, and that are in the best interests of the country, are often neglected.

Accounting for public-sector finances on a cash basis promotes such a short-term focus, and means that decisions are made that may not promote economy and efficiency. The House of Commons Treasury Select Committee report on the Private Finance Initiative (PFI) in the UK identified the incentives and short-term focus implicit in the PFI. These result in a primary aim being to ensure that debt remains 'off-balance sheet'. It notes that:

> There remain significant incentives to use PFI which are unrelated to value for money:
>
> - The majority of PFI debt still does not appear in government debt or deficit figures;
> - Government departments can use PFI to leverage up their budgets without using their allotted capital budget – the investment is additional and not budgeted for.
>
> These incentives unrelated to value for money need to be removed. (House of Commons 2011, p. 3)

A consequence of continuing to budget and report on a cash basis is that governments and politicians will continue to be less accountable and less transparent than the private-sector organisations that they regulate.

Reforms needed to effect change

Those who rely on government reporting, such as debt holders, suppliers and citizens, have expectations that information reported and disclosed by governments is accurate and reliable. Reforms necessary to ensure robust financial reporting and financial management arrangements range from changes to systems and processes and the use of internationally accepted high-quality reporting standards, to developing and enhancing professional accounting expertise in the public sector, improving governance and transparency arrangements, and requiring that reported information be subject to audit. More specifically, institutional arrangements that could be expected in strong public-sector financial management arrangements include: high-quality and timely financial reporting; audited financial statements; budgets and appropriations on the same basis; full economic and financial transparency ahead of elections; independent, audited projections to accompany budgets; and limitations on deficit spending, with full transparency for breaches of limits. For developed nations there is no real excuse to delay the implementation of these important reforms. The major obstacle – as noted previously – is the lack of political will.

However, there is no use in having strong systems and processes if the financial reporting framework and standards are deficient, and if there is a lack of accounting expertise to ensure that systems function correctly and that standards are appropriately implemented. As noted previously, internationally accepted, high-quality public-sector reporting standards are available in the form of IPSASs. They are structured in a manner that allows for ready adoption across a broad range of government and public-sector arrangements. Consistent and appropriate use of these standards provides high-quality information for politicians and investors, and as global adoption increases it provides for enhanced comparability and analysis. Consistent adoption and implementation are critical to ensuring that the full benefits of using IPSASs are achieved.

In turn, adoption, implementation and use of robust standards can be successful only when accounting skills, expertise and experience are present, available and utilised. Governments must enable and encourage the appointment of professional accountants in key financial positions in the public service. The advice of professional accountants, using accurate and reliable accounting information, complements the advice and information provided by economists and other specialists when considering government initiatives. In ensuring that governments have appropriate candidates from which to choose, the accounting profession must be cognisant of the needs of the public sector when designing professional programmes, training and specialisations.

Furthermore, desired outcomes will not be attained where governance arrangements are deficient. Essential for good governance are arrangements that promote trust – typically achieved through high levels of transparency and accountability. Governments must ensure that they report regularly and widely, providing key information to support decisions and policy directions. The UK's recent experience in the establishment of the Office of Budget Responsibility is an example of where a government has aimed to improve the transparency of its operations and financial decision-making. Ultimately, heightened transparency promotes greater accountability. Governments and politicians providing more accurate, reliable and timely information are more likely to be held accountable for their decisions. It allows others to more critically assess the performance of government in terms of its actions and whether decisions have been made in the public interest.

An important governance initiative, which significantly enhances transparency and accountability, is to have reported and disclosed financial information independently assured – that is, require an audit of the government's financial statements. A key feature of financial reporting in accordance with an established framework such as that provided by IPSASs is that a solid basis ('suitable criteria') is provided for an independent audit. Under traditional cash-based methods of accounting, especially if a well-established reporting framework is not in use, the work of auditors is particularly fraught. With no sound basis for financial reporting, audit reports – where they are sought, for some governments do not seek the benefits of an independent audit and therefore do not subject themselves to scrutiny – will often include modified opinions and scope limitations. Where this happens a key objective of commissioning an audit – to enhance the credibility of reported information by auditors opining on the accuracy and reliability of that information – is lost. Clearly, it is ideal that a system of financial reporting and financial management be structured in a manner that permits independent audit.

Pictorially, Table 3 shows the continuum through which various financial reporting and audit arrangements may be conducted. Ideally, the most meaningful arrangements involve full accrual-based financial reporting, utilising a high-quality accepted reporting framework, such as that provided by IPSASs. This permits a high-quality, independent financial

Table 3: Public-sector financial reporting and audit

Full accrual-based accounting (IPSASs)	Audit opinion can be obtained – robust financial reporting framework; suitable criteria exists
Accrual-based financial statements	Audit opinion may be obtained – suitable framework for reporting may be used: scope limitations and qualifications possible
IMF government finance statistics	
Cash-based IPSAS	
Cash-based accounting	Audit opinion difficult to obtain – lack of high-quality consistent framework for reporting: scope limitations and qualifications common

statement audit to be performed. As noted earlier, there is an inconsistency of methods used in reporting according to the IMF GFS. It is possible that a high-quality, independent financial statement audit may be able to be undertaken. However, in other situations it may not. Descriptions of scope limitations and qualifications of audit opinions would be expected in audit reports in certain circumstances; for example, where particular assets are not recorded and reported, and therefore suitable accounting records are not maintained. Finally, a cash-based system of accounting generally does not permit the undertaking of high-quality audits, given that reporting rules are often idiosyncratic.[4] Of course, the aim for governments should be to move along the continuum towards full accrual-based accounting and independent audit; which in turn would lead to (hopefully) greater fiscal responsibility, accountability and transparency.

Improving decision-making

Reforms that enhance financial reporting, disclosure and financial management should not be seen as merely additions to the vast array of statistics and other information furnished by governments. Furthermore, they should not be seen as substitutes for some of the information and statistics that are currently being provided. Statistics such as those provided to the IMF GFS serve an important purpose. However, the diversity of approaches, the widespread use of cash-based accounting – representing a failure by many governments to effectively implement GFS reporting – and the number of areas where information is not provided, means that these statistics have a limited use in the context of either political accountability or capital markets.

Inadequate information and poor decision-making by governments have serious consequences. Decisions made by politicians today to promote the short-term wealth or benefit of constituents – and that often enhances the re-election chances or meets other short-term objectives of politicians – have an opportunity cost for future generations (Ball 2010). Without the advantage of knowing the future consequences of decisions made today, politicians may be sacrificing the wealth and welfare of future generations for short-term outcomes and political expediency. Full

[4] Although a strict framework for cash-based reporting, such as that provided by cash-based IPSASs, arguably does provide suitable criteria for an audit to be conducted.

accrual-based reporting and budgeting assists in making clear the short-term:long-term trade-offs inherent in many government decisions. The reporting of liabilities, and the disclosure of contingent liabilities, are the most obvious examples.

However, it is not solely about opportunity costs and long-term implications. Poor decision-making has a number of other critical consequences, such as the potential for civil unrest and loss of democratic control that comes from inadequate decision-making. One need look no further that the situation in Greece and the ‘occupy’ protests as examples of these concerns. A government that is more transparent and accountable is more likely to have constituents trust decisions made by politicians, as they are well informed and involved throughout the process. More fundamentally, poor decision-making may reflect in the reduced efficiency and effectiveness of the operations of government. Insufficient and inaccurate information may result in ineffective programmes and projects being implemented and maintained, and a misallocation of resources.

Conclusion

As global economic and financial woes continue, and the inadequacy of many governments’ financial and investment decision-making becomes apparent, there is no better time to promote the need for – indeed, force – improved public-sector financial reporting, disclosure and financial management.

Much of what needs to be done is available and obvious. It is a poor reflection on the political will or capacity of governments if the current opportunity is not taken to reform and enhance public-sector financial management and accountability. Politicians and public servants who act in their own self-interest, and ignore the public interest in reform, will consign future generations to a repetition of the type of mistakes that have led to the current situation, with the cost and disruption that entails.

Would the situation be better now if governments had better information available? It would be foolish to suggest that accounting would, by itself, have saved the world from the current sovereign debt crisis. However, when reflecting on the fraudulent and sub-standard accounting arrangements of many governments, it is clear that accurate, reliable, high-quality information, enhanced transparency and accountability, and better institutional design, would have contributed to better decision-making. It would have permitted governments to have engendered greater trust from constituents, and to be more fully acquainted with the implications and consequences of what they were doing; and, in doing so, would have more properly aligned the incentives of politicians and public servants with the public interest objective of governments.

Clearly, it is time for sovereign debt issues to be addressed and considered from an accounting perspective, as well as the more traditional economic and political perspectives, which by themselves are shown to be inadequate.

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