

Economic governance: requirements for budgetary frameworks of the Member States.

'Six pack'

2010/0277(NLE) - 06/03/2013 - Follow-up document

This report from the Commission entitled “Towards implementing harmonised public sector accounting standards in Member States” fulfils the Commission’s obligation, under [Council Directive 2011/85/EU](#) on requirements for budgetary frameworks of the Member States, to assess the suitability of the International Public Sector Accounting Standards (IPSAS) for the Member States by 31 December 2012. IPSAS is currently the **only internationally recognised set of public-sector accounting standards**.

Background: the sovereign debt crisis has underlined the need for governments to clearly demonstrate their financial stability and for more rigorous and more transparent reporting of fiscal data. This report discusses one of the tools for building this trust and for better measuring and forecasting the fiscal situation, i.e. **harmonised public sector accruals-based accounting standards**. Accruals accounting is the only generally accepted information system that provides a **complete and reliable picture** of the financial and economic position and performance of a government.

Legal framework: Council Directive 2011/85/EU requires Member States to ‘have in place public accounting systems comprehensively and consistently covering all sub-sectors of general government and containing the information needed to generate accrual data with a view to preparing data based on the European System of Accounts (ESA) 95 standard’. It thereby acknowledges the **essential incoherence between public sector accounts**, which only record cash flows, **and the fact that EU budgetary surveillance is based on ESA 95 accruals data**. This means that cash data have to be converted into accruals through approximations and adjustments involving macro-based estimates.

It is founded on the international financial reporting standards (IFRS) widely applied by the private sector and at this point consists of a set of 32 accruals accounting standards, plus one cash-based standard.

Current situation with regard to accruals accounting in EU Member States: the majority of Member States have already implemented accruals accounting according to national standards across the government sector, or are in the process of doing so. Eleven have mixed systems, in that they have implemented different accounting practices at different levels of government. The accounting framework and accounting systems of the European Commission and the other EU institutions and bodies are accruals based and inspired by IPSAS. This is also the case for several other international organisations. Acceptance is growing (but is not unanimous) of the need for accruals accounting for government throughout the EU and its Member States, but a harmonised approach is currently lacking.

Macro-accounting framework: the ESA provides the macro-level statistical accounting framework for the government and non-government sectors in the EU and is accruals based. ESA-based government debt and deficit data for Excessive Deficit Procedure (EDP) purposes are the result of consolidating the individual accounts of general government entities in the Member States and are defined by EU legislation.

The existence and quality of comparable and coherent upstream accruals data (i.e. the primary accounting data for government entities) at micro-accounting level are **preconditions** for the high quality of debt and deficit data at accruals-based macro-accounting level. Micro public-sector accounting in the Member

States has many variants, making comparisons difficult both within and between Member States. The current approach of reconciling non-harmonised micro-level public-sector accounting data for EDP purposes is reaching its limits.

Need for harmonisation: for the compilation of macroeconomic statistics on government and with reference to Article 338 TFEU, the requisite statistical data would be considerably improved if all government entities used harmonised accounting standards. This would allow for the **use of common bridge tables** to compile the entity accounts into ESA accounts, thus greatly facilitating the statistical verification processes. Harmonised standards for public sector accounting would enhance **transparency, comparability and cost efficiency**, and provide the basis for **improved governance** in the public sector. Harmonised accruals-based public-sector accounting would provide a firmer basis for understanding the economic position and performance of governments and government entities at all levels.

Future EU governance of budgetary policies: according to the report, the EU's new governance framework (the "Six Pack", the Treaty on Stability, Coordination and Governance and the "Two Pack" currently under negotiation) will provide for ample *ex ante* coordination of annual budgets of euro area Member States and enhance the surveillance of those experiencing financial difficulties.

Many of the principle objectives advocated at the Council Directive 2011/85/EU, such as the greater transparency and accountability of the public sector, as well as more reliable, timely and more comparable fiscal statistics, necessitate a common, harmonised and detailed accounting and reporting tool.

Potential costs of harmonisation: the information made available by countries which have moved to accruals accounting allows only a very broad estimate to be made of what the costs for the Member States might be, although **they are likely to be significant**. Costs are strongly influenced by the scale and pace of accruals implementation, the size and complexity of the government sector, and the completeness and reliability of existing systems. It is expected that harmonisation will bring about a **reduction in bureaucracy and costs which**, in the medium to longer term, **would far outweigh the expected investment**.

International Public Sector Accounting Standards (IPSAS): IPSAS stems from the idea that **modern public sector management depends on management information systems that provide timely, accurate and reliable information on the financial and economic position and performance of a government**.

Eurostat carried out a public consultation between February and May 2012 to collect views on the suitability of IPSAS. The overall conclusion is twofold: (i) it seems clear that **IPSAS cannot easily be implemented in EU Member States as it stands currently**; and (ii) **the IPSAS standards represent an indisputable reference for potential EU harmonised public sector accounts**.

The following **concerns** will need to be addressed: (i) the IPSAS standards do not describe sufficiently precisely the accounting practices to be followed, which would limit harmonisation in practice; (ii) the suite of standards is not complete in terms of coverage or its practical applicability to some important types of government flows, such as taxes and social benefits; (iii) IPSAS can also be regarded as insufficiently stable, since it is expected that some standards will need to be updated once work is completed on the current project of completing the IPSAS conceptual framework, expected in 2014; and (iv) the governance of IPSAS suffers from insufficient participation from EU public-sector accounting authorities.

Nevertheless, most stakeholders agree that **IPSAS would be suitable as a reference framework for the future development of a set of European Public Sector Accounting Standards (EPSAS)**.

EPSAS – a way forward: the Commission considers that, before deciding on the actual project of creating EPSAS and implementing it in the Member States, some further preparatory steps are necessary. There remain several important questions concerning issues outside the scope of this report, such as **establishing the EPSAS framework and specifying a first set of core EPSAS standards**, as well as the **planning of the implementation**. The Commission would need moreover to describe the necessary milestones for the future project, and take into account impact assessment considerations. A decision can be made only on the basis of an *ex-ante* review of pros and cons, and likely costs and benefits.

The process could take place in **three stages**:

1. A **preparatory stage** to gather more information and points of view, and to develop a roadmap. This stage would begin in 2013 and would involve further consultations, a high-level conference and the preparation of further more detailed proposals;
2. A stage to **develop and put in place the practical arrangements**, addressing issues such as finance, governance, possible synergies and the concerns of smaller government entities. This stage should culminate in the publication of a proposal for a Framework Regulation which would require the application of the accruals principle and set out plans to develop further specific accounting standards over time; and
3. The **implementation stage**: this should be gradual, and allow more time where a Member State's existing accounting standards differ greatly from EPSAS. It could be envisaged that implementation should be achieved in all Member States in the medium term.

The next steps, to be started in 2013, will take into account **impact considerations** and include a **road map** setting out in more detail the steps to be taken, including legislative initiatives, to achieve harmonised public-sector accounting standards across the Union.