

INTERNATIONAL EXPERIENCE OF COUNTRIES PREPARING CONSOLIDATED FINANCIAL STATEMENTS OF THE GOVERNMENT, MONGOLIAN CHALLENGES

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Abstract

Currently, public sector entities applied accounting guidelines and regulations approved by Minister of Finance rather than directly adopting IPSAS. Because accountants of budget entities only use the accounting standards in Mongolian. Such as, IPSAS 1-4, 6, 9, 12-13, 17 and 31 have been fully and partially applied according to a research conducted on accounting guidelines and regulations approved by Minister of Finance among accountants of budget entities and general budget governors. But IPSAS 32-40 have not been fully complied.

However, the researchers confirmed that the accounting guidelines and regulations are based on modified accrual basis and have not been revised since 2007. Also fully and partially state-owned entities (SOEs) comply IFRS according to the Law on Accounting, it is still theoretical and methodological problem that how to consolidate SOEs into the consolidated financial statements of the government (CFSG).

In 2017, IFAC, Chartered Institute of Public Finance and Accountancy (CIPFA) and the University of Science and Technology have conducted the survey on accounting basis and accounting documents of the Central/ Federal Government Entities of countries. Based on the result, a few countries that representing developing countries and more developed countries were selected as research objects in following common characteristics: i) government, ii) basis of accounting is transferred to accrual or accrual basis, iii) applying IPSAS in directly or indirectly to public sector accounting, and iv) representative of the region.

Regarding the results of the study on consolidated financial statements of the government of some countries, international common practice is avoiding combining the elements of financial statements of a legal entities that uses different accounting principles and accounting basis. In other words, a single set of consolidated financial statements of the legal entities with same accounting policies and principles are prepared.

Based on above mentioned survey, there is a challenge for the current methodology for preparing consolidated financial statements of the government of Mongolia. Therefore, it is important to change the policy decision for fully implementing IPSAS in public sector reporting.

Keywords: public entity, IFRS/IPSAS, consolidated financial statements of the government (CFSG), cash accounting, modified accrual accounting.

ONE. ADOPTION OF INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS (IPSASS) BY COUNTRIES AT THE INTERNATIONAL LEVELS

Government accounting practices are generally classified into four categories, moving from the least to the most sophisticated side of spectrum (PwC Global, July 2015):

Table 1. The spectrum of government accounting practices

Cash accounting	Modified cash accounting	Modified accrual accounting	Accrual accounting
Cash payments and receipts are recorded as they occur.	Cash receipts and disbursements committed in the budget year are recorded and reported until a specified period after year end.	Accrual accounting is used but certain classes of assets (e.g. fixed assets) or liabilities are not recognized.	Transactions and economic events are recorded and reported when they occur, regardless of when cash transactions occur.

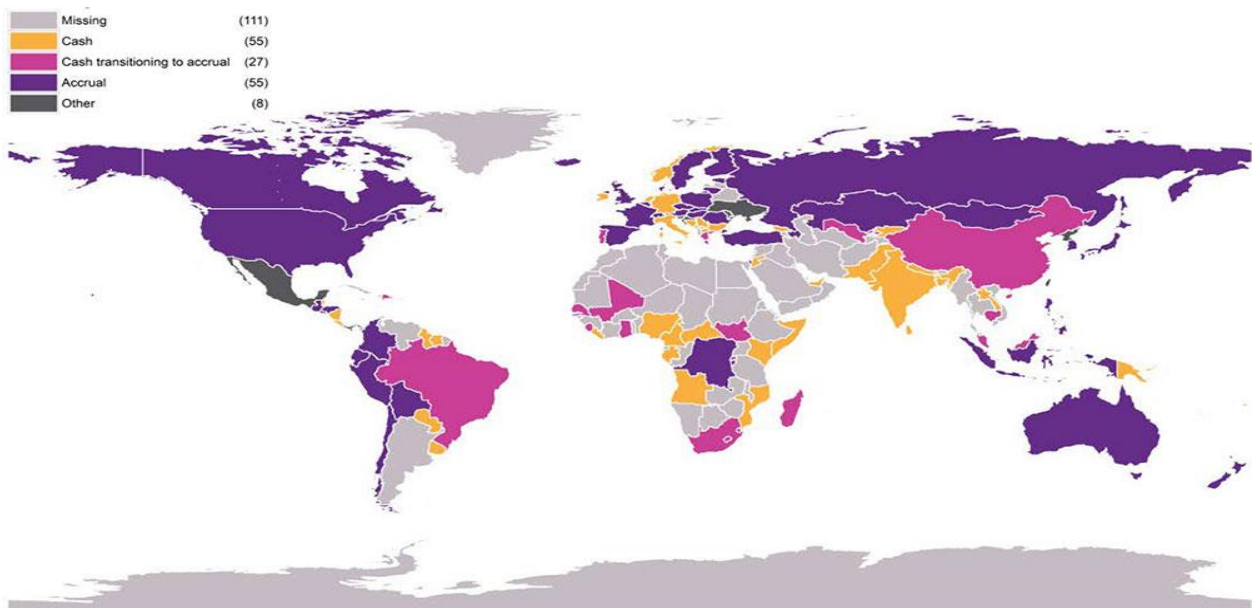
Classification in one of the four categories requires judgement and is inevitably somewhat subjective.

In 2017, IFAC, Chartered Institute of Public Finance and Accountancy (CIPFA) and the University of Science and Technology have conducted the survey on accounting basis and accounting documents of the Central/ Federal Government Entities of countries

The survey questionnaire was covered two main issues that are i) accounting basis and ii) financial reporting standards were/will be applied and in preparing the financial statements/reports for the Federal/Central Government for the most recently completed financial year.

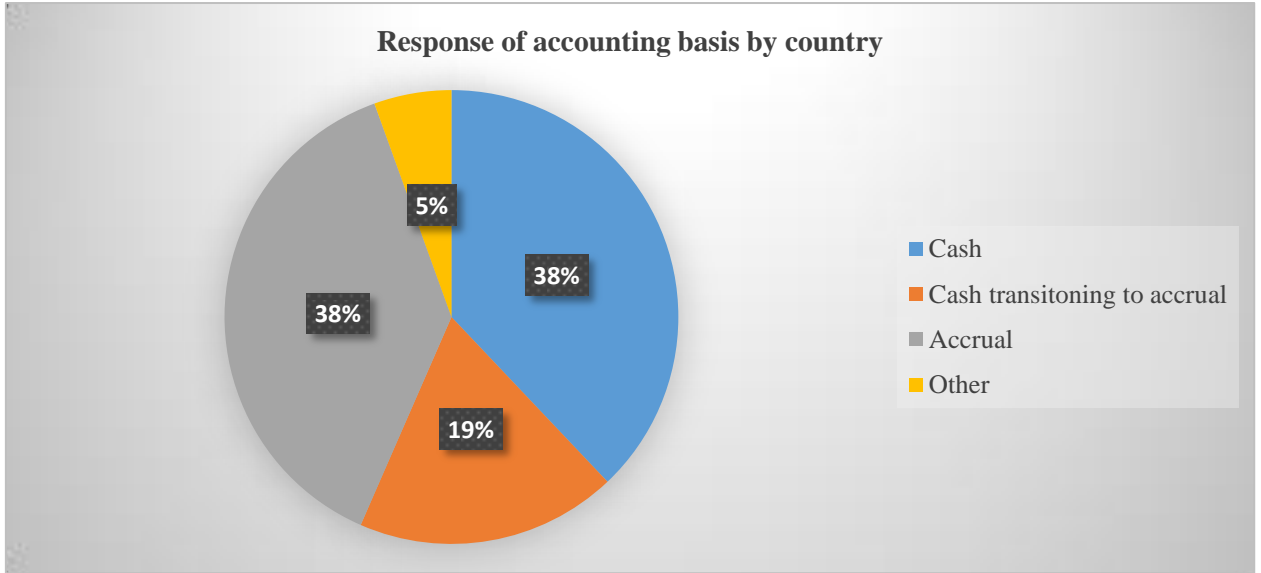
The following figures of 1 and 2 show that survey responses of accounting basis and financial reporting adoption by country.

Picture 1. Accounting basis by country



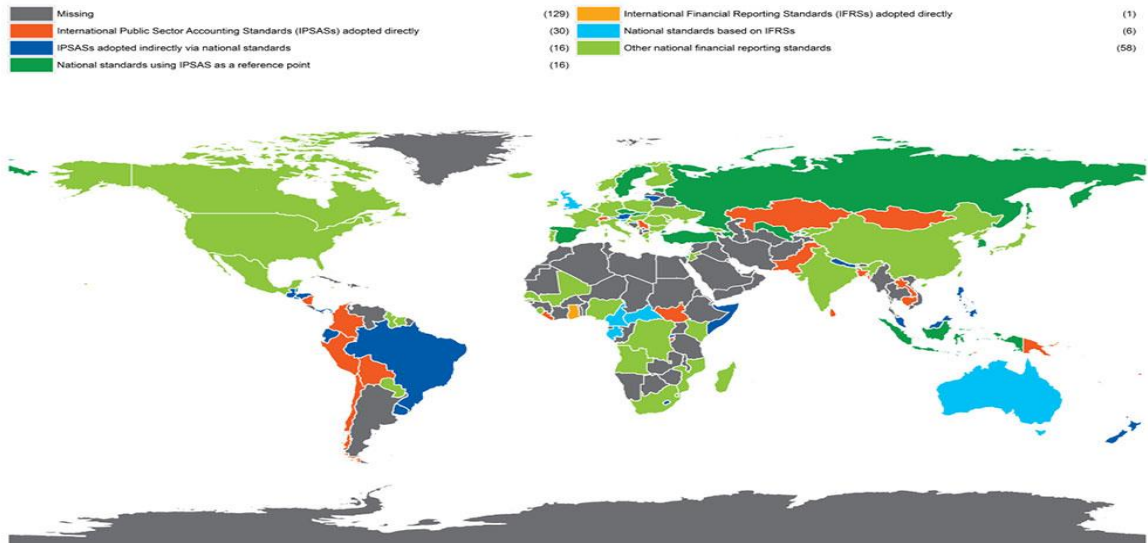
The following figure shows the response of questionnaire of accounting basis by country. Answers from Government of 145 countries were submitted to this issue. Here are the responses given below:

Figure 1 Survey result of accounting basis by country



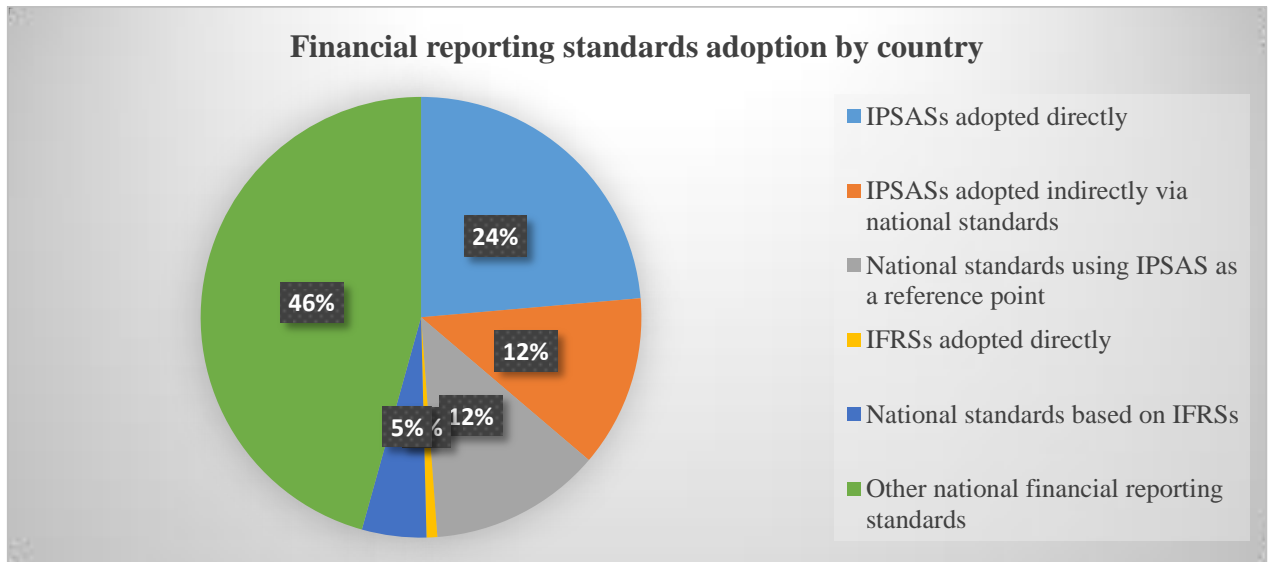
According to the above survey, if the countries that are moving from cash transitioning to accrual basis to accrual basis will be applied in consolidated financial statements of the government in the future, approximately 60% of the governments will report on its accrual basis.

Picture 2. Financial reporting standards adoption by country



Answers from Government of 127 countries were submitted to the 2nd issue. Here are the responses given below:

Figure 2 Survey result of financial reporting standards adoption by country



As a result of this surveys, IPSASs have been used in 62 countries as a direct or indirect.

Two. The study on consolidated financial statements of the Government (CFSG) by countries at the international level

Based on the results of the above research conducted the implementation status of IPSASs at the international level, we selected some countries (including The South Africa, Kazakhstan, China, Japan, Malaysia, Philippines, Russia and Portugal) from among the developing and more developed countries and Australia, United Kingdom, New Zealand and Serbia/Switzerland to represent the best international practice in a few common characteristics. The purpose of this international study is to compare the condition of Mongolia.

2.1 Selected rationale

The following indicators are based on the selection of countries. These include:

- Governance and administration are closely related to our country;
- The country's development level is similar or more developed to our country;
- Basis of accounting is transferred to accrual or accrual basis
- Applying IPSASs in any way to public sector accounting (directly or indirectly. See the Table 2)
- Representatives of the best regional practice, and
- Information availability

Table 2. Information from selected countries

№	Country	Region	Sub-region	Accounting basis	Financial reporting standards	Government
	Mongolia	Asia	Eastern Asia	Accrual	IPSASs adopted directly	Unitary semi-presidential republic
Selected countries as a research object (general):						
1	South Africa	Africa	Sub-Saharan Africa	Cash transitioning to accrual	Other national financial reporting standards	Unitary dominant party parliamentary constitutional republic
2	Kazakhstan	Asia	Central Asia	Accrual	IPSASs adopted directly	Unitary presidential constitutional republic
3	China	Asia	Eastern Asia	Cash transitioning to accrual	Other national financial reporting standards	Unitary one-party socialist republic
4	Japan	Asia	Eastern Asia	Accrual	Other national financial reporting standards	Unitary dominant party parliamentary constitutional monarchy
5	Malaysia	Asia	South-eastern Asia	Cash transitioning to accrual	IPSASs adopted indirectly via national standards	Federal parliamentary elective constitutional monarchy
6	Philippines	Asia	South-eastern Asia	Accrual	IPSASs adopted indirectly via national standards	Unitary presidential constitutional republic
7	Russia	Europe	Eastern Europe	Accrual	National standards using IPSAS as a reference point	Federal dominant party semi-presidential constitutional republic
8	Portugal	Europe	Southern Europe	Cash transitioning to accrual	Other national financial reporting standards	Unitary semi-presidential constitutional republic
Selected countries as a research object (the best practices):						
9	Australia	Oceania	Australia and New Zealand	Accrual	National standards based on IFRSs	Federal parliamentary constitutional monarchy
10	United Kingdom	Europe	Northern Europe	Accrual	National standards based on IFRSs	Unitary parliamentary constitutional monarchy
11	Switzerland	Europe	Western Europe	Accrual	IPSASs adopted directly	Federal semi-direct democracy under a multi-party parliamentary directorial republic
12	New Zealand	Oceania	Australia and New Zealand	Accrual	IPSASs adopted indirectly via national standards	Federal parliamentary constitutional monarchy

2.2 Legal entities included and excluded in the consolidated financial statements of the government (CFSG), their characteristics and the structure and content of the CFSG

Information on legal entities included and excluded in the CFSG, their characteristics and the structure and content of CFSG are summarized in the table below. These include:

Table 3. Summary information of CFSG from selected countries

№	Structure and content of CFSG	Methods used for preparing the CFSG
1	<p>South Africa</p> <p>Public Finance Management Act (PFMA) requires that the National Treasury (NT) preparing one set of consolidated annual financial statements (AFS) for national departments and public entities. Due to the significant different accounting bases being applied by departments and entities (modified cash and accrual), the Minister has allowed the NT to prepare separate sets of consolidated financial statements (CFS) for departments and public entities respectively. Consolidated AFS is included the following components of statements:</p> <ol style="list-style-type: none"> 1. Department's Consolidated Financial Statement (modified caash basis accounting) 2. Public Entities' Consolidated Financial Statements (accrual basis accounting) 3. National Revenue Fund's Financial Statements <p>The public entities that are consolidated also include unlisted public entities that are accountable to parliament.</p> <p>Notable exclusions: You can see the lists of entities not consolidated but included in the PFMA list from CFS's annexures</p>	<p>Consolidated financial statements of the government consist three statements comprising two separate set of consolidated statements for departments and public entities and National Revenue Fund's financial statement. Because the same accounting principles and policies do not apply, separate sets of consolidated financial statements are prepared by the National Treasury of Minister of Finance avoid the consolidating financial statement's elements in line by line. Method for consolidating line by line or equity method is selected and used for consolidation depending on the characteristic of the included entities in consolidated financial statements of the government and the accounting basis applied for the financial statements.</p>
2	<p>Japan</p> <p>A consolidated accounts for (Japanese Government Financial Statement, 2009):</p> <ol style="list-style-type: none"> 1. A general account 2. 18 special accounts of all the ministries <p>Notable exclusions: No additional information is provided.</p>	
3	<p>Malaysia</p> <p>The consolidated fund accounts including:</p> <ol style="list-style-type: none"> 1. Consolidated revenue account 2. Consolidated loan account 3. Consolidated trust account 	<p>The financial statements' elements of entities invested by the government ownership with voting rights (0.2-100%) other than the main bodies of the government are not consolidated line by line, but their investments are consolidated and reported in the CFSG.</p>
4	<p>Philippines</p> <p>A separate combined accounts for: (Annual Financial Report of Republic of the Philippines, 2016)</p>	<p>AFR for the GCs consists two set of volumes. The first volume is consolidated financial statements that covers</p>

	<p>Government owned or controlled corporations (GOCCs) include:</p> <ul style="list-style-type: none"> ▪ Government Financial Institutions (GFIs) and their subsidiaries ▪ Water Districts (WDs), <p>The Government Accountancy Sector prepares the Annual Financial Report (AFR) that covers financial condition and operation of the GOCCs, including GFIs and their subsidiaries, and WDs, collectively referred to as a Government Corporations (GCs).</p>	<p>entities concerned with the government corporations, and the second volume is consolidated financial statements of WDs.</p> <p>The two separate set of statements are prepared depending on different principles in accounting.</p>
5	Portugal	
	<p>Appropriation Statement shows the some following financial information with below categories. These include: (Annual Report, 2016/2017)</p> <ol style="list-style-type: none"> 1. Administration¹ 2. Legal and Governance² 3. Portfolio Management and Strategic Partnerships³ 	<p>There is no information about methodology for consolidation. But government financial statements show that some financial statements' elements of entities classified by each sector are consolidated.</p>
6	Australia	
	<p>Individual consolidated accounts for:</p> <ol style="list-style-type: none"> 1. Commonwealth (federal) government 2. Each of the six state and two territory governments (e.g New South Wales, Victoria) 3. All local government municipalities <p>Notable exclusions: No consolidation for the whole of Australia as a single entity</p>	<p>The country has own Board that approves the national standards. The CFSG is prepared according to the standard #1049 approved by the Board.</p>
7	United Kingdom	
	<p>A single set of consolidated accounts including: 1) Central government,</p> <ol style="list-style-type: none"> 2) All local governments and 3) Public corporations <p>Notable exclusions: i) Parliament, ii) National Audit Office⁴ iii) Nationalized banks</p>	<p>Accounting system is based on IFRSs.</p>
8	New Zealand	
	<p>Consolidated reports for:</p> <ol style="list-style-type: none"> 1. Central government (including Crown entities and state-owned enterprises) 2. All local government entities <p>Notable exclusions: Central government consolidation separate from local government.</p>	
9	Canada	
	<p>Individual consolidated accounts for:</p> <ol style="list-style-type: none"> 1. Federal government 2. Each of the 10 provincial and the three territorial governments (e.g Ontario, Yukon) 3. All local governments <p>Notable exclusions: No consolidation for the whole of Canada as a single entity. Government business enterprises (GBE) excluded</p>	<p>Combine like items of assets, liabilities, revenues and expenses in line by line. For this consolidation procedures, eliminate in full intra transactions and balances of relevant items. In some cases, there are adjustments for consolidation.</p>
10	Switzerland	
	<p>Generally, consolidation process is implemented as required in IPSASs because IPSASs are applied in public accounting sector.</p>	

¹ Including Ministry, Management, Corporate Services, Chief Financial Officer, Human Resources, Communications, Strategic Planning, Monitoring and Evaluation, Intergovernmental Relations, Internal Audit and Office Accommodation

² Including Management, Legal and Governance

³ Including Energy and Broadband Enterprises, Manufacturing Enterprises, Transport Enterprises, Economic Impact and Policy Alignment and Strategic Partnerships

⁴ Excluded to emphasis the importance of Parliament's role in holding government to account and hence it.

Three. Current situation of public sector accounting of Mongolia

The most recent IPSASs were issued in 2018 and a total of 40 standards. IPSAS 1-4, 6, 9, 12-13, 17 and 31 have been fully and partially applied according to a research conducted on accounting guidelines and regulations approved by Minister of Finance among accountants of budget entities

and GBGs. Public sector entities applied accounting guidelines and regulations approved by Minister of Finance rather than directly adopting IPSAS. (Bolormaa.B, 2018)

It is one of the investors' requirement that the CFSG of Mongolia should be comply with the international standards. Accountants of public sector entities only use the accounting standards in Mongolian. Therefore, the MOF is going to translate the IPSAS as at 2018 funding by World Bank and to introduce the translated IPSAS to the public within 2019. Also, the MOF will train the trainers of IPSAS, strength the capacity of accountants of budget entities about accounting standards through the trainers and develop the regulations and guidelines of public sector accounting and CFSG compliance with IPSAS from 2019 to 2021. Also, ADB will apply accrual-based financial reporting for ADB-financed projects from 2nd quarter of 2019.

However, the researchers confirmed that the accounting guidelines and regulations are based on modified accrual basis and have not been revised since 2007.

The purpose of identifying the current situation and challenges in public sector accounting and consolidated reporting of the government (including the implementation of the guidelines in preparing the CFSG, how well the policy approach is being used, its practical application and difficult in consolidated reporting, the software used by the entity, how well they are compatible with software of other authorities, and the need to improve of the consolidation process in public sector) in practice related to prepare the CFSGs and the CFSG, we conducted at two main surveys follow as:

- I. Review of documents relating to the preparation of consolidated financial statements of the public sector
- II. Current practice of methodology of consolidation process in public sector
 - a. Interview with 41 staffs of 32 organizations (comprising 26 General Budget Governors (GBGs), one Central Budget Governor (CBG), two Direct Budget Governors (DBGs), three projects/ funds and an audit firm) from 29 June, 2018 to 16 August 2018.
 - b. Questionnaires were prepared in 3 types such as for i) GBGs and CBGs, ii) DBGs, and iii) SOEs and LOEs. As a result, 18 of 18 SOEs and LOEs, 10 of 54 GBGs, and 21 of 21 CBGs, 18 DBG submitted the questionnaires between 13-17 August, 2018.

Currently, the financial statements' elements of legal entities included in CFSG are combined line by line and reported. These are:

Table 4. Some information about applicable regulations of the preparation of CFSG

№	Type of legal entity	Accounting standards	Approved order	Notes
1	Budget entity	IPSASs	Order #388 of the Minister of Finance	Accounting guidelines and regulations are applied in financial statements and approved financial statements' templates
2	Treasury fund	IPSASs	Order #171 of the Minister of Finance	
3	Project and fund	IPSASs	Order #326 of the Minister of Finance	
4	State-owned	IFRSs	Depending on the type of state-owned entities,	

	entity	<p>the following orders are in force:</p> <ul style="list-style-type: none"> ▪ Joint order #A-294/340 of the Minister of Finance and President of Bank of Mongolia (for banks) ▪ Order #361 of the Minister of Finance (for entities) ▪ Order #386 of the Minister of Finance (for NGOs) 	of those entities are different from each other.
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Regulation for preparing the financial statements of the budgetary entities was approved by Order #388 of the Minister of Finance in 2006 that has been developed in accordance with IPSASs as of 2005. The line items of the financial statements are not consistent with each other and financial statements' formats are different because of differences in timing of the regulations for consolidated financial statements and budgetary entities and the newly accounting standards have not been included in these regulations. It creates uncertainty about whether or not to merge or split any of the line items because the line items and classifications contained in these regulations have not been provide any criteria and definitions.

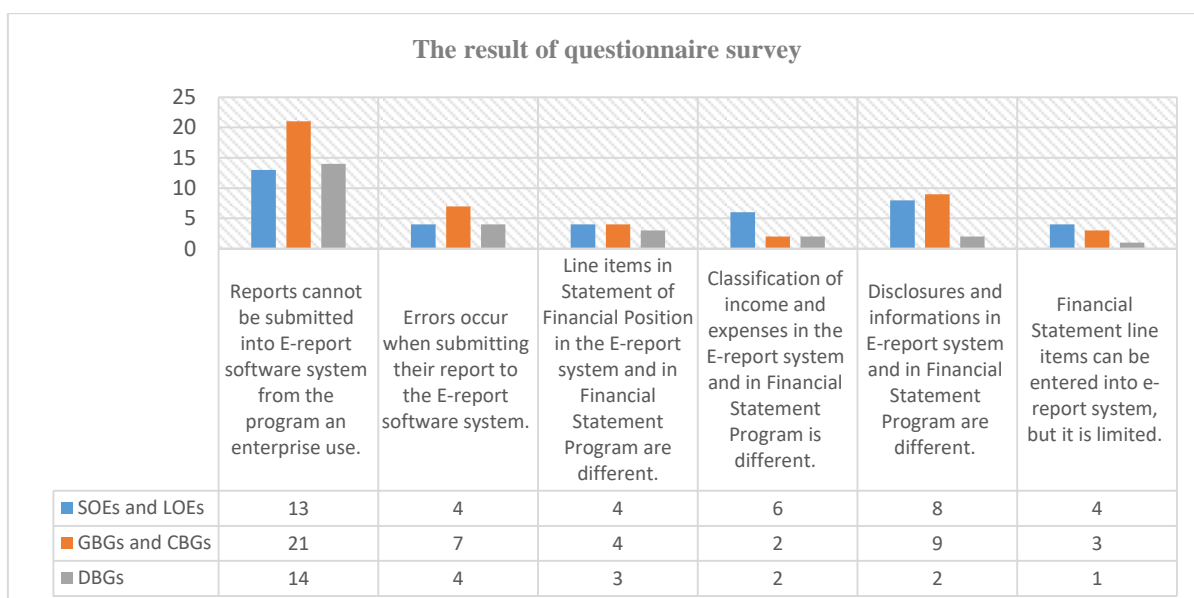
Fully and partially SOEs and LOEs comply IFRS according to the Law on Accounting, it is still theoretical and methodological problem that how to consolidate SOEs into the CFSG. There are common issues related to elimination entries for CFSG and accounting on consolidation. Such as, i) only the balance sheet and transactions generated between the Treasury and GBGs and CBGs are fully eliminated in consolidated reporting. But the balance sheet and transactions generated between the budget entity, project/fund and SOEs are not eliminated ii) for local GBGs, duplication of transactions between provinces and soums or inter-soums is not eliminated.

It is impossible to get information and conduct research from the financial statements of the SOEs according to the financial reporting form in compliance with IFRS as stated in Article 4.1.1 of the Law on Accounting. Those entities are incorporated in CFSGGBGs as stated in article 54.2 of Law on Budget. Therefore, there is necessity to convert financial statements of the SOEs to E-Report system with financial reporting form for public sector.

Accountants face difficulties because the software used for its own activity, other software systems (including E-Report, Freebalance, and Fiscal that used in Treasury and Fiscal Policy and Planning Departments at MOF) require different types of information input. It shows there is no unified policy from the government body and no integration system of those information submitted to the above mentioned soft wares. Therefore, MOF should require and monitor regularly software companies to develop continuously their programs based on the changes of the accounting standards followed by financial reports, instructions from orders by MOF, and E-Report documentaion changes.

Followings are the answers to the questions related to some difficulties between Financial Statement Program and E-report software system:

Figure 3 The result of questionnaire survey



Source: Researchers' survey

According to the main survey result, there is no chance for SOEs, LOEs, GBGs, CBGs, and DBGs to download their financial statement to the E-report software system automatically.

Four. Conclusion

1. Regarding the results of the study on consolidated financial statements of the government of some countries, international common practice is avoided the combining the financial statements' elements of a legal entity that uses different accounting principles and basis in line by line.
2. Instead of that, the content, scope and structure of the consolidated financial statements are vary between them depending on the type of legal entities and government bodies involved in consolidated financial statements of the government by combining the financial results of legal entities that use the same accounting policies and principles and preparing a single set of consolidated financial statements. For countries covered by this study, the appropriate accounting methodologies (e.g. method for combining line by line, equity method) for consolidation process are selected and used depending on legal entities and government bodies included in consolidated financial statements.
3. It is reducing the opportunities of realistic and accurate representation of financial results because of combining financial statements of SOEs with more than 90% in line by line and there is no consolidation for SOEs with less than 90% in CFSG of Mongolia. Therefore, it is important to change the policy decision for fully implementing IPSAS in public sector reporting.

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