

## **Holding Governments Accountable: Fiscal Sustainability and Stewardship Reporting for Citizens**

### **Abstract**

Citizens of countries patterned strongly after the modernizing nation-state live in a wholly monetized economy. Their economic security depends on the fiscal sustainability of their state and the economy it regulates. To hold politicians accountable, voters need reliable information on the state's finances. The search for the rules and principles which shape such information leads to the critical domain of accounting where economics and law meet. Fiscal crises world-wide show that this mundane instrument to measure fiscal sustainability is ignored.

We argue that enough is known about the limits of the nation-state as a body-politic pattern to make good public sector accounting one of the great progressive causes of the 21st century. Pursuit of the goal of fiscal transparency, through use of accruals-based financial statements that comply with high quality standards such as the International Public Sector Accounting Standards (IPSAS), leads neither to socialist Leviathan nor to an unsustainable libertarianism based on outmoded tenants of economic thought. It leads to an ideal of responsible stewardship of resources both public and private.

In this paper we outline a regime of fiscal transparency, drawing in part on our experience as participants in New Zealand in the transition of a quasi-socialist state ('a mixed economy') to a more open market economy and a commitment to such a regime. We then discuss progress towards fiscal transparency in nine Eastern European countries.

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## **Holding Governments Accountable:**

### **Fiscal Sustainability and Stewardship Reporting for Citizens**

Gwenda R. Jensen and John Francis Stuart

#### **1—Introduction**

##### 1.1 Good Public Sector Accounting—A Progressive Cause for Today

Most citizens in a modernizing nation-state live within a wholly monetized economy. Their economic security depends on the fiscal sustainability of their state and the economy it regulates. To hold politicians accountable, citizens need trustworthy information on their state's finances. Such information can only be found in the domain of accounting where economics and law meet. All around the world, from the Greek crisis to the situation in Venezuela, from the United States (US) debt ceiling to the claims about money flows which formed part of the British Brexit debate, politicians have tried to ignore, with uniformly negative results, the mundane instruments which make visible the nation-state as a financial going concern.

We argue that enough is known about the limits of the modernizing nation-state as a body-politic pattern to make good public sector accounting a progressive cause today. Effective public administration needs reliable accounting standards to monitor progress towards fiscally sustainable public interest goals. These goals include the ratio of government debt to Gross Domestic Product (GDP), the regulation of monetary policy to restrain inflation, the creation of sovereign wealth funds, the provision of dependable public security, education, and pensions, and public investment in infrastructure.

Pursuing fiscal transparency leads neither to a socialist Leviathan nor an unsustainable libertarianism based on outmoded tenets of economic thought. It leads to the pursuit of responsible stewardship of both public and private resources. The achievement of fiscal transparency depends on specific mechanisms, such as accruals-based financial statements, that comply with high quality standards, such as the International Public Sector Accounting Standards (IPSAS).

## 1.2 Background and Orientation: The New Zealand Experience

The authors grew up in a country mired in fiscal crisis and suffering from an inability to hold its government properly accountable for management of the public purse. In the 1970s New Zealand, a primary producing country, began to suffer from unfavorable terms of trade and falling commodity prices. The efforts of central government to manage the situation brought to light serious shortcomings in public sector management. Eventually, in the mid 1980s, after significant policy failure led to a crisis of confidence in the ruling party, there was a change of regime and the nation was led down a path of economic liberalization and restructuring. Integral to this change was reconsideration of the management framework for the public sector. A new framework, put in place piecemeal, addressed state fiscal transparency, monetary stability and the management of inflation, and accrual accounting in the government sector, as well as adoption of full consolidation on the government balance sheet. Both authors worked in New Zealand's public sector during this transformation and witnessed at first hand the effects of these changes.

Barry Gustafson, *His Way: A Biography of Robert Muldoon*, presents a helpful overview of the New Zealand economy's crisis and the government's inability to respond effectively. (Robert Muldoon was Minister of Finance from 1967 to 1972 and Prime Minister from 1976 to 1984.) Jonathan Boston et al, *Reshaping the State: New Zealand's Bureaucratic Revolution* (1991) describes the massive reforms to New Zealand's public administration in the 1980s, updated by the same authors in *Public Sector Management: the New Zealand Model* (1996). A deeper insight is provided by Graham and Susan Butterworth, *Reforming Education: the New Zealand Experience 1984-1996* (1998), which shows the interplay between financial information and stewardship in a public policy area of direct concern to the majority of citizens.

## 1.3 The Structure of this Paper

In the next section we outline the structural rationale for fiscal transparency, focusing on (1) a working model of the nation-state, (2) the desideratum of fiscal transparency, and (3) the growth of expectations for public sector information (particularly accounting standards) which have continued to lag behind events. Having thus set the scene we will

conclude Section 2 with a look at some critical issues which continue to recur within the modernizing nation-state. Then in Section 3 we will (1) discuss current progress towards fiscal transparency in a selection of former communist countries, and (2) consider comparisons with reference to some high GDP European Union (EU) states. The final section draws some conclusions.

## **2—The Structural Rational for Fiscal Transparency**

### 2.1 An Idealized Cognitive Model of the Nation-State

An idealized cognitive model (ICM) is a functional not a metaphysical construct. It is an effort to describe the gestalt properties of an ecological structure. It does not presuppose an eternal Platonic archetype. An ICM accepts a certain imprecision in the interests of functionality and the existence of other, at times overlapping, ICMs.

The ICM outlined below relies on ideas explicated in John H. Jensen's *the Origins of Nation Building*, which the second author of this paper has been editing for publication. Our ICM of the nation-state may be summed up (with apologies to Le Corbusier) as 'a machine for living in'<sup>1</sup>. In this machine the state is the cockpit through which the nation is guided to its destination. This metaphor deliberately emphasizes both pertinent information and professional responsibility.

As a machine for living in the nation-state is:

- A physical entity legally defined and subsisting as a set of:
  - reciprocal parts—state, people, institutions and processes;
  - intricate linkages—society, economy, government;
  - overlapping centers and peripheries, bureaucracy, academy, NGOs etc.

Within the ethos of modernity these elements have given rise to the 'society of organizations.' As Peter Drucker, who coined this expression, puts it, 'the function of organization is to make knowledge productive,' (Drucker, 1993). Therefore, one way to measure the capacity of a modern nation is the extent to which each major social function

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<sup>1</sup> What Le Corbusier actually said was, 'Une maison est une machine-à-habiter,' in *Vers une architecture*.

is placed in the care of a dedicated institution, which acts as an instrument of innovation. The growth of government bureaucracy in the modern age is due to the need to make knowledge productive.

The ‘ethos of modernity,’ originating in the American and French revolutions, is summed up in the claim that the nation-state exists to effect rational improvement in the human condition. In concrete terms the source, goal, and path of any public improvement project may vary. So individual projects may impact one upon another. There need not, however, be a radical opposition between people and state nor a form of idealized union. But we suggest that a good relationship between people and state should at least be symbiotic.

The most important aspect of modernity is its drive for continuous improvement. No state of rest within some once-and-for-all configuration of elements is desired. Thus, we speak of the *modernizing* nation-state, which emphasizes the state’s ongoing mission as the prime sponsor of the *processes* of continuous improvement. These processes play out in different parts of the nation and constitute much of its politics at any one time.

Some commentators have said that the European world of the 1800s had a general ‘belief in progress’, which was destroyed in the carnage of the First World War. But what existed as a widespread supposition in the 1800s was that the social problem (i.e. the basis of class war between the haves and the have-nots) could be eliminated by material progress, if everybody’s life improved. This supposition proved correct in many parts of the world during the 20<sup>th</sup> century. It was also assumed that the state could not expand beyond a certain limit; that its functions were severely limited, given lack of capacity and reasons to expand.

But the First World War required both extensive innovation in organization and intensive resource mobilization. It obliged states to innovate in many areas—health, education, military resources, finance—simultaneously. It also obliged states to effectively conscript wealth. Thus, in the course of the 20<sup>th</sup> century, *innovation* ‘purposeful, directed, organized change’ (Drucker, 1957) replaced ‘inevitable progress.’

In contemporary debates there is a recognition that countries variably imprint on the 'machine for living in' model. Thus, countries can be ranked according to:

- the rule of law and the extent of internal security; (passenger safety)
- the successful co-ordination and/or subordination of the parts to the whole; (everything is working smoothly according to specifications)
- the strength and function of the linkages between elements; (telemetry is good)
- the capacities and co-operation between different centers and peripheries, especially in terms of hierarchies and partnerships;(communication with ground control is clear, cabin crew are trained and ready)
- the source, path, and goal of improvement projects; (our new airbus features...)

In view of the contemporary habit of international country rankings we emphasize that we are not trying to present a simplistic, value-laden checklist view of the nation-state. Ideological bundling of the above elements, whether in some variant of the Washington consensus or, at the other extreme, state capitalism, or simple chauvinism, brings in too much that is extraneous and merely associative. It is inimical to good research and citizenship because it is far too shallow.

The issue we are focused on here is:—What are the information systems within the machine? What is the data used by the pilots? Is it available to the passengers? And can they use that data to hold the pilots accountable?

The ICM we employ is frankly instrumental in contrast to many idealized cognitive models of the nation-state which focus on the human element through an essentially psychological approach. Current research on the nation-state is awash with papers analyzing identity politics, the recruitment and deployment of partisans of this or that meta-narrative, or the rhetoric of state action at the international level. While hardly surprising given recent events, the employment of such models misses critical elements of the situation. True, psychological based models can add value, because states are run by human beings of different personalities, temperaments, capacities, and cultures, but they often fail to show us what is technically possible for good policies. For example, democracy owes a good deal to the pragmatic rules and procedures for voting—the use of

ballot papers, transparent ballot boxes, independent observers, trained polling station staff, secure voting booths, sensible rules around voter identification, and whether the election day is a holiday or a working day. Attention to these elements does not imply neglect of the human factor.

So, we do not claim that our model is exhaustive of the phenomena of nationalism. We simply note that the utility of any ICM of the nation is directly proportional to the range of its policy implications. Once founded, with membership and territory defined, a nation must be managed, and its administration must be adequate to its perpetuation. Our concern therefore is with the nation-state as a going concern, as a kind of publically owned business.

## 2.2 Public Administration Issues and Appearance of the Fiscal State

Different eras since the French revolution have been obsessed with different indices of national well being. In the clash between *Les droits de l'homme et du citoyen* and the power of Europe's dynastic states the indices were constitutions, conscription, and the extension of the franchise. In the industrial revolution the popular indices, among European statesmen and advocates of national aggrandizement, were coal and steel consumption. In the era of economic development, which became popular after the Second World War, the preferred indices were statistics on infant mortality, school enrolment, and national rates of literacy.

Now, in the world-wide age of management, we are concerned about the money.

Since the First World War, the state has become the fiscal state and learned that:— property can be subordinate to politics, money supply and taxation are more elastic than classical economics supposed, resources can be inventoried, tagged and reconfigured. And all these aspects of public management can be 'weaponized.'

Socially the rise of the fiscal state has been abetted by population movement to urban areas and the urbanite's reliance on monetary exchange in order to live. In the 20<sup>th</sup> century urbanization has occurred irrespective of whether the governing regime has been capitalist, communist, or something in between. And within the terms of a wholly

monetized economy the state alone controls the means of life and so has the power, actual or latent, to touch virtually every urban denizen.

Contemporary state control of the money supply has become a complex business encompassing regulation of the banking sector, issuance of currency and government bonds, oversight of the rate of inflation, and determination of the scope and incidence of taxation. There is now a significant literature on these matters but for the ordinary citizen its impacts are assessed primarily in terms of education, employment and income opportunities, personal debt burden and the capacity to save, the local cost of living, and the risks attendant on ill health, old age, and the incidence of crime.

Today we can point to countries around the world where these things are in crisis. In Venezuela the government has largely switched off its indicator panel, so pertinent information about the state of the state is hard to come by. In Argentina the rate of inflation is near 40% and the government struggles to restore credibility to its department of statistics which only a few years ago doctored the numbers on the inflation rate. In Zimbabwe citizens use the American dollar as well as other currencies to enjoy some price stability. Lest we think these crises an entirely exotic affair we should recall the 2008 banking crisis and its aftermath, the example of Greece, and the current Italian budget crisis.

We have been here before. Hyperinflation occurred in most of the countries defeated in World War One. The first extensive experiment in deficit financing occurred in Germany between the wars when the United States lent Germany the money to buy American goods. Each generation since the First World War offers examples of the problems of the fiscal state. In the 1960s and 1970s inflation was a problem. In the 1980s there was a sovereign debt crisis in Latin America and Eastern Europe, a crisis which hastened the end of communism in Europe. These experiences are matched by muted instances of the same phenomenon in many countries small and great. They point to a generic—the limits within the ecology of the nation-state of:

- taxation as a portion of state income;
- the money supply and inflationary risk; and,

- the level of sovereign debt.

While there is no precise knowledge on these matters, we do know that there are limits to:

- how much a national government can tax its way into solvency;
- the state's capacity to print money to solve its problems; and
- how much a state can borrow from abroad to address its needs.

Our knowledge of these limits is largely the fruit of much bitter experience arising when the signs of the problem of limits are ignored. For that reason, a great deal of contemporary attention in the pages of investment journals is devoted to monitoring these matters, for investors do not like to lose money. Such journalistic attention presupposes the nation-state as a going concern, a form of business owned by its citizens but trading, in one way or another, with the rest of the world as an entity which can be relied on to keep its word, pay its debts, and safeguard the property and lives of those who live in it.

### 2.3 Fiscal Transparency: Growing Expectations

For investors it is unsurprising that public sector accounting standards have begun to take center stage, for if wealth has not been well defined it cannot be transferred, allocated, or relied upon. The communist experiment taught us that policy and regulation must take note of basic economic principles as well as basic democratic ones. Recent experience has also reminded us that we cannot make economic principles work for everyone in the absence of an intelligent legislative and policy framework. If the legal instruments used to define and store wealth, describe and exchange value, define and regulate transactions, and establish and maintain probity in economic affairs are not regulated then citizens are not supported by their state either as consumers or producers.

When Alexander Hamilton, the first Treasury Secretary of the new United States, studied public finance the subject was called 'political arithmetic.' State housekeeping was only gradually distinguished from the domestic management of the estate of the prince as the discipline of economics developed. And for a long time, it was assumed that the 'state of the realm' could take care of itself (*Laissez faire!*). We do not propose to trace the

evolution of financial theory here, but we do think there is a need to appreciate how comparatively recent its development has been.

A significant part of the development of public finance has been the creation of a body of statistical material from which reliable inferences can be made. But creation of reliable statistics is in itself a slow and difficult business. The index of GDP was not invented until just before the Second World War and did not come into widespread use until after 1945. Although GDP was supposed to facilitate international comparisons the national accounting systems which underlay any particular instance of it were not uniform and often did not reflect the same principles. The creation of International Public Sector Accounting Standards (IPSAS) only occurred in the late 1990s when a former Chief Accountant of the New Zealand Treasury convinced the International Federation of Accountants (IFAC) that it should sponsor their development, thereby transforming IFAC's Public Sector Committee into the International Public Sector Accounting Standards Board (IPSASB). (Jensen and Smith, 2013).

At the time of writing the situation has certainly improved. The first author of this paper was instrumental in moving the United Nations family of organizations onto IPSAS. This change facilitated organizational autonomy, donor confidence, and management effectiveness for those organizations. But among national governments only a small number have adopted IPSAS completely, while many have declared their intention to adopt and made some progress along the way. Full adopters include Switzerland, Austria, Estonia, as well as New Zealand, and the Vatican.

## 2.4 Researching the Fiscal State

### *2.4.1 Introduction*

The headlines proclaim the gross policy failures. Ideally, we should like to avoid being a citizen in a country experiencing hyper-inflation, a banking crisis, high crime levels, or a significant and protracted rise in the cost of living. But how does the ordinary citizen assess more subtle state behavior impacting the health of the fiscal state she is a member of?

This might appear to be a naïve question. Are we not living in an information age? Does not every government have a dedicated web site on which can be found all the information necessary to answer any reasonable question a citizen might ask?

It is certainly true that in many countries, particularly former communist countries, the quality of basic data has become more reliable in the past three decades. But this does not mean that answers to difficult, time dependent, questions are easily found, even when they happen to have some sort of answer for the time being.

#### *2.4.2 Researching the Fiscal State: An Example*

For example, what happens if the citizen asks: *Can the government of my country afford to pay me a pension when I am old?*

Where and how would she find the answer to this question?

Most likely the citizen would turn to the ministry responsible for the administration of old age pensions. She will likely find on that ministry's website a good deal of material about what the current national pension system is, how it is organized, along with what is required to make an application, as well as downloadable forms and a 'list of frequently asked questions.' That same website might possibly provide actuarial reports, demographic forecasts, and possibly even some sense of the financing of the national pension system in the short to medium term. But, except within the reports of an independent government pension fund with some form of specific trustee obligations, the ordinary citizen is not likely to find direct statements about the long term financial viability of any scheme.

Former communist countries in Europe have had, like many other countries, to grapple with changes to state pension arrangements consequent on government fiscal weakness, increased demand due to extensions to the average lifespan, and the need to adjust pension rates to address changes in the cost of living. In many places the solution has been to reform the pension regime by increasing the age of retirement, encouraging or mandating the uptake of private pension scheme plans, and (in some cases) the establishment of a stand alone national pension fund. Governments hope that this configuration will suffice to support retirees no longer working. All this change has no

doubt generated much public debate, a lot of reports, and a fair quantity of data. None of that material answers the question as raised.

The argument here is not about the detail of pension arrangements in any one country. The question is: what sort of information is provided on the long term fiscal sustainability of any national pension structure? And how easily accessible is that information?

Implicit in any research on this question is the distinction between data and information. This distinction does not lie in the content of a given item; it lies in the relationship of that item to the required decision. Information is the answer to a question asked. Typically, the most difficult decisions exist in relation to the time required for their fruition. It is precisely on these that good information is hard to get. True, this is a perennial human problem. But, in the age of the fiscal state, neither states nor citizens are in a position to act blindly on critical issues.

#### *2.4.3 Researching the Fiscal State—The Current Lack of Transparency*

The contemporary lack of transparency becomes obvious when we ask other valid citizen questions which involve the intersection of time, money, and risk:

- Can my country provide a decent and affordable education?
- Can my country provide a decent and affordable health care service?
- Can my country employ its resident, skilled working age population?
- Can my country employ its resident savings productively?

Each of these questions has become a major area of public policy debate because each now involves the intersection of significant time, money, and risk for the citizen. A hundred years ago, and in some places only fifty years ago, this was not the case.

Today, education is a major capital investment which only begins to pay off in early middle age. Fifty years ago, outside of the United States, education meant schooling which ended around the age of seventeen, if not earlier. Health care is now a major contingent liability which must be constantly balanced against public health needs and private choices. (The recent measles outbreak in the United States exemplifies this.) Fifty

years ago it was largely assumed, even in the United States, that addressing the environmental causes of disease—lack of clean water, a functioning sewage system, immunization etc.—had broken the hold of disease on humanity. Now the economic impact of income and productivity foregone from health issues is a major concern in all nations. Employment represents an ongoing commitment and becomes a constantly renewed arena of conflicting policy agendas as the configuration of a national economy changes over time. Fifty years ago this dynamic was essentially a function of the industrial system. Professionals were supposed to be beyond its reach. Today the most intractable ‘industrial’ issues in North America and Europe are found in the professions. In these the majority of individuals will experience changes to their only major source of income and may have to bear much of the risk of those changes themselves. This hardly makes for ‘industrial’ peace. For the fiscal state employment policy also becomes a headache. Every government has to collect tax revenue from incomes and regulate work so as to at least be able to manage its tax collection and social welfare responsibilities, however minimal. Finally, the question of whether income saved, or consumption deferred, can find a return in-country becomes a significant issue for the financing of business activity and innovation, and the decision of the citizen to save at all.

#### *2.4.4 Researching the Fiscal State—Using Accountancy*

Accounting was first developed to help manage the interplay of time, money and risk. But where once this was mainly the private concern of the trader or merchant working in a very limited and controlled way within or beyond the borders of the kingdom in which he was a subject, it is now the critical concern of the employee-citizen. The contemporary knowledge worker or employee cannot be productive alone. She can only be productive within an organized setting. But the establishment of organization, within which knowledge can be made productive, whether by government or voluntary or private enterprise, involves real costs. And, in view of such costs, new institutional arrangements will not be set up unless the benefits of their creation promise to exceed the costs. But on this question: do the benefits of their creation promise to exceed the costs, we can have no reasonable opinion without the appropriate financial data. And we cannot possibly hope to get this data unless we press into service the discipline of accountancy.

### **3 Progress Towards Fiscal Transparency—Country Examples**

#### **3.1 Nine Former Communist Countries**

We consider nine countries: Croatia, the Czech Republic, Estonia, Hungary, Poland, Romania, Serbia, Slovakia, and Slovenia and compare these to the four European Union (EU) countries with the highest nominal GDP: Germany, the United Kingdom (UK), France and Italy.

The region from which these countries are selected is historically under-represented in terms of IPSASB membership, meetings, and outreach. Since its inception in 1996 the IPSASB has had no members representing the government of a former communist country, though there has been a public interest member from Romania. Only two of the 60 plus IPSASB meetings to date have been hosted in a former communist country—one in Zagreb in 2001 and one in Moscow in 2008. In 2019 a representative from the Polish Ministry of Finance became a member of IPSASB’s Consultative Advisory Group. By contrast, the IPSASB’s history of membership, meeting locations, and outreach shows extensive participation by countries such as Austria, France, Italy, Switzerland, and the United Kingdom, as well as on-going representation from African, North American, Latin-American, and Asian-Pacific countries.

#### **3.2 The IMF and Fiscal Transparency Monitoring**

Subject to the caveats set out below, International Monetary Fund (IMF) reports are the logical starting point for assessment of a government’ fiscal transparency, given the IMF’s work to operationalize the meaning of the term. The IMF defines fiscal transparency as ‘the comprehensiveness, clarity, reliability, timeliness, and relevance of public reporting on the past, present, and future state of public finances.’ (IMF 2014)

The IMF took the lead in the pursuit of fiscal transparency, beginning with its first *Code of Good Practices on Fiscal Transparency* (the Code) published in 1998. The IMF uses the Code to review countries’ fiscal reporting practices. By the end of 2006 the IMF had reviewed around half of its member countries resulting in country-specific *Reports on the Observance of Standards and Codes* (ROSCs).

After a lull the IMF decided to revise the Code and its approach to fiscal transparency standards (IMF 2012 and Heald 2013). The IMF issued a revised Code in 2014 and the ROSC-*Fiscal Transparency Module* reviews have been replaced with what the IMF calls *Fiscal Transparency Evaluations* (FTEs). The most recent version of the Code is dated 2019 (IMF 2019). The IMF has also issued a *Fiscal Transparency Handbook* (2018), to accompany the Code, and a *Guide on Resource Revenue Transparency* (2007), which is expected to be replaced by Volume 2 of the Code towards the end of 2019.

The 2014 Code sets out four principles:

1. Fiscal reports should provide a comprehensive, relevant, timely, and reliable overview of a government's financial position and performance.
2. Budgets and their underlying forecasts should provide a clear statement of a government's budgetary objectives and policy intentions, and comprehensive, timely, and credible projections of the likely evolution of public finances.
3. Governments should disclose, analyze, and manage risks to the public finances and ensure effective coordination of fiscal decision-making across the public sector.
4. Government revenues from natural resource exploration and extraction activity should be collected, managed, and disbursed in an open and transparent manner.

The Code lists specifics to achieve for each principle, with a table summarizing what is to be assessed as 'basic,' 'good,' and 'advanced' in practice. For example, '1.1.2 Coverage of Stocks' states that, 'reports should include a balance sheet of public assets, liabilities, and net worth.' 'Good' practice requires governments to fully report financial assets and liabilities, while 'advanced' practice requires application of accruals financial reporting standards to prepare a government's balance sheet.

The Code's statements around this one point (coverage of stocks) illustrates that the IMF's expectations need to evolve further. Private sector *minimum* expectations for a reporting entity are those the Code describes as 'advanced,' while what the IMF describes as 'good,' would be viewed as laughably inadequate for a private sector entity. Given the

role that government plays in the economy and the essential nature of the services it provides, it seems reasonable to ask why expectations for government financial reporting are so much lower than the standards governments themselves require of other entities—both the private sector entities that they regulate and the international organizations that they fund.

### 3.3 Governments' Support for Accruals Accounting and IPSAS

International organizations such as the OECD, the UN family of organizations, NATO, and the European Commission have adopted accruals financial reporting and IPSAS, with most changing during the period 2000-2016. Member States fully supported (indeed insisted on) these changes, which they described as best management practice necessary for international organizations' accountability and transparency.

Fiscal transparency is viewed as crucial for the functioning of the EU's multilateral budgetary surveillance framework and the function of the single market (Müller-Marqués Berger 2016; Mussari 2014). Eurostat's *European Public Sector Accounting Standards* (EPSAS) project had its beginnings in the need for accounting reform and harmonization highlighted by the sovereign debt crisis (Müller-Marqués Berger, 2016). The European Commission appreciates that without a harmonized accrual-based system there can be no real transparency of EU Member States' financial position and performance. Government finance statistics (GFS) are unreliable when the information system used to generate them is incapable of preparing accruals-basis financial statements. That is the case whether GFS reports are prepared for Greece or Germany. From a fiscal transparency perspective, the two countries differ only to the extent that one has been shaken by economic shocks that have exposed the inadequacy of its financial management while the other has not.

IPSAS provides the best support for achievement of the fiscal transparency principles defined in the IMF Code. IPSAS has rigorous and comprehensive requirements for identification and measurement of revenue, expenses, assets, resources, rights, obligations, and liabilities. IPSAS is also the only set of *international* standards applicable to governments. Only by using IPSAS can a national government claim to be applying standards that facilitate international comparisons.

Some countries, such as the UK, have adapted International Financial Reporting Standards (IFRS) for their public sector. The adaptation process has two defects. First, it generally lacks the necessary rigor and independence to be either technically robust or demonstrably in the public interest. For example, the UK operates an in-house adaptation process without scope for public input even from financial statement users. Second, adaptations result in standards that vary between countries and do not, therefore, facilitate international comparisons. The same problems arise when countries decide to adapt IPSAS to address their specific needs. (Baskerville and Grossi, 2019).

#### 3.4 IMF's Coverage Augmented by Other Sources

Although the IMF has taken a lead in promoting fiscal transparency its reports do not provide complete coverage of countries, and its assessments are not easily comparable, because they reflect different versions of the IMF's fiscal transparency code, evolving over time with increased expectations for government's financial reporting. To augment the IMF's fiscal transparency evaluations and ROSCs, the first author of this paper reviewed additional sources for country-specific information on fiscal transparency, specifically: Open Budget Index; Global Initiative for Fiscal Transparency (GIFT); Transparency International (Corruption Perceptions Index); and also considered the following sources of information on governments' financial reporting: Financial Accountability Index 2018 (CIPFA-IFAC-University of Zurich Reports); Eurostat; and OECD; and the United Nations Conference on Trade and Development (UNCTAD). The high level summary of this data appears in Table 1 on the following page.

Table 1 shows that the available data on use of accruals is inconsistent, despite the importance of this for governments' achievement of fiscal transparency. This highlights the primitive state of fiscal transparency monitoring.

**Table 1: Fiscal Transparency and Factors Contributing to Fiscal Transparency**

Country	OBS 2017 (1)	Accruals OECD 2017	% IPSAS E&Y 2012 <sup>2</sup>	Accruals IMF-WEO	Accruals CIPFA(3)	Accounting Standards	CPI (2)
Croatia	57/100	Not OECD	Not yet EU	Accruals	No data		48 (R60)
Czech Republic	61/100	Accruals	46%	Accruals	Cash*		59 (R38)
Estonia	Not covered	Accruals	91%	Cash	Accruals	National standards/IPSAS	73 (R18)
Hungary	46/100	Accruals	42%	Accruals	Cash*		46 (R64)
Poland	59/100	Accruals	63%	Accruals	Cash*		60 (R36)
Romania	75/100	Not OECD	51%	Cash	Cash*		47 (R61)
Serbia	43/100	Not OECD	Not in EU	Cash	Cash		39 (R87)
Slovakia	59/100	Accruals	69%	Accruals	Cash*		50 (R57)
Slovenia	69/100	Cash trans <sup>2</sup> accruals	59%	Cash	Cash*		60 (R36)
France	74/100	Accruals	87%	Accruals	Accruals	National standards	72 (R21)
Germany	69/100	Cash	34%	Accruals	Cash		80 (R11)
Italy	73/100	Cash	47%	Accruals	Cash*		52 (R53)
UK	74/100	Accruals	95%	Accruals	Accruals	IFRS–adapted	80 (R11)

(1) The International Budget Partnership (OPB) describes 61 and higher as ‘sufficient.’ Ranges for Open Budget Scores (OBSs) include: 21-40 minimum information available, 41-60 limited information available, and 61-80 substantial information available.

(2) CPI Corruption Perceptions Index 2018 shown as a score followed by a rank.

(3) \*Countries described by the CIPFA-IFAC report as ‘transitioning to accruals.’

### 3.5 IMF’s Reports on Countries’ Fiscal Transparency

We turn then to the IMF reports. The IMF has become more demanding with respect to governments’ financial reporting. This is evident from a comparison of its fiscal transparency reports on Romania, for reviews in 2002 and 2015. The 2015 review emphasized that progress was needed to implement full accruals and high quality financial reporting standards, while the 2002 review accepted that a cash basis could generate adequate fiscal reporting information. The 2015 report emphasized that ‘while national accounting norms ... follow some International Public Sector Accounting

<sup>2</sup> Page 23 summary table of Ernst & Young 2012.

Standards (IPSAS) principles [they] are not [yet] fully consistent with IPSAS.’ (IMF 2015, page 9)By contrast, the 2002 report highlighted many individual issues that better financial reporting would have addressed but failed to link those issues to a need for better financial reporting. At the same time, that report was positive about Romania’s ‘fiscal reporting,’ despite its poor quality. The 2002 report claimed that, ‘the public is provided with adequate information on the fiscal activity of the general government’ while acknowledging that there are ‘a few notable exceptions.’

With this evolution in mind Table 2(on the following page) summarizes comments from the IMF ROSC-FTM reports on the selected countries. Where there are relatively recent assessments the reports highlight significant improvements. As early as 2009 the IMF assessed Estonia as meeting nearly all of the Code’s requirements. A 2003 IMF report on EU accession countries assessed seven of the nine countries (the exceptions being Croatia and Serbia) against four fiscal transparency areas, noting that their objective of joining the EU had been a motivating force for fiscal transparency improvements. The seven countries had made progress on medium-term budget frameworks but had significant weaknesses with respect to including all off-budget activities in fiscal reports and analysis. With respect to fiscal monitoring, reporting and control, the report highlighted weaknesses with budget controls and audit functions in six of the seven countries, with only Poland escaping negative comment.

**Table 2A - IMF ROSCFiscal Transparency Evaluations**

<b>Country</b>	<b>Year</b>	<b>Summary Comments</b>
Croatia	2004	Croatia meets the Code in a number of areas and has been making significant progress in strengthening fiscal management and transparency. Nonetheless, major weaknesses remain.
Czech Republic	1999 & 2004	The original ROSC concluded that the Czech Republic meets many of the requirements of the Code. Annual updates have reported steady improvements in addressing the remaining transparency issues. Most of the ROSC recommendations have been addressed, but there are still areas where transparency could be improved.
Estonia	2009	Estonia now meets nearly all of the requirements of the Code and approaches best international practice in some areas. Nevertheless, there are a few areas where further reforms could usefully enhance fiscal transparency.
Hungary	2007	Hungary has increased its level of transparency in a number of areas since the 2001 ROSC. However, the cause of fiscal transparency has not been served by the fact that the Hungarian government has, on a number of occasions in recent years, sought to rely on transactions which have the effect of reducing the measured deficit and debt without changing the underlying fiscal position. There is scope for further improvement in fiscal transparency in a number of other areas.
Poland	2001 & 2004	The 2001 report identified areas where progress had been made in meeting the requirements of the Code, while flagging areas where transparency could still be improved. While fiscal transparency in Poland has improved in recent years, and is generally in line with international standards, there are still some outstanding issues which need to be addressed.
Romania	2015 (FTE)	Since 2010, a comprehensive program of reform in Romania has led to significant improvements in fiscal transparency. Romania performs well against the Code in many areas. The government is rated as good or advanced in 15 of the 36 dimensions while on 15 dimensions it is rated as basic. A further five are regarded as not met, while one dimension was not assessed given the absence of Public-Private Partnerships (PPPs) at the time of the evaluation.
Serbia, Republic	2009	Serbia has made solid advances under all four pillars of the Code. Nevertheless, some major shortcomings in fiscal transparency need to be addressed.
Slovak Republic	2002	The Slovak Republic now meets the Code's standards in several areas. The staff team identified a number of areas where progress would be needed to meet all the requirements of the code and to move towards best practices.
Slovenia	2002	Slovenia meets the Code's requirements in many important respects. Despite high degrees of fiscal transparency in many areas, there is room for further improvement to comply with the Code and be consistent with best international practices.

In 2003 the IMF described seven of these countries' accounting and reporting as generally 'sound,' despite the lack of full accruals. This highlights the IMF's low expectations at that time. Worse, the IMF stressed that 'adoption of accrual based reporting standards does not imply immediate adoption of accrual based accounting'

noting that ‘cash-basis measures of fiscal balance remain very relevant to macroeconomic analysis and are still a key focus for most advanced countries.’ In effect, the IMF’s 2003 view was that cash accounting was sufficient for fiscal transparency. Yet EU member states had directed the European Commission to adopt full accruals and IPSAS, and within ten years of that report, the EU Parliament had initiated the Eurostat project to investigate moving all EU countries onto accruals, with IPSAS proposed for consideration as the applicable standards.

### 3.6 Comparison with High GDP EU Countries’ Fiscal Transparency

Let us then compare:

Table 2A Comparison countries		
France	2000 & 2004	France has made further progress, including confirmation that accrual-basis accounting has been implemented.
Germany	2003	Germany has achieved a high level of fiscal transparency. This should be improved in several areas, including that planning, budgeting, and reporting of the general government fiscal position must be strengthened.
Italy	2002	There has been significant progress on budget management, although the quality of fiscal data falls short of the Code. Focus should expand beyond control to also include the efficient allocation of resources, with further areas for improvement described.
United Kingdom	2016 (FTE)	Across all pillars evaluated in the code, the UK scores very highly when compared to other countries that have, to date, undergone an assessment. Of the 48 principles in the Code, the UK meets 9 principles at the basic level, 10 principles at the good level, and an unprecedented 23 principles at the advanced level. Fiscal transparency practices are strongest in the area of fiscal reporting and resource revenue management, while the UK also scores strongly on fiscal risks. In four principles, the UK’s transparency practices do not currently meet basic practice.

## 4. Conclusions

A recurring characteristic of the fiscal state is its *après nous le deluge* attitude. Trans-generational public interest goals, such as the provision of good health services or the building of high quality infrastructure, are not reflected in cash-based government accounting which serves only the immediate needs of the present moment and then only in a very limited fashion. On this demonstrably antiquated accounting basis public needs which exist now, but are not yet insistent, can be starved of investment until the demand

for them is patent. By which time the situation has become critical. The infrastructure crisis in the US is a good example.

The same lack of accounting for necessary future commitments means that the fiscal state has an unassailable capacity to simply declare tomorrow that its promises of yesterday are unaffordable. The Province of New Brunswick's attempt to "renegotiate" its employee pension obligations to avoid insolvency illustrates the pension fund problems throughout Canada and the United States. Underfunding of pension obligations and the run-down of public infrastructure occurred before adoption of high quality accruals accounting, which would otherwise have conferred enough transparency to hold politicians accountable for their decisions to underinvest and over-promise<sup>3</sup>.

Behavior which would be regarded as scandalous for any business is treated as acceptable in the larger entity of the state, despite its significant role in the well being of its citizens. Behind these behaviors lies the structural reality that the state's role in a wholly monetized economy cannot be delegated or abrogated. That role must be managed within clear and defined limits so that its risks to the lives of its citizens are matters of public knowledge.

Concretely it would seem that significant progress has occurred in the countries under review since the IMF's first fiscal transparency assessments. There are however gaps and inconsistencies in the data available. The majority of the nine countries cited need to improve their financial reporting, which appears to have become stuck in 'transitioning to accruals.' The benefits, however, to both government financial management and citizen trust and confidence in their state make the movement to good quality public sector accounting a progressive cause for our time.

Institutional interest in governments' financial reporting continues to increase, and yet reliable information on the state of play is difficult to obtain, with analysts 'talking past each other' when assessing key concerns such as the use of accruals accounting, application of accruals financial reporting standards, and the extent to which national

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<sup>3</sup>Flescher et al (2019) explains that "The realization that pension funds are typically underfunded stems from the fact that the accounting standards associated with state and local government employee pension funds have led to greater transparency since 2011." Stoycheva (2011) shows that "...political interference through reduced contributions was the main factor explaining pension performance."

governments' financial reporting standards are consistent with IPSAS requirements. There is obviously a need for more education and discussion amongst policy makers on the place of accounting in good public sector management.

The data available shows that there is significant variation with respect to achievement of fiscal transparency within both the nine former Communist countries and the comparison four high-GDP EU countries. Each group includes at least one country with demonstrably advanced levels of fiscal transparency (Estonia and the UK). Each group also includes countries that need to make significant progress on fiscal reporting. One country in each group—Serbia in the former Communist countries and Germany in the comparison countries—remains stuck in the past with seemingly no plans to move from their cash-basis financial reporting and thereby achieve higher fiscal transparency levels across all four of the Code's principles<sup>4</sup>.

National and international demands for fiscal transparency are likely to become more insistent. The European project is unworkable without reliable country comparisons. Nor can powers such as the United States and China expect to sustain a healthy relationship with their citizens over the course of generational time without an increase in fiscal transparency as the requirements of environmental conservation, participation in world trade, and provision of sustainable quality services for citizens at different life stages demand conscientious public sector management with reliable financial information. Small countries have even less room to procrastinate. They cannot continue to furnish the headlines for this or that crisis of state action in violation of the limits of the state's ecology. How the politics of fiscal transparency play out over this generation will therefore shape the course of the 21<sup>st</sup> century.

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<sup>4</sup>Although Serbia is considered to be part of the PULSAR initiative, which suggests that its position on moving to accruals accounting could be changing. See <https://www.pulsarprogram.org/members>

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