GASAB

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Operational Framework
Of Accrual Basis of Accounting
In Governments in India

Government Accounting Standards Advisory Board

Operational Framework of Accrual Basis of Accounting in Governments in India

Introduction

1. Traditionally Government accounting aims at ensuring compliance with budget and proper utilization of public monies. The main concern of Government financial managers has been to find sufficient cash to fund public schemes. Reporting under cash based accounting systems typically takes the form of a cash flow statement which details the sources and applications of Government cash during the period and its cash balance at a given point in time.

2. Public financial management has evolved significantly in recent years. In the last couple of decades, many countries have reviewed the way their governments function, manage their resources and disclose their operations. Issues like operational efficiency, results, effectiveness of the delivery system, cost of service delivery, ability to support welfare programs, good governance, etc., have been actively debated and considered. The financial, budgetary, accounting and management systems have seen many changes and experimentation. Many countries have shifted towards accrual based accounting systems, fully or partly or with some variation.

3. The Twelfth Finance Commission, recognizing the need for improvements in accounting and financial reporting, recommended a gradual shift to accrual accounting by the Union Government. The Central Government has accepted the recommendation in principle. In its explanatory memorandum as to the Action Taken on the recommendation of the TFC, Finance Minster had stated that the Government Accounting Standards Advisory Board (hereinafter GASAB) in the Office of the Comptroller and Auditor General of India would recommend an operational framework and detailed road map for its implementation.

4. Apart from the Central Government, so far, eighteen (18) State Governments have accepted the idea of accrual accounting in principle. These States are Andhra Pradesh, Assam, Bihar, Chhattishgarh, Goa, Gujarat, Himachal Pradesh, Karnataka, Madhya Pradesh, Maharashtra, Manipur, Meghalaya, Rajasthan, Sikkim, Tripura, Uttaranchal, Uttar Pradesh and West Bengal.

5. Pursuant to Government's directions GASAB has prepared this document to provide a framework for transition from the existing cash based accounting to accrual based accounting by the Union and State Governments and Union Territories with Legislature. The Framework provides a phased approach to the

transition, as recommended by the TFC and broad guidance on the issues peculiar to government accounting. This can serve as the guiding document for pilot studies being undertaken by various departments of the Union Government and State Governments. In the absence of an Operational Framework, the implementation of accrual basis of accounting at various levels in a Government may end up in disparate and incomparable information incapable of being integrated for preparing the financial statements of the Government.

6. The Operational Framework will be comprehensively reviewed by GASAB after three years of date of its issue. At the time of review, feedback received from the stakeholders as well as results of pilot studies as available by then would be taken into consideration.

Existing Framework of Accounting in the Union & State Governments

7. Article 150 of the Constitution provides for maintenance of the Government accounts "in such form as the President may, on the advice of the Comptroller & Auditor General, prescribe".

8. The Government Accounting Rules (GAR), 1990 issued by the Office of the Controller General of Accounts in the Ministry of Finance lay down the general rules of government accounting. The system of accounting classification in terms of functions, sub-functions and programme is laid down in the List of Major and Minor Heads.

9. The Government Accounting Rules require, "with the exception of such book adjustments as may be authorized by these rules or by any general or special orders issued by the Central Government on the advice of the Comptroller and Auditor General of India, the transactions in the Government accounts shall represent the actual cash receipts and disbursements during the financial year as distinguished from amounts due to or by Government during the same period". Government accounts are thus maintained on cash basis. Expenditures are recorded at the time of release of payment, and receipts are recorded on actual realization. Movements in the Government cash balance kept with RBI as a result of such payments and receipts are also simultaneously recorded in the account books. Thus, the main accounts record flows of cash into and out of Consolidated Fund and Public Account, and the effect of these cash flows on Government's liquidity position.

10. In terms of Article 266 & 267 of the Constitution, Government accounts are maintained in three parts:

    a. Consolidated Fund of India [CFI]
    b. Public Account
    c. Contingency Fund

11. CFI transactions are classified using a functional classification divided into functions and programs [largely conforming to plan heads of development] with a 6-tier hierarchical structure.

12. Articles 112 and 202 relating to the Annual Financial Statement of the Union and the State Governments respectively, require that expenditure embodied in the annual financial statement shall show separately: (a) expenditure charged upon the Consolidated Fund, thereby requiring depiction of ‘charged’ and ‘voted’ expenditure, and (b) expenditure on ‘revenue account’ from ‘other expenditure’, thereby requiring depiction of revenue and capital expenditure.

13. India has followed the policy of planned allocation of resources for economic development. This has given rise to reporting requirements of Plan and Non-Plan expenditure.

14. Transaction on Public Account are recorded as receipts and disbursements and classified into the broad categories of Small Savings, Reserve Funds, Deposits and Advances, Suspense and Miscellaneous, Remittances, and Cash Balance.

15. The financial reporting framework includes presentation of two audited annual accounts - the Finance Accounts and the Appropriation Accounts. These are prepared separately for the Union Government, each of the State Governments and Union Territories having Legislative Assembly. The Appropriation Accounts is compliance reporting on legislative appropriations and grants. Explanations are provided for significant variance [both excesses and saving] between the original demand and final appropriation and final appropriation and actual expenditure. The Finance Accounts contain the financial statements of the Government concerned. It contains statements showing functional head-wise distribution of Government receipts & disbursements during the year and debt and other obligations at the end of the year. Information on financial assets and guarantees issued by the Government is also provided in this document.

16. Budget documents use Fiscal Deficit to show Government’s revenue-expenditure gap and measures its dependence on non government savings for funding its expenditure. The Revenue Deficit is also reflected. The emphasis in these documents is on flows into and out of Consolidated Fund, deficit and its financing from various sources.

17. As per the provisions of the FRBM Act, additional disclosures are also being made of assets held by the Government including non-financial assets, arrears of tax and non-tax revenues and guarantees.

Accrual Basis of Accounting

18. Basis of accounting refers to a set of accounting principles used for recording events that determines when the effects of transactions or events are recognized for financial reporting purposes. Accrual system recognizes financial flows at the time economic value is created, transformed, exchanged, transferred or extinguished, whether or not cash is exchanged at that time. It records events as

they happen. The associated cash flows generally follow the event after some time and may or may not take place during the same accounting period.

19. Accrual accounting differs from cash accounting in following ways:

    a. It records consumption of resources during a period whereas cash accounting records payments. The accrual accounting, thus, focuses on cost of resources consumed whereas cash accounting focuses on expenditures incurred without linking them to the triggering event. Similarly, accrual system recognizes income as it is earned. This implies that while in cash based system only cash flows are recorded; in accrual accounting, in addition to cash flows, unpaid consumptions (payables) and unrealized incomes (receivables) are also recorded.

    b. The revenue flows from an output are matched with the consumption of resources that produced the output. This helps in bringing out the operating performance of an entity. Cash accounting does not apply matching principle.

    c. Accrual accounting provides a complete measure of an entity's financial position at any given point of time by a comprehensive presentation of entity's assets and liabilities.

20. Broadly, the perceived benefits from introduction of accrual accounting in Government are:

    - Better management of receivables and payables
    - Better assets management
    - Better liabilities management
    - Better management of contingent liabilities
    - Assessment of full cost of service delivery
    - Assessment of fiscal sustainability of operations

Objective of Transition

21. Internationally accrual accounting has been introduced as a part of wider management reforms in Public Sector including Government and not on a stand-alone basis. **In other words, accrual accounting is a means to an end, and is not to be seen as an end in itself.** It is therefore important that this aspect is kept in proper perspective in the strategy devised for transition to accrual accounting and the main objective of providing greater information for internal management purposes is not lost sight of.

22. As has also been recognized in the Roadmap, accrual accounting on a stand alone basis does not confer specific advantages unless it is shaped to meet the specific

information requirements for managing the operations of each organization. While the user departments/ ministries, the State Governments and Union Territories having Legislative Assembly would have unique information requirements for their internal financial management; there is need for an overarching reporting framework that would cater to the requirement of legislative reporting on common and comparable basis. **This operational framework therefore, has been designed keeping in view of the need to marry organization specific requirements with wider stakeholder interests in government finances**. The operational framework provides ample flexibility for governments to incorporate their unique requirements without harming the need of legislative reporting on a common and comparable basis.

Reporting Entity

23. The purpose of identifying reporting entity is to identify the Governmental unit that should prepare and present financial statements. This determines the boundary within which accounts of various subunits are fully consolidated. Under the existing system, the Union Government, State Government and Union Territories with Legislature form separate reporting entities. Each one of these prepares separate Finance Accounts. These boundaries should be retained under the accrual system. However, in case of Union Government an exception may have to be provided, as it works on departmentalized accounting arrangements. Different Union Ministries are at different levels of preparedness for this transition and are therefore likely to move at different pace towards it. In view of this, as an interim arrangement, it would be prudent to define each Union Ministry as a separate reporting entity. This arrangement may continue till the entire Union Government completes the transition. Thereafter, accrual based consolidated accounts for the Union Government as a whole should be prepared and reported.

Salient Features of the Roadmap

24. The Roadmap prepared by GASAB for transition to accrual accounting envisages a period of 10-12 years for completing the transition. The Roadmap gives a common prescription, which has to be tailored to departmental requirements. Main activities included in the Roadmap for transition to accrual accounting are:

- Setting up a Task Force or Cell or designating a nodal agency preferably at Ministry for Finance level for coordination and overseeing the implementation. Besides representative from the Min. of Finance, the said Task Force may comprise of:

    a. representative of the office of the CAG,

    b. representative from the office of the CGA,

    c. representative from Railways,

d. representative from the office of the CGDA,

e. representative from Posts, and

f. representative from State Governments (select State Governments).

Terms of Reference of the Task Force may include the following:

a. work as a nodal agency for implementation and coordination of transition to accrual accounting,

b. consider and suggest ways and means of setting up separate task forces in the concerned ministry/ department and State Governments for supervision and monitoring of transition to accrual accounting,

c. facilitate an integrated approach across Governments maintaining broad uniformity in the form of accounts,

d. provide a forum for evolving accounting policies and accounting standards and experience sharing and facilitating resolution of issues faced by different stakeholders,

e. consider GASAB's report on roadmap and operational framework for implementation,

f. detailed plan of action for scheduling of different activities,

Since changes in the accounting system would necessarily involve modifications in the existing system of accounting, separate task forces need to be set up in the concerned ministry/ department headed by the administrative Secretary being the Chief Accounting Authority

- Identification and collection of data required for preparation of accrual based Financial Statements.
- Pilot Studies covering a few Ministries/Departments/State Governments with a view to assess the gaps and problems in the existing system. This would also be crucial for process mapping.
- Detailed process study of various activities and accounting practices to assess the extent of departure from the existing system in terms of accounting principles, recognition and measurement of elements, classification and disclosure of information.
- Preparation of a detailed accounting framework in line with the broad contours of the operational framework prescribed by GASAB.
- Laying down accounting policies

- Preparation of a Chart of Accounts
- Devising subsidiary ledgers/records to be maintained in accounting offices
- Streamlining accounting dataflow and defining role and responsibilities amongst officials dealing with accounting data.
- Putting in place a new IT system
- Capacity building
- Pilot implementation of the new system in few Ministries/Departments
- Full implementation.

Operational Framework

25. As a general approach [and in recognition of the fact that accrual accounting should be targeted towards improved internal financial management], Departments/organizations should have the flexibility to decide the appropriate degree and extent of accrual base that is useful and sustainable for them. This decision will obviously be based on a careful cost-benefit analysis and functional desirability [internal to them].

26. Following the above, it would also be in the fitness of things that the accounting policies are framed independently by the departments/organizations. Accounting policies will, however, be consistent with generally accepted accounting principles.

27. The Operational Framework outlined in this document provides broad contours of the accrual accounting framework that will have to be developed further and tailored to suit organization specific requirements. Some departments have already initiated pilot accrual accounting projects. The Roadmap prepared by GASAB for transition to accrual accounting recognizes the importance of these pilots for assessment of gaps and problems in the existing system. Pilots have also been considered crucial for process mapping for the new system. Results of such pilots should be weaved into the detailed framework developed by individual departments/organizations for its refinement.

28. The design of operational framework indicates broad deviations from the conventional accrual basis of accounting as followed by the commercial, industrial and business enterprises. This is necessitated due to the specific requirements of accounting and reporting emerging out of the nature of Government’s transactions, types of assets held, liabilities carried and revenue collected. These, amongst others, include: (a) social and welfare orientation, provision of public goods, such as, law and order, defence and not-for-profit activities; (b) tax revenues, which are germane to Government’s sovereign right to tax; (c) budgetary reporting and correlation between budget and accounting; (d) assets in the nature of defence,

environmental and forest, electromagnetic spectrum, heritage, infrastructure, etc; and (e) fiduciary liabilities. These specific requirements warrant defining architecture of accrual basis of accounting that should be followed in Governments.

29. A broad framework for transition to accrual accounting is as under.

Stages	Expenses	Revenues	Assets	Liabilities	Contingent Liabilities
Current Stage	Exp - Current & Capital	Receipts	Financial assets	Stock of Public debt and Borrowings on Public Account	Guarantees
Stage I	**Current Expense on accrual basis** and Capital Expenditure on cash basis	Receipts	Financial assets	Stock of Public debt and Borrowing on Public Account + **Payables**	Guarantees
Stage II	Current Expense on accrual basis and **Capital Expenditure on cash basis [Excluding Expenditure on Military Assets]**	**Non Tax Revenues on accrual basis** + Tax Revenues on cash basis	Financial assets + **Receivables** + **Military assets**	Stock of Public debt and Borrowing on Public Account + Payables **+** **All other Liabilities** [except superannuation benefits, compensated leaves, provisions and social security]	Guarantees
Stage III	**All expenses on accrual basis + Depreciation**	do	**All Assets** (excluding infrastructure, land, heritage, intangible assets)	All liabilities (except superannuation benefits, compensated leaves, provisions and social security)	**All explicit contingent liabilities**
Stage IV	All expenses on accrual basis + Depreciation **+** **Provisions**	do	All assets including **infrastructure and land** [excluding heritage and intangible]	do	do
Stage V	**All Expenses**	**All Revenues on accrual basis**	**All Assets**	**All Liabilities**	**All explicit contingent liabilities**

30. **GASAB suggests** that Stage I depicted in Table above should be the starting point for introduction of accrual basis of accounting in Governments. Accounting reforms should incrementally graduate to Stage V, which represents full accrual accounting. It is, however, noted that there could be certain entities within the Government, e.g. the Railways, which may like to straightaway adopt full accrual due to their preparedness and nature of activities.

31. **Stage-I introduces accrual based recognition principle for current expenses.** Capital expenditures, as well as all revenues, will continue to be accounted for on cash basis as at present. Recognition of current expenses on accrual basis would lead to recognition of payables, which will be shown as a liability.

32. Stage**-II introduces accrual recognition of non-tax revenues.** Tax revenues will continue to be recognized on cash basis. Recognition of non-tax revenues on accrual basis would lead to recognition of receivables, which will be included in assets. Military assets will also be recognized on accrual basis at this stage and included in assets shown in the Statement of Financial Position. The remaining capital expenditure will continue to be shown on cash basis. Another change would be inclusion of all other liabilities except those on account of superannuation benefits, compensated leaves, provisions and social security.

33. Stage-III requires recognition of all expenses on accrual basis including recognition of depreciation. No provisions will be recognized at this stage. **Assets recognized at this stage on accrual basis would include all financial and physical assets [with the exception of infrastructure, land, heritage, and intangibles] and inventories.** Tax Revenue continues to be recognized on cash basis. There is no change in terms of liability over Stage-II. **Disclosure of all explicit contingent liability is made.**

34. **Stage IV** requires **inclusion of provisions as expense and extension of physical assets to cover infrastructure and land on accrual basis. Other elements are same as that in the previous stage.**

35. **Stage V is introduction of full accrual accounting for all the four elements – expense, revenues, assets and liabilities**. All expenses, all revenues, all assets and all liabilities are recognized on accrual principles and presented.

36. **As the transition through these stages in likely to happen at varying pace in different departments of Government entities, successful completion of every stage should be considered for consolidated reporting for the entire Governments at different levels. The time frame for Stage-I can be three to five years.**

Elements of Financial Statements

37. GASAB seeks to clarify certain concepts and principles and other related issues involved in reporting under accrual basis of accounting. These include the following:

    1. Elements of Financial Statements,
    2. Principles of recognition and measurement of the elements of the Financial Statements,
    3. Criteria for their classification and the Charts of Accounts
    4. Presentation of Financial Statements and formats,
    5. Disclosure Requirements

38. While standard definitions and guidance is available, it has to be carefully adapted/adopted or applied to instant situation. A general discussion of these follows.

Expenses

39. *Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrence of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.*

40. The types of expenses/expenditures that governments generally incur include:

    - Personnel expenses
    - Government transfers
    - Cost of goods sold
    - Costs of services provided
    - Capital asset use (depreciation)
    - Interest
    - Maintenance & working expenses.

41. Most of these items may be similar to expenses recognized by business enterprises, such as personnel expenses, or interest on debt, but may be more material in the government context. Exchange expenses/expenditures that are similar to those identified in the private sector do not pose particular accounting or reporting issues for government.

42. Most recognition criteria for expenses by business enterprises relate to the point of exchange or consumption of an asset. In the case of non-reciprocal transfers, there is no point of exchange on which to base recognition. Non-reciprocal

expenses that are unique to governments mainly include government transfers. The general principle in such cases is to go by the degree of discretion the Government possesses in making such transfers. As a guiding principle, the discretionary grants may be recognized at the time of payment (or sanction). In the case of non-discretionary transfers fulfillment of the eligibility criteria by the recipient should be taken as the point of recognition. Distinctive recognition criteria for each class/category of transfer payments will have to be prescribed by the individual departments/organizations.

43. The concept of reporting entity will also have to be clearly applied to separate custodial flows where the government is merely acting as an agent of another party or where the government is acting as trustee, as these will have to be excluded from expenses.

Revenues

44. Revenues are increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.

45. Reciprocal transfers form the majority of revenues in the for-profit sector and constitute some of the revenues of governments. Inflows to governments which have an exact counterpart in the for-profit sector include those arising from:

- Sale of goods
- Rendering of services
- Interest
- Royalties
- Dividends
- Commissions
- Long term contracts
- Lease agreements

46. Governmental revenues arising from peripheral or incidental transactions (e.g., from the sale of fixed assets) also have counterparts in the private sector. In some cases, such as divestment proceeds, such gains are very significant.

47. Revenues could also include gains that occur in the absence of transactions. For a number of these items, there are counterparts in the private sector. For example, gains arising from:

- changes in the fair value of financial assets and financial liabilities;

- changes in the value of other assets such as forests and mineral resources; and changes in foreign currency exchange rates.

48. Whilst gains can be classified as revenues under a comprehensive definition of income, it is practice in some jurisdictions to take gains directly to net assets or equity.

49. The accounting issues for exchange revenues, including gains are usually no different from those in the private sector. However, in some circumstances, the distinct nature and characteristics of governmental assets and liabilities may warrant a different accounting treatment. Also, to the extent that governments have significant holdings of certain asset types (e.g., forests or mineral resources) and generally accepted accounting practice (GAAP) for these types of assets in the private sector is underdeveloped, specific guidance might be required. The detailed accounting frameworks prepared by individual departments/organizations will have to address each of these issues.

50. Much governmental revenue is in the form of taxes, rates, levies, fines and non-reciprocal grants in which the existence of an exchange relationship is tenuous. In addition to taxation receipts, governments may also receive grants, donations and payments on behalf of other parties. Recognition and measurement of such revenues presents a challenge. While attempting to account for taxation and other such non-exchange revenues two aspects have to be kept in mind:

    1. Taxation revenues do not accrue to the agency responsible for collecting it, and
    2. since governments are able to obtain taxation revenues through their sovereign powers to demand payment, the amount of revenues does not necessarily provide an indication of their efficiency or effectiveness.

51. Considering the complexities involved with such transactions and in view of the overall objective of the transition, GASAB suggests that while non-tax revenue is recognized on accrual basis from Stage I, tax revenue continues to be recognized on cash basis until Stage V is implemented. However, if there is reasonable certainty of collection and measurability, certain tax revenues may be recognized on accrual basis at any stage convenient. The fact that such recognition has been included should be disclosed in the financial statements.

Liabilities

52. Liability *is present obligation of the Government arising from past events, the settlement of which is expected to result in an outflow from the Government of resources embodying economic benefits or service potential*.

53. There is emphasis on the following:

a) Existence of present obligation arising from past events. This implies legally enforceable and contractual duty or responsibility to a third party, which is to be fulfilled. For example, repayment of debt, amounts payable for services and goods acquired, employees' pensionary benefits, committed transfer payments, grants, shared cost, etc.,

b) Liability has adverse financial consequences for Governments. Settlement of the present obligation involves the Government or the entity giving up resources or disposing off assets to satisfy the claim of the other party.

54. It can be argued that, in the government context, the existence of a present obligation arising from past events occurs only when there is a legal obligation. The legal obligation could be the result of contracts, agreements or legislation that commit the government, for example, to repay borrowings; or to pay for goods and services acquired or provided prior to the accounting date; to provide services or use resources in a specified way; or to make transfer payments, even where no value is received directly in return (e.g., entitlements, shared cost agreements or grants). Usually, an external party has a legal right of recourse if the government fails to meet the terms of the contracts, agreements or legislation.

55. Building on that concept, two additional criteria may be useful in assessing the difference between legal obligations and policy decisions:

- whether or not the government has the discretion to avoid the obligation; and
- whether or not the government can vary its liability without the consent of the party affected.

56. The types of liabilities that governments may report include:

- accounts payable arising from the purchases of goods and services;
- accrued interest payable;
- accrued salaries and wages;
- accrued vested vacation pay or other accrued compensated absences;
- employee pension obligations and other accrued employee benefits, including any accrued termination benefits;
- amounts payable under guarantees and indemnities where events and amounts have become certain;
- deferred or unearned revenue (where amounts have been received but have not yet met the revenue recognition criteria, such as where there are restrictions on use of resources);
- transfer payments payable;
- currency issued;

- lease obligations related to capital leases; and
- borrowings
    - bank loans and other short term borrowings;
    - long term debt; and
    - loans and advances payable to other levels of government or government entities.

57. A liability is recognized in the Statement of Assets and Liabilities when it is probable that an outflow of resources embodying economic benefits will result from the settlement of a present obligation and the amount at which the settlement will take place can be measured reliably.

58. Most of the liabilities mentioned above are similar to those of business enterprises and, therefore, do not inherently pose unique accounting or reporting issues for governments.

59. Accrued liabilities on account of compensated absences of employees and unfunded superannuation benefits require special mention. Recognition of these liabilities on accrual basis ensures that full personnel costs are shown in the period in which they occur. However, the measurement of such liabilities requires actuarial valuations, which are quite complex in nature.

60. Liabilities that are unique to governments would include government transfers payable. Government transfers payable arise from entitlements, shared cost or grants where there is no direct exchange relationship with the recipient. In concept, the related liabilities are not significantly different from other accounts payable. It is the recognition criterion that is unique because there is no direct exchange relationship.

61. Two items which often do not meet the definition and recognition criteria are commitments and contingencies. GASAB would suggest these are disclosed separately through Notes to Accounts.

Assets

62. An asset is a resource controlled by the entity as a result of past events which has a future service potential and from which future economic benefits are expected to flow to the entity.

63. The emphasis is on three fundamental characteristics:

a) Origin in past transactions or events. This may include budgetary expenditure for asset creation, inherited assets such as environmental and natural resources, electromagnetic spectrum, etc., or assets received as grants;

b) Future economic benefits or service potential. Future economic benefits or service potential may contribute to cash flow or may provide goods or services that include national security, law and order or public goods, etc.

c) Ownership of assets through control by Government. Government may control assets not only because of budgetary expenditure, but also in its sovereign right as custodian of national natural resources, heritages, etc. Certain other transactions such as grants may also give control to an asset.

64. Assets held by Governments may be classified depending on the types of assets such as Financial Assets, Physical Assets and Intangible Assets. Assets may further be classified in terms of current and non-current nature. Some of the asset categories such as military assets are relevant only in case of the Union Government. Assets held by Governments may be classified as:

Financial Assets

Current Financial Assets

a) Cash and cash equivalents (Cheques and short term financial instruments)

b) Revenue receivables

c) Prepayments

d) Others

Long-term Financial Assets

a) Loan and advances to employees

b) Loan and advances to other Governments and Entities

c) Investments

d) Others

Physical / Tangible Assets

Current Physical/Tangible Assets

a) Inventories including Office Stationary

b) Work-In-Progress

c) Arms and Ammunitions (e.g., Police)

d) Defense / Military Assets

e) Un-issued Stamps (e.g., Posts)

f) Others

Long Term Physical / Tangible Assets

a) Plant, Property and Equipments including Buildings, Motor Vehicles, Furniture and Fittings, IT Resources, etc.,

b) Land including commercial and non-commercial land,

c) Infrastructure such as roads and railways networks, water and sewerage system, communication networks, dams and reservoir, etc.,

d) Investment property,

e) Heritage Assets,

f) Natural Resources such as Forests, Mines, Oil Reserves, etc.,

g) Others

Intangible Assets

a) Copyrights and Patents,

b) In-house developed Software,

c) Electromagnetic Spectrum,

d) Others

65. An asset is recognized in the Statement of Assets and Liabilities when it is probable that the future economic benefits or service potential associated with it will flow to the Government and the asset has a cost that can be measured reliably.

66. Materiality is an important consideration in recognition of tangible assets in terms of determining capitalization threshold. Individual departments/organizations may prescribe threshold values for recognizing assets. Assets less than this value may be treated as an expense. Despite the use of capitalization threshold, the Government may choose to record and report all of a particular type of assets if considered appropriate. For example, regardless of capitalization threshold, the Government may report all land. The Government may not determine any capitalization threshold for heritage assets and may recognize and report all such assets. Some assets may have lower value per unit than the capitalization threshold. For example, office automation equipments if recorded individually may have value below the threshold. However, such assets may be material as a group. In this case, the assets may be recognized as single group / block assets with one combined value.

67. Ownership and control aspects should be carefully judged in identification of assets.

68. Reliable measurement of assets may initially be more difficult. As a general rule valuation of assets should generally follow the historical cost method. The basic

data on historical cost may be taken from the stock registers. Finance Accounts contain data on financial assets as also capital expenditures.

69. However, cost records may not be available in some cases. In some others, ownership may not be clear. Alternative valuation methods depending on the nature of assets and data availability will have to be adopted in such cases. These deviations must be reported in terms of asset measurement policies and valuation methods.

70. These broad principles should help departments in identification of assets and liabilities and collection of data required for presentation of accrual based financial statements, as required in the Roadmap for transition to accrual accounting.

Chart of Accounts

71. The roadmap requires preparation of a chart of accounts for capturing accrual based information in account books.

72. Classification of government expenditure is important for policy formulation and decision-making on sectoral allocation of funds, performance monitoring of various government programs and activities, establishment of accountability for budgetary compliance, and in the analysis of overall economic impact of government policies.

73. The main challenge in designing a classification scheme for government expenditure is to keep it simple and yet meet the requirements of budget management and reporting to different stakeholders. The guiding principle should be the administration's capacity to consistently capture different attributes with sufficient reliable details.

74. The information requirements for macro management [at Government-wide level] and micro management [at the Ministry level] are different. At the macro level data on functions, programmes, economic categories are of importance. From the point of view of budget administration and control at the micro level it may be desirable to break down the appropriations to lower operational levels, such as divisions within the Ministry/Department and activities within the program. This distinction has to be kept in view while designing the Chart of Accounts (COA).

75. The Chart of Accounts should, therefore, logically have two tiers, one which captures information for use at the macro level [this will be uniform for all the departments as in the case of existing Major and Minor heads] and the other which captures information for budget management in the Ministries. Departments/Organizations should have the flexibility to design their own Chart of Accounts for the second tier.

76. GASAB would advise a minimalist approach to changes in existing classification structure for accommodating accrual elements.

Financial Statements

77. The structure of financial reporting will comprises primarily three interrelated statements:

    - Statement of operating performance (Income & Expenditure Account),
    - Statement of financial position (Balance Sheet) and
    - Statement of sources and uses of cash

78. Since the conventional format of a profit and loss statement will not be appropriate, the emphasis of the operating statement will be on the cost of providing services (i.e., expenses) and how these expenses are funded by governments from year to year (i.e., revenues) with the consequential impact on the financial position (i.e., the balance sheet).

79. The accrual based financial statements will provide two important measures of financial performance – Fiscal Balance and Net Assets/Equity (Net Worth). Fiscal balance will measure the operating performance and provide an indicator of the saving-investment gap of the government; Net Assets/Equity will provide a measure of governments' financial position in terms of its ability to relinquish its liabilities. Changes in the net worth over time provide a measure of the sustainability of government fiscal policies.

80. All information previously recorded according to the cash basis of accounting will be retained and presented in a reorganized format in the Statement of sources and uses of cash – still serving the analysis of liquidity management. In addition, other statements will serve to provide an integrated presentation of the economic operations and position of government.

81. Formats of these statements will perhaps evolve on different lines as different organizations go along the transition path. For the purpose of uniformity, GASAB would come up with a guidance document in this regard.

82. The Appropriations from Parliament will continue to be obtained on cash basis and this will necessitate preparation of Appropriation Accounts showing compliance with parliamentary supply. Similarly, Finance Accounts will also continue to be prepared on cash basis till the new framework stabilizes. The statement of receipts and disbursements (Statement No. 1 of Finance Accounts) will serve as the link between the accrual based Statement of Operating Performance and cash based budgets.