

Finance Minister's Speech

Accrual based Financial Reporting in Government, June 21, 2011

Shri Vinod Rai, Comptroller & Auditor General of India,
Finance Ministers from State Governments,
Shri Gopalan, Secretary Economic Affairs,
Senior Officials from Central and State Governments,
Ladies and Gentlemen.

It gives me great pleasure to be here with you at this Conference on the issue of accrual based financial reporting in the Government. This is an important initiative in the reform of the system of accounts and financial reporting in the public domain. As you are aware, the Government has already accepted the recommendation of the Twelfth Finance Commission for introduction of the accrual accounting in principle. Accordingly, the Government Accounting Standards Advisory Board (GASAB) in the Office of the Comptroller & Auditor General of India has prepared an operational framework and a detailed road map for its implementation.

2. The relevance of accrual accounting has to be looked at from the overall perspective of public financial management. It covers a broad spectrum of activities including budget preparation and execution, internal

controls, accounting and financial reporting, internal audit, audit by the Comptroller & Auditor General of India, monitoring and reporting arrangements. Moreover, accrual accounting has to be assessed against the prevalent accounting practices, for improving the effectiveness of planning, policy making and budgeting process of public resources.

3. At the heart of the any fiscal management system is the accounting system, which maintains the basic records of government transactions. A robust, comprehensive and transparent accounting system is a must for any government.

4. Government accounting and financial reporting in India has a history of several centuries. Our current accounting system derives its form and substance largely from cash based accounting procedures. This system has worked well over the years and has the advantage of simplicity and provides a wide variety of information. However, there is scope for improving the content and quality of the cash based accounting system so as to reflect the financial health of governments more appropriately. We have to keep in mind that, today, it is not only the Parliament and the government that require accounting information, but there are other important stakeholders including citizens, analysts and national and international financial institutions. In this age of awareness and information revolution, an average citizen and a social activist wants information to assess the financial health and performance of

governments in delivering public services and development schemes for the benefit of the society at large.

Ladies and Gentlemen,

5. One area where our accounting system needs further improvement is with regard to having an adequate framework for accounting the assets and liabilities of the Government. Although the FRBM Act at the Centre and State levels now prescribe maintenance of asset registers, systems have to be put in place for proper detailing and updating of these records. There has to be an effective method for tracking assets created out of public money. Without that the accountability of departments in managing government assets would get diluted. I have asked that a strong IT based system for recording assets be established to strengthen the existing disclosures under the FRBM Act.

6. Another area of inadequate reflection of government liabilities in our accounts relates to pensions. In case of pensions only yearly expenditure is reflected in the accounts, but future liability of the government is not accounted for. Calculation of future pension liabilities is indeed a difficult task as it depends on longevity of individual pensioners. The assumptions for this calculation have to be carefully made. Similarly, it is often pointed out that the present system does not account for goods and services received but payment not made, revenue demand raised but not realized etc. There are

multiple views on these issues, both theoretical and of practical nature. We need to be careful while addressing these issues. We should focus on areas which foster transparency, Parliamentary accountability and are of use to decision makers in government. I feel that, today, the Government needs more comprehensive financial information, while taking decisions about the feasibility of financing the services it wishes to provide and for planning the future funding requirements of asset maintenance and replacement.

7. International experience in accrual accounting has been varied with mixed results. We have to recognize that success stories are not many. I understand that some pilot studies have been undertaken in selected state government departments and other entities. Based on the knowledge gained through these pilot studies and the experience of some other countries, it is clear that introduction of accrual accounting is not going to be an easy task. In fact, we need to clearly identify the critical and the preparatory steps which need to be taken. While doing so, the requirements and the capacity of the third tier of governance, at the level of local bodies, should be borne in mind. Of course, adequate support and guidance would have to be provided by both Central and State Governments. An incremental and phased introduction of accrual systems would therefore be appropriate. As I mentioned in my speech at the 150th anniversary of the institution of Comptroller & Auditor General of India, there are many challenges in view of

the complex nature of administration and accounting in a diverse nation as India and these will have to be carefully factored in.

Ladies and Gentlemen,

8. I am happy to note that two Indian Government Accounting Standards (IGAS), namely, IGAS-1 on Disclosure Requirements for Guarantees and IGAS-2 on Accounting and Classification of Grants in Aid proposed by GASAB have already been notified by the Government and work on some more standards is underway. In order to facilitate a gradual and seamless transition to accrual accounting, GASAB could prepare guideline notes in various areas of accrual accounting for the assistance of the officials in all tiers of governance.

9. The most important element on which the success of accrual accounting hinges is the capacity of the people who would be preparing the accounts in accrual form. As much of the data needed for accrual based accounts resides with the administrative managers, we would need to build up the capacity of administrative units along with the staff of accounting organizations.

10. The implementation of accrual accounting system would also need strong Information Systems with an IT backbone. The computerization efforts

being made in various departments of Central and State governments need to be synchronized so that there is compatibility. The IT systems should be able to seamlessly integrate with each other. The Central and the State governments should take ownership of this initiative in accounting reforms. I solicit full cooperation from all Finance Ministers and Finance Secretaries of States in ushering in this important reform, which will go a long way in improving the financial reporting and fiscal discipline of the governments. While institutions like Comptroller & Auditor General of India through GASAB can provide the technical support, it is the executive that has to take the lead in the implementation process with a view to succeed.

11. The daylong conference being held today provides a very useful platform for exchange of views. The conference will benefit from the interventions of State Finance Ministers. I am sure there would be many valuable takeaways from today's deliberations.

12. In conclusion, I am sure that together we will be able to build a robust modern accounting system that will promote more efficient financial reporting and serve as a vital tool for decision makers in the government. I would like to thank Shri Vinod Rai, for organizing this conference and to the State Finance Ministers for coming here to be a part of these deliberations. I wish this endeavour all success.

Thank you.