

RESEARCH ARTICLE

Comparison of Accrual and Cash Accounting Principles in Slovakia

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Abstract

Quality financial information is necessary for effective management in the public sector sphere. A role of accounting in the public sector is to ensure a database of relevant information necessary for public finance management and for the needs of the presentation of results of our country's economy within the European Union. This information can currently be divided into two basic groups: State budget (central government), which comprises all budget chapters and their subordinate organisations. Public administration budget (public sector), which comprises state budget and other components of public administration budget, e.g. public universities, Social Insurance Company, health insurance companies, state funds, etc. Our article will deal with public administration and the process of international harmonisation and accounting regulation within the European Union as well as accrual accounting, thus contributing to the equivalence and comparableness of financial information in time and space.

Keywords: *Information, Accounting, Accrual principle, International Accounting Standards.*

Development of Accounting Information

Accounting in the public sector should generally, i.e. not only in Slovakia but also in other EU countries, represent a complex information system recording, analysing, classifying, summarising and interpreting the results of financial and economic activities of public sector entities and their impacts, aiming at:

- Providing information necessary for planning, organisation and control to management.
- Preparing and providing financial statements compiled in accordance with specific accounting standards and reporting standards for external users [1].

International integration, acquiring global dimensions, is typical of the current development of global economy. With regard to such a development of global economy, we observe, besides the international flow of goods and capital, also economic information flow, whose key source is accounting. Due to this reason, the process of international harmonisation and regulation in accounting, based on overcoming of the existing differences between individual national accounting systems, is natural. European Union trend is a unification of accounting and

reporting in state and public sectors, while the Slovak Republic has also accepted the implementation of accrual accounting and International Public Sector Accounting Standards in our legislation.

The objective of this change is to bring more effective public finance management, effective information provision for the needs of management and compilation of relevant financial statements for external users by means of accrual accounting principles [2].

General trend in the European Union countries is an effort to unify accounting and reporting of state and public sectors on the accrual basis, with the European Commission recommending the adoption of International Public Sector Accounting Standards. The accounting system of the European Commission was until 2005 based on financial flows. This system only recorded budgeted costs and revenues over a year, while it was supplemented by end-of-the-year information necessary to compile financial statements. As auditor's report on audited financial statements for 2002 implied significant problems in the present accounting system, the European

Commission decided to carry out a project of the transition to accrual accounting, defining the key requirements:

For a new accounting system – a unified data format, one fully integrated input of data in the whole information system, consistency of central and sector systems, multiannual consistency of data and information, fully accrual principle in accordance with international standards, - for information technologies – one data input, full integration of systems, elimination of double data, effective data safety, datatrustworthiness, auditability guarantee, etc.

Harmonisation of accounting represents a process of approaching accounting principles, accounting methods, accounting and balancing rules, and particularly the content of the financial statements of individual countries so that they are mutually comparable and transparent for the users of information from such financial statements in any state worldwide.

Gradual harmonisation of financial statements content is marked as harmonisation process. The basis of this process is the creation of accounting standards which are generally recognised and used [3].

Public sector accounting has had a separate place in the process of international accounting harmonisation since 2005. By issuing International Public Sector Accounting Standards, the international harmonisation and regulation of accounting have also expanded by such a specific sphere as public sector accounting.

Within the international accounting harmonisation and regulation, the International Federation of Accountants – Public Sector Committee - has been developing and issuing a set of recommended accounting standards for public sector entities - International Public Sector Accounting Standards (IPSASs). The committee has worked on the development of the set of accounting standards for public sector entities across the world, aiming at achieving its goal defined in the preface to International Public Sector Accounting Standards as follows: to develop programmes focused on the improvement of financial management and responsibility in the public sector, including accounting standards development and support of their implementation.

The objective of accounting and reporting harmonisation is to achieve the equivalence (equality) of information provided by accounting

to ensure their comparability in time and space [4].

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As International Public Sector Accounting Standards (IPSAS) are derived from International Private Sector Accounting Standards, in the Chart of Accounts for entities according to the methods of the European Union – ESA 95 – European System of Accounts, revenues and costs are regulated on the accrual basis, also regarding movements in assets and liabilities of public administration organisations, with links to the System of National Accounts. This demanding method provides information on the overall management of public finance as a decisive input upon the analysis of public administration budget management and information source for investors.

Characteristics of Cash and Accrual Accounts-Keeping Systems

Cash System

Public budgets and financial means allocation were traditionally compiled on cash basis. It was one of the reasons leading to the prevalence of cash basis in public sector accounting. The favouring of cash basis in public administration accounting originated in the need to monitor annual tax collection and to expend such revenues subsequently. Cash basis was focused on cash flow over an accounting period as well as it provided a basis for comparison with a budget. Information obtained from financial statements by means of direct comparison between a budget and actual state are useful for legislative bodies and other external as well as internal users monitoring actual costs compared to budgeted costs.

Cash accounting provides information on cash flow and thus enables monitoring of costs compared to their actual state according to the cash basis; however it is not intended to meet information needs. Its objective is to report cash inflows, cash outflows and changes to cash balances. It ignores other flows of financial means which can also affect the ability of public sector to provide goods and services. One of the advantages of cash accounting compared to other accounting

bases is the fact that compilers of financial statements are not forced to carry out any decisions at specifying the height of cash flows for the given period, and they have a possibility to manage the timing of cash flows by means of holding revenues or payments until further reporting period, and thus report favourable, respectively unfavourable results. From this viewpoint, the cash basis is less subjective than other accounting bases. In spite of apparent simplicity of cash accounting, it does not have to be easy for users to understand financial statements in practice, which is in a significant extent caused by the practice of created very detailed reporting of revenues and payments (detailed classification of revenues and costs), which significantly affects the complexity of bookkeeping. All cash revenues and costs regardless of their type are recognised at the moment of receiving or providing cash within cash accounting [5].

Accrual System

Accrual principle: the effects of accounting transactions and other events are displayed at the moment of their occurrence (not when financial means or their equivalents are received or expended) and are accounted in the books and reported in financial statements in the respective period.

The accrual principle, as one of the piers of double-entry bookkeeping, represents the basis of the principle of taking all costs and revenues into account in the accounting period in which they are incurred or generated regardless of the day of their payment, receiving or the day of balancing in another way.

The accrual principle is ensured by means of implementing accruals and deferrals of costs and revenues. Independence of accounting periods is emphasised by the accrual principle, which has significance at quantifying economic results for a current accounting period, not taking into account economic results in other accounting periods. The accrual principle contributes to real and truthful financial statements compiled on its basis, leading to real and truthful depiction of reality and management of an accounting entity.

The model of accrual accounting, which is a basis of financial reporting under International Accounting Standards, is predominantly included and explained in the framework of International Accounting Standards IAS/IFRS. The accrual principle transferred into the accounting of public administration and self-government means that

accounting provides information on assets, liabilities, costs, revenues, incomes and expenses in the period when such transactions occur. Compared to the cash principle, these transactions are to be reported in the period of their occurrence, not in the period when financial means related to such transactions were received or paid. Another condition of the accrual principle implementation is sustained duration continuity of an accounting entity. This principle is also grounded in a new law on budgeting rules [5].

In cash accounting, transactions were only accounted in case of receiving or paying financial means. Contrary to accrual accounting, cash accounting does not distinguish between a purchase of assets and a payment of expenses. It does not keep track of revenues, only costs, and profit and loss statement therefore has no statement value. It basically only keeps track of the income of different grants from different entities in relation to their drawing as well as to budget.

The European Federation of Accountants recommends to governments and public sector entities to use accrual-principle-based accounting, as it brings transparency, intelligibility and comparability of financial information in the public sector in Europe as well as outside of it.

Adoption of a unified set of accounting standards based on the accrual principle at all public administration levels in the whole EU would result in definite advantages from the viewpoint of management and administration of the public sector. It is expected that accrual accounting at the micro-economic level in the public sector will enhance the efficiency and effectiveness of public administration and facilitate the ensuring of liquidity, which is a necessary condition of maintaining and functioning of public service.

Like in case of any other economic activity, the administration and control of the efficiency and effectiveness of public sector depends on the management and control of its economic and financial situation and on the results of its economy. Double-entry accrual accounting is the only generally accepted system providing necessary information reliably and timely. In addition, harmonised public administration accounting based on the accrual principle enhances the transparency, responsibility and comparability of financial reporting in the public sector and can serve to enhance the efficiency and effectiveness of public audit.

Analysis of Harmonisation and Functioning of Accrual System in Practice

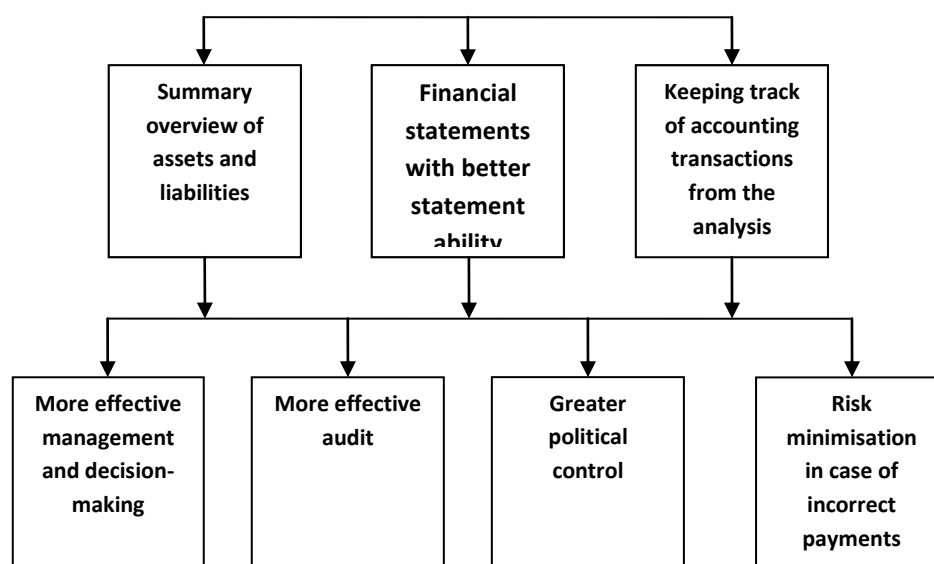
Practical part of the research was focused on the collection and obtaining of information on practical usage of the European standards in practice. These have been implemented in the accounting of budgetary and allowance organisations, municipalities and self-governing regions since 1st January 2008. Since then, these accounting entities have adopted the accrual principle in accounting, i.e. accruals and deferrals of costs, revenues, incomes and expenses also refer to them. Data within the research were obtained from randomly selected municipalities from whole Slovakia. The overall number of distributed questionnaires was 166. They were evenly divided according to individual self-governing regions. The subject of the research was 16 questions regarding practical usage of the European standards and related problems, as well as the assessment of the accrual system in practice in Slovakia. Localities selection (whole Slovakia) was made in order for the research to provide a broad picture of the issue of accrual principle application under individual conditions of whole Slovakia [6-11].

Conclusion

On the grounds of conducted examinations, the present situation in double-entry bookkeeping can be characterised as follows:

- Implementation of International Accounting Standards in practice. This has brought significant changes to public administration accounting, resulting from the requirement of the European Commission. The European Commission started accounting and reporting all transactions on the accrual principle on 1st January 2005 in compliance with the modernised accounting system. The objective of the implementation of a unified state accounting and reporting in SR was to ensure comparability of the outputs of public sector accounting in the Slovak Republic within the European Union countries.
- The new accounting system means the accrual principle application in practice, also affecting the economies of municipalities and towns. The answers show that no significant problems have occurred in its implementation in practice.
- Legislation harmonisation was ensured by adopting the principles of International Public Sector Accounting Standards and their partial application in national legislation regulating the accounting of public sector organisations. Advantages of the accrual system of bookkeeping can be unequivocally expressed by means of the following picture:

Advantages of Accrual Accounting



Picture 1: Advantages of accrual accounting

Accrual accounting from the viewpoint of public sector administration management appears as the only generally accepted system providing necessary information reliably and timely. Harmonised accounting under the accrual principle enhances the transparency, responsibility and comparability of financial

reporting in the public sector and can serve to enhance the efficiency and effectiveness of public audit.

The key objective of a unified state accounting and reporting application has been fulfilled. The implementation of International Accounting Standards principles in generally binding legal

regulations created an adequate legislative environment for accrual principles implementation at the level of accounting entities, consolidated entities and whole public sector.

Public sector budgeting, based on the global budgeting of incomes and expenses, remains a problematic sphere. This issue will be dealt with in other parts of our research.

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