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## PUBLIC FINANCIAL MANAGEMENT REFORMS

# Public Sector Accounting: Why Standards Matter to Cambodia

## Significance

Most people (unless you are an accountant) find accounting pretty boring and dry, but on the other hand, many people find the end result of accounting, namely financial statements, pretty interesting and useful. Accounting is ‘the language of business’ and tells the story of the financial results and health of a public or private entity. When reviewing a national government’s annual financial statements, a reader can find out how much revenue the government received that particular year from taxes (customs, income, VAT, other taxes), from grants or other aid, or from the sale of government property or equipment. Similarly with expenses, a reader can study how much money was provided to and spent by a particular ministry or government entity such as Health, Education, Planning, the Council of Ministers, and so on. But that’s only part of the story!

## Objectives of Accounting Standards

Like any language, accounting has its own rules called Accounting Standards. The objectives of accounting standards are threefold. First, they help to standardize different accounting policies. Second, they facilitate presentation of transparent and comparable information. Third, they minimize subjectivity in financial statements. Once such set of standards for the public sector is the International Public Sector Accounting Standards (IPSAS). IPSAS are global financial reporting standards for governments that set out the requirements that are applicable to all entities.

## The Old Story Line

Public sector accounting in Cambodia is a mixture of accrual and cash accounting with many transactions recorded on an accrual basis. The previous Chart of Accounts (COA)—the list used by government that identifies each item for which money or the equivalent is spent or received—was originally based on the French accounting system and over time was adapted to reflect the RGC’s accounting requirements and practices. It was not designed to handle both accrual- and cash-basis accounting, to facilitate implementing accruals or producing accrual based reports. The categories of the previous COA were different from IPSAS and International Financial Reporting Standards making it difficult for those accountants (or anyone) outside the Cambodia public sector to use or understand. In addition, the COA was

crowded, which meant that classification numbers were full, forcing heavy use of accounts labeled ‘other’. This rendered it practically impossible to track many expenditures or liabilities.

## IPSAS sets out the requirements for the two main bases of accounting:

**Cash-basis accounting:** Accounting method in which revenue is recorded when cash is received & expenses recorded when cash is paid out. The total of these receipts and expenditures are shown in the financial statements of the reporting period whether or not they relate to that period. Example: A government entity enters into a contract for 3M Riels (payment is due after completion of a several tasks) and only records the expense when a particular cash payment is made.

**Accrual-basis accounting:** Based on the ‘accrual’ principal under which revenue is recorded when earned and expenses recorded when incurred (committed). The total of these receipts and expenditures are shown in the financial statements of the reporting period whether or not cash was received or paid out in that period. In the example above, the entity records the entire contract value of 3M Riels at the time the contract is signed.

*Source: IPSASB Handbook, Vol II, 2012.*

## A New Chapter for Public Sector Accounting in Cambodia

In 2012, the RGC adopted IPSAS accounting and reporting standards and agreed to meet the requirements under cash-basis IPSAS and gradually transition over time to accrual-basis standards<sup>1</sup>. It joined the many governments around the world using these standards to prepare their financial statements. In doing so, the Government expressed its commitment to improve the consistency, quality and transparency of its accounting and reporting policies and standards. This change also signals the Government's desire to embrace the future direction of accounting in the country since Cambodian universities now teach either IPSAS or US accounting standards.

### The RGC's new COA meets the 7 principles of internationally recognized good practice:

- **Comprehensiveness**
- **Granularity (sufficient detail)**
- **Mutual exclusiveness**
- **Non-redundancy**
- **Internal consistency**
- **Scalability (flexibility for further additions and changes)**
- **A unified framework**

In the future, the Government will need to provide its cash position, consolidate the statements of all reporting government entities, and ensure these statements are prepared using uniform accounting policies. To facilitate the transition in meeting the requirements under the standard, the Government has prepared a sequenced plan of action (roadmap). As a first step, the Government changed its classification structure and COA—commonly referred to as a uniform Account Code Structure (UAC)—to be consistent with the standard. The next step (currently under way) is the preparation and dissemination of a detailed set of instructions, known as posting rules, for recording and posting all transactions under the new COA. To achieve these immediate and longer-term goals, the National Treasury will be required to lead the development and implementation of a training program to build officials' capacity in the use of these standards.

A key exercise undertaken as part of the roadmap was the trial production of a draft set of government financial statements for 2011 using both the budget-basis and cash-basis financial data to meet the requirements under cash-basis IPSAS. While the prepared document reflects remaining gaps in the financial data available, it does provide the blueprint necessary for further improvements to reporting formats and financial information, and paves the way for the preparation of the 2012 cash-basis IPSAS compliant statements.

## Conclusion

The adoption of IPSAS will make the RGC's accounting processes and reports easier to use and understand as the number of government officials and accountants trained in IPSAS grows and will accommodate the Government's future requirements with an internationally recognized standard. In the future, information provided by these reports will enable those with an interest in tracking the Government's allocations to health, education and other sectors over time, as well as to compare and contrast these allocations against those spent in other countries.

<sup>1</sup> Although very few countries have adapted fully the standards for both cash and accrual accounting under IPSAS, most countries do adhere to the many guidelines and requirements as a matter of good practice.

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