



ACCOUNTING (CASH BASIS AND ACCRUAL BASIS)

*Lucie Rouillard, Retired professor
École nationale d'administration publique
lucie.rouillard@me.com*

Government accounting is an approach for presenting the situation of public finances. This approach consists in a set of standards that are used to report the income and expenditures of a government over a given fiscal year and to present its overall financial situation on a specific date.

References to government accounting date far back in time, with such practices being attested in the kingdoms of China and India as well as among the pre-Christian governments of Athens. Thus, starting a long time ago, control mechanisms were used to record transactions and render accounts to the sovereign so as to ward off losses and fraud. The first phases in the development of accounting systems are characterized by an effort to codify the recording of transactions, a trend that came to the fore between the 16th and 18th centuries. Subsequently, government financial statements would provide a system for controlling the public purse on behalf of a new master, the sovereign people. The field of action and the responsibilities of governments also expanded prodigiously, generating a new complexity that would be reflected in government accounting methods. And, to an ever increasing extent, the public would seek out useful information not merely on *how much* the government collected, spent and borrowed but on *how well* the funds entrusted to it were spent (Premchand, 1995, p. 46). It is this sequence of changes that explains the constant evolution of government accounting principles over the last several decades.

Various accounting approaches have been adopted by governments for the purpose of presenting their financial situation. To begin with, the cash method of accounting means that income and expenditures are recognized (or recorded) whenever cash is received or paid. The cash-based method is appropriate if transactions are recorded with the objective of assessing the government's cash flow. Conversely, accrual accounting refers to a method in which the use of resources is recognized irrespective of when a cash transaction takes place (Bhatta, 2006, pp. 7 and 82). This approach is used more with the aim of assessing the flow of a government's economic resources (or the cost of the services provided by the government).

For several decades now, government accounting principles have shifted between these two poles, moving from the cash basis to a modified cash basis and, more recently, to full-accrual accounting. Traditionally, governments have opted for the modified cash basis of accounting, which entailed travelling a considerable distance toward an accrual basis of accounting. Under the modified cash basis, a government must record income whenever the latter is on hand and measurable – i.e., when it is practically certain that the cash or financial asset has been received. Likewise, a government must register its expenditures whenever it receives a liability or has been billed for a service (Glick, 1990, pp. 17-18).

ACCOUNTING (CASH BASIS AND ACCRUAL BASIS)

With the advent of the new public financial management, an outgrowth of the New Public Management (NPM), the modernization of government finance systems has sought primarily to increase efficiency, effectiveness and accountability in the public sector. For several governments, the preferred vehicle of modernization efforts has consisted in the transition to accrual accounting (Olson, Humphrey and Guthrie, 2007, p. 5), an approach that until lately was the preserve of private enterprise. From the perspective of governments, accrual accounting is more of a reflection of the moment when a manager has committed to performing a transaction (e.g., authorizing severance pay) than of the moment when this transaction is actually concluded. In addition, this approach provides a basis for recognizing the value of physical assets, such as land, buildings, facilities, operating systems, etc., in a government's financial statements (Aubry, 2004, p. 2). The expected outcome is thus a snapshot of government finances offering greater credibility and transparency and that lends itself more readily to comparisons with other governments.

It is worth noting that the choice of an accounting method is the full prerogative of governments. In actuality, however, the federal and provincial governments of Canada have strived to apply the accounting principles recommended by the Canadian Institute of Chartered Accountants, which, since 2005, has established full-accrual accounting as the standard (Christie, 2009, p. 11).

Several questions arise in relation to recent trends involving government accounting methods, chief of which being the adoption of full-accrual accounting, mirroring private sector practice. Public accountants have, as a rule, looked favourably upon the modernization of government accounting methods, stressing the superiority – in terms of democracy – of relying on independent standards that are shielded from political motivations and that are thus better able to safeguard the public interest. Other observers note, however, that governments are fundamentally different from business enterprises and wonder how private sector standards will be able to meet the accountability requirements specific to governments (Christie, 2009, p. 12). Others point to the inherent complexity of using the accrual basis of accounting, and challenge the argument according to which this method enhances the transparency of financial statements. At issue, in short, is whether or not full-accrual accounting will be able to ensure the financial accountability of a government vis-à-vis legislatures and whether or not it is genuinely conducive to more enlightened decision-making on the part of politicians. (Olson, Humphrey and Guthrie, 2007, pp. 19-23).

Bibliography

- Aubry, J.-P. (2004). *Progrès dans la comptabilité de nos gouvernements*, Association des économistes québécois, Comité des politiques publiques, Document CPP 2004-02.
- Bhatta, G. (2006). *International Dictionary of Public Management and Governance*, Armonk, NY, M.E. Sharpe.
- Christie, T. (2009). *Accrual Budgeting by Canadian Federal, Provincial and Territorial Governments*, Toronto, The Canadian Institute of Chartered Accountants.
- Glick, P. E. (1990). *A Public Manager's Guide to Government Accounting and Financial Reporting*, Chicago, Government Finance Officers Association.
- Gouvernement du Québec (2007). *Rapport du groupe de travail sur la comptabilité du gouvernement*, Québec, Ministère des Finances.
- Gouvernement du Québec (1998). *Rapport du Comité d'étude sur la comptabilité du gouvernement*, Québec, Ministère des Finances.

ACCOUNTING (CASH BASIS AND ACCRUAL BASIS)

- Government Accounting Standards Board (2007). *Why Governmental Accounting and Financial Reporting Is – And Should Be – Different*, www.gasb.org/white_paper_full.pdf (last retrieved in April 2010).
- Government Finance Officers Association (1994). *Governmental Accounting, Auditing and Financial Reporting*, Chicago, Government Finance Officers Association.
- Khan, M. (2003). “Accounting, Financial,” in J. Rabin (ed.), *Encyclopedia of Public Administration and Public Policy*, New York, Marcel Dekker, Inc., pp. 15-20.
- Olson, O., C. Humphrey and J. Guthrie (2007). *Into the Shadows: A Reflection on International Developments in Public Sector Accounting*, 30th Annual Congress of the European Accounting Association, 25-27 April, Lisbon, Portugal.
- Premchand, A. (1995). *Effective Government Accounting*, Washington D.C., International Monetary Fund.
- Rose, P. (1998). “Financial Reporting,” in F. Thompson and M. T. Green (ed.), *Handbook of Public Finance*, New York, Marcel Dekker, Inc., pp. 523-556.
- Schiavo-Campo, S. and D. Tommasi (1999). *Managing Government Expenditure*, Manila, Asian Development Bank.

REPRODUCTION	Reproduction in whole or part of the definitions contained in the <i>Encyclopedic Dictionary of Public Administration</i> is authorized, provided the source is acknowledged.
HOW TO CITE	Rouillard, L. (2012). “Accounting (cash basis and accrual basis),” in L. Côté and J.-F. Savard (eds.), <i>Encyclopedic Dictionary of Public Administration</i> , [online], www.dictionnaire.enap.ca
INFORMATION	For further information, please visit www.dictionnaire.enap.ca
LEGAL DEPOSIT	Library and Archives Canada, 2012 ISBN 978-2-923008-70-7 (Online)