
ACCRUAL ACCOUNTING ADOPTION IN THE ROMANIAN PUBLIC SECTOR

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Abstract

In Romania the development of public sector accounting was initiated in 2002, and enlarged for all public sector entities in 2005, but the transition is a static process although there are many issues that should be changed. Based on Hepworth's (2003) preconditions of success in adoption accrual accounting for public sector, this paper aims to analyse through a qualitative research whether accruals implementation in Romanian public sector was fulfilling its purposes or not. Financial information disclosed through public sector entities' financial statements make the connection between citizens and state over the last one's capacity to respond to community's goals.

Keywords: public sector, accrual accounting, preconditions

This paper uses a qualitative research approach in order to estimate whether the implementation of accrual accounting in Romania was a success or not. The method of research used for achieving the research goal is the descriptive case study based on the preconditions enumerated by Hepworth (2003). The techniques of research used were semi-structured, individual interviews and documentary analysis. For each of the preconditions we tried to find clues in the accrual accounting system of Romania based on literature review, prestigious international indexes, regulations in force in Romania, opinions expressed by the representatives of government in different official scientific or professional events. Consequently, all these clues and findings have been discussed and analyzed in order to conclude whether the precondition has or has not been met.

Hepworth critically analyses the trend of adopting accrual accounting in the public sector, being aware in the same time, of its potential benefits. Supported by developed nations and international credit institutions such as International Monetary Fund and World Bank, this transition to accrual accounting in the public sector can be a requirement from the funds providers or a fashion trend. Hepworth states that no matter the argument for the transition, this switch must be understood and acted properly if its purposes are desired to be achieved. He identifies countries with important disclosures

on the transition process (such as New Zealand, Sweden), countries that switch to accruals but do not disseminate advantages, difficulties, results in an exhaustive manner (Hepworth mentions Croatia, while the author would add to this particular list Romania) and countries that performed research and impact studies before making the decision of switching to accruals (Norway and The Netherlands).

The culture in accounting perception should be changed, as it is an integral and very important part of financial management, going beyond financial reporting purposes. This is Hepworth's opinion who states that looking at accrual accounting only as a new accounting technique would be a mistake. Accrual accounting should manifest itself for accrual budgeting so that actual and budgeted inputs can be easily compared.

NPM philosophy requires a closeness of the public sector management culture to that of the private sector. In terms of accounting, Hepworth identifies issues such as the valuation of assets, efficiency in their use and the cost of capital that must be addressed through a new perception which involves a management change in the public sector. The same change is to be needed in Hepworth's opinion in terms of the "thinking" of legislature and executive powers of the state.

The internal control in public sector is another issue considered by Hepworth in his study as influencing the success of adoption accrual accounting. The executive has to loosen up the control over its subordinates managers, otherwise the benefits from the extra information disclosures that accrual accounting can give are not to be achieved.

Another important issue with crucial consequences for the success of accrual accounting in the public sector is the settlement of accounting standards. Hepworth pleads for the co-operation between the governments (through the ministries of finance) and, at least, the national accounting profession. This cooperation has at least two benefits: the government can benefit from the accounting profession expertise and the issue of accounting standards that serve the executive's own political interests is avoided. Independent audits must also be involved in the accrual accounting transition process, Hepworth also believing that the external auditor of the government should play an important role in this accruals adoption.

Hepworth's (2003) preconditions are enumerated and for each one of them comments and results of the research are added for the case of Romania.

- *"Consultation and acceptance are indispensable to the introduction of accrual accounting, without them there will be neither understanding nor acceptance"* (Hepworth).

According to studies performed within public sector institutions,

public sector accountants consider the accrual accounting system only an imposed rule (Tiron Tudor *et al.*, 2008, Dumitru *et al.*, 2009) and there is a huge need of training for the accountants in the public entities. The public sector accounting reform started in 2002 when a Government decision established the use of accrual accounting in addition to cash accounting. In 2005, several pilot entities were involved in the full accrual accounting implementation process, the transition to accrual accounting being performed for all public sector entities in 2006. However, for the pilot entities there was not any public informing whether the project was a success or not.

• *“The accountancy profession must have the capacity and be prepared to be interested in and involved with the public sector, because not only is the accountancy profession the expert in accounting standards but it has traditionally trained financial managers for the private sector”* (Hepworth).

The accounting profession in Romania is represented by The Body of Licensed Accountants and Experts Accountants in Romania (CECCAR). However, the accountants in public sector do not have the obligation of being CECCAR members, and, much more, if one accounting expert is employed in a public sector institution he/she is declared inactive from the CECCAR point of view. Only the chief accountant or the manager of the financial department is obliged to have a bachelor’s degree in economic studies. Even if the CECCAR has tried to organize training sessions and publish professional guides for public sector accounting, its initiatives were not very successful. This is a conclusion derived from the semi-structured interviews performed individually with the managers of regional offices of CECCAR. The employment of public sector accountants in public sector entities is based on laws issued by or with the approval of the Ministry of Public Finance, CECCAR not being involved in this process in any way.

CECCAR connection with public sector accountants has been marked through the publishing of several books, manuals on public sector accounting and through the translation of IPSAS in 2009.

• *“To be successfully implemented and operated, the reform requires an increase in the number of financial managers (who may be qualified accountants) employed by government and an acceptance of their contribution to the efficient and effective management of the public services. There also needs to be a willingness to meet the financial management education and training requirements of the public sector, either directly by the accountancy profession or through other institutions”* (Hepworth).

Romania is characterized by a too small number of public sector

accounting specialists and a doubtful quality of their work. These assertions are supported by the following analysis:

- the Ministry of Public Finance claims a further increase in the number of personnel in accounting departments of public sector entities and also in the Department of Public Sector Accounting methodology inside the above mentioned Ministry (Alec, 2012).

- the Accounting Law contains a provision that public sector institutions can externalize accounting services based on contracts concluded according to legal requirements with certified accountants (CECCAR). However, generally, public sector institutions do not use this legal prescription, and the arguments could be: the control of information is better ensured with an employee than an external accountant; the public acquisitions procedures for contracting an accounting service are too bureaucratic; the fee for an external accountant may be greater than the salaries' expenses with the persons employed on accounting positions (there are local governments, especially communes, where there is only one accountant whose salary is usually below the average salary in the economy).

- The need for further training in public sector accounting is recognized by the representatives of central government (Alec, 2012) and by empirical studies (Tiron Tudor et al., 2008; Calu et al., 2008; Dumitru et al., 2009; Tiron Tudor, 2010).

- There are only several types of public sector entities who employ managers on performance criteria and that require a management contract with indicators to be fulfilled (for instance, the managers of the hospitals). For the rest of the managers employed on a salary basis, the efficiency and effectiveness of their management is not necessarily a priority.

- Vasile (2012) synthesized the effects of the economic crisis for Romanian public sector personnel: the proportion of persons at low incomes increased, poverty among lower qualified personnel in the public sector has also raised in the crisis years, specialists leave the system to private sector or migration, there is no stimulus for the university graduates to develop a career in public sector.

- *"Another essential element is co-operation by the accountancy profession in the development of accounting standards for the public sector and to become involved in the application of those standards and the monitoring of their implementation"* (Hepworth).

Based on pre-accession funds, in 2002 there has been developed an impact study that analyzed the benefits of accrual accounting, the cost of transition (IT systems, personnel training, etc.), the calendar of transition

and the need for an external audit during the implementation process. So far, no external independent audits have been performed for the accrual based financial statements of Romania's public sector entities.

The accounting profession is not involved in the development of accounting standards for the public sector, this task is the exclusive privilege of the Ministry of Public Finance, although it admits the need of twinning programs that reunite public sector with private sector expertise (Alec, 2012). Also, CECCAR has never been involved in the application or monitoring of accrual accounting implementation. Thus, it is reasonable to believe that the Ministry of Public Finance is seen as setting its own accounting standards and apply them in a manner that suited the political circumstances of the moment (Hepworth, 2003). The damage to the process is that it misses credibility, and in the end it does not reach its purpose. There was not a critical appraisal of the process of adoption accrual accounting on behalf of the accounting profession.

•"Successful implementation of accrual accounting depends heavily upon the understanding of, and willingness to support, the system by the external auditor of central government. (...) the external auditor should be involved in the process from the outset. That may require that the organization, career structure and training of auditors should be significantly changed as well as the audit approach and mandate. (...) That may require the appointment of qualified accountants to the staff of the central government auditor, rather than relying upon the more traditional training of auditors" (Hepworth).

Preparation of financial statements is subject of internal audits which are not required to be performed on an annual basis. Financial statements are also verified by the national Court of Accounts which performs an external audit. The Court of Accounts has the competence of discharging the management's institution for each budgetary year, but the audits are not necessarily performed every year, but two or three years and then the discharging is made for each year. The external audit is mainly concerned with legality of expenses and respecting the legal procedures and it is less preoccupied with the judgments made for assets valuations, prudence, materiality, etc.

Internal auditors in public sector entities are not required to be members of the statutory audit professional organism (The Romanian Chamber of Financial Auditors) and most of them are not. Their requirements for professional training resemble to those described for accountants employed in public sector. The external auditors of the Court of Accounts are also not obliged to be members of CECCAR or the Romanian Chamber of Auditor. These assertions based on provisions of national regulations in force make us wonder how pertinent are the opinions expressed by the auditors (external or

internal) from the accrual accounting objectives point of view.

As accrual accounting in public sector requires special attention due to its particularities, the training of auditors also implies more advanced training courses so that they can handle properly the difficult concepts.

• *“A comprehensive management-training programme for line managers in how to use an accrual accounting system is essential, so they can derive benefits from its operation. (...) To make proper use of an accrual accounting system, managers not only need to understand the differences, but also need to appreciate how they can use the accrual-based information to manage activity more efficiently and effectively”* (Hepworth, 2003).

Usually, when implementing accrual accounting, training sessions were designed for the accountants and not for managers. This focus determined little understanding from the management of what accrual accounting means and the possibility of using the information derived from the accrual financial statements in the best interest of the entity’s efficiency and effectiveness. The perception “accounting is an accountant job” is still used as the management, as mentioned before, is not yet held responsible for the results of the entity and is not educated to understand what the accounting is good for in a public sector entity.

• *“There must be a public sector cultural ethic that has internalized the requirements for a neutral (i.e. non-political) civil service, with a strong, well-regarded central agency (the ministry of finance) responsible for the management of government finances. There need to be well-understood and accepted systems of budgetary control over departments, coupled with a willingness to promote line ministry control and the management flexibility that that requires”* (Hepworth).

The public sector ethic is quite limited, the general perception being that civil service is, at least for the head positions, under political influence. The systems of budgetary control over departments are very strict as well as the line of ministry control which gives management little flexibility. A proof in this respect is the National Report on Corruption 2011 prepared by Transparency International Romania that mentions and discusses the involvement of political spectrum in public administration. (National Report on Corruption 2011, http://www.transparency.org.ro/politici_si_studii/studii/national_coruptie/2011/RNC2011.pdf, pages 28-30).

• *“A comprehensive, annual independent audit of the accounts of each government ministry or department is essential at the end of each financial year, with reports to the legislature and detailed scrutiny where appropriate”* (Hepworth).

As mentioned before, independent audit is not required for public sector institutions, irrespective their level of hierarchy. There also can be

mentioned here that public sector entities are not subject, according to the law, to making publicly available their financial statements or internal audits reports, thus being explained, in our opinion, at least in part, the absence of an independent auditor, “too curious” and too transparent. The Chamber of Financial Auditors of Romania (CAFR) is involved in auditing public sector entities only for reports on projects funded from non-reimbursable funds received from EU. However, under these circumstances, the audit reports have as scope only the project itself and not the entire activity of the entity.

•*“There must be no systemic corruption, and no informal parallel processes that are allowed to complement the formal processes should exist. The prevailing culture should ensure that rules specified about the introduction of accrual accounting and budgeting will be obeyed”* (Hepworth).

Romania’s public sector, according to Transparency International Corruption Index 2012 scores an amount of 44 among 176 countries, on a scale of 0 to 100, where 0 means highly corrupted country and 100 means a “very clean” sector. Romania’s standing in the middle of the classification, means that the climate of honesty and fairness claimed by Hepworth is only half accomplished. Public sector entities have only recently developed Codes of Ethics, most of them being prepared as a requirement of the implementation of managerial control. Rules about introduction of accrual accounting and budgeting are obeyed as “this was asked for” and not because the prevailing culture said so, studies (Tiron Tudor et al. 2008, Dumitru et al., 2009) performed so far have already established this reality.

Other authors (Androniceanu, 2011) prove that although transparency is one essential prerequisite for increasing the quality of public administration (the study analyzes this for the local level public sector) yet there are still serious problems in implementing the legal provisions concerning the transparency of public sector information.

•*“From the outset, there must be a willingness to recognize that the introduction of accrual accounting and budgeting will take time— usually stretching beyond the lifetime of one legislative term and potentially beyond the period of office of one political party. The reform therefore needs widespread support across the political spectrum”* (Hepworth).

Accrual accounting, its principles and advantages, have not been disseminated too much to the Romanian political spectrum while the budgeting is still performed on a cash basis. Accrual accounting has been introduced not because it has been perceived as a necessity and an improvement, but as a requirement of adhering to European Union. The political spectrum was involved in accrual accounting adoption only as the supplier of Government members, as the Government is usually formed of politicians from the party

owing the majority of votes in the Parliament in a certain period of time. The accrual accounting for public sector entities was introduced through Order of the Ministries of Finance (in 2002, 2005) and not by laws that must be approved by the Legislative power, that is the Parliament. The interest for accrual accounting implementation in public sector entities was quite low, as it was a prerequisite for Romania's harmonizing its regulations with the European ones, in order to become a member state of the EU.

•*”There must be an IT capacity that is able to respond to the new and additional requirements that the introduction of accrual accounting and budgeting will introduce (for example charging for the cost of capital”* (Hepworth).

Public sector institutions use IT capacities able to support the requirements of accrual accounting, but improvements are necessary and at present there is one important project developed by the Ministry of Public Finance, financed through the European Social Fund and entitled “The increase of public administration responsibility through the modernization of IT system for reporting financial statements of public sector entities” http://discutii.mfinante.ro/static/10/Mfp/afaceri_europene/anunt_demarare_proiectSMIS34952.pdf.

•*”There must be the capacity to develop and apply financial incentives and penalties to encourage a practical day-to-day management approach that looks for more efficient ways of using resources and delivering services”* (Hepworth, 2003).

Public sector personnel is paid based on fixed salaries established by provisions of laws on categories of functions, years of functions and studies, and the financial incentives do not exist. There were some bonuses paid to public sector employees but when the economic crisis arrived they were suppressed and even more, the financial resources allocated to personnel expenses reduced the employees' performance and their motivation in the last years (Vasile, 2012).

•*”The introduction of accrual accounting and budgeting should be seen as part of a wideranging process of reform, and it has not ‘parachuted’ into a stable, unchanging management process”* (Hepworth, 2003).

Hința (2011) citing Profiroiu (2006) states that the evolution of public sector reform in Romania has been a “lot more intense and chaotic” than the processes developed in Western countries. The deficiencies of the process are partially due to a weak managerial ability of state and public sector entities. In Hința's opinion some of the things to be done for a true reform should be:

- reconsidering the size of the state, in terms of being more flexible and much better organized;

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- changing the role and the functions of the public administration
 - governance and quality should be top priorities in a new management policy of the state, these being in direct relation to performance;
 - significantly decrease in bureaucracy and increase of managerial capacity;
 - more involvement of private sector and NGOs in public sector.

Therefore we cannot appreciate that introduction of accrual accounting was “parachuted” into an unchanging management process. However, accrual accounting as implemented in Romania still pays tribute to some old concepts that remained from the economic and administrative point of view inside regulations that govern public sector. Among these concepts derived from the old perception of public sector management we can enumerate: “passive”, “patrimony” (which is divergent from prevalence of substance over form concept, stipulated by regulations), the maintenance of the funds, the different treatment for the fixed assets belonging to the public domain of the state and to the private domain of the state, etc. There are also elements of novelty that accrual accounting could bring, such as segment reporting, the possibility of capitalizing borrowing costs, employees benefits, fixed assets investments, pension liabilities, etc., but they cannot be accounted for as the necessary economic and administrative framework for their implementation does not exist.

Conclusions

Adoption of accrual accounting is a long and demanding process for governments. Either a requirement or a self government decision, the transition process involves more than a change of techniques. There are many factors to be considered so that the process achieves its goals. Based on the preconditions synthesized by Hepworth (2003) we tried to analyse the Romanian success of adopting accruals for public sector accounting. The results are that some of the preconditions are not met at all and others are met only in half. However, the government authorities acknowledges that there are problems in the accrual accounting of public sector entities (Alec, 2012) which makes us conclude that in the future, near or far, the accrual accounting in Romania will enter the right path and its objectives will be fully accomplished.

The **limits of our research** are the use of oral history for evaluating some of Hepworth’s (2003) preconditions and the little accounting literature in the field. One of the difficulties of the paper was the lack of information publicly available over public sector accounting and the transition process. The other limit mentioned concerns the fact that Romanian literature on public sector accounting topics is not very vast and the studies analyzed have

different objectives, that is the adoption of accrual accounting and the syncope in the process were not put and explained in an economic, social, political and organizational culture context for our country.

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