IMPLEMENTATION OF ACCRUAL ACCOUNTING: THE IMPACT ON PUBLIC SECTOR AUDIT

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About FEE

FEE (Fédération des Experts comptables Européens – Federation of European Accountants) represents 43 professional institutes of accountants and auditors from 32 European countries, including all of the 27 EU Member States.

In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 500.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent, and sustainable European economy.

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1. EXECUTIVE SUMMARY

The implementation of accrual accounting in the public sector has been identified as a fundamental change for the public sector. Under accrual based financial reporting it is important that an audit verifies that the financial statements of the audited entity give a true and fair view of the net assets, financial position and results of operations in accordance with the relevant financial reporting framework.

FEE has therefore produced this discussion paper to examine what impact the introduction of accrual based accounts has had on public sector audit in Europe. The key source used to prepare this paper was a questionnaire that was sent to selected public authorities in European countries via their FEE Public Sector Committee representative. Between March 2007 and April 2008, FEE received questionnaire responses from 26 countries. Of the 26 respondents 15 have already introduced some form of accrual accounting at the national level and 20 at the local level.

In the majority of the responses, the responsibility for the audit of the financial statements of the national government remains in the hands of the respective supreme audit institution. About 50% of the supreme audit institutions employ staff with a professional accountancy qualification for the financial audit. In all of the analysed countries, the audit of the accrual based financial statements of national government is conducted on the basis of auditing standards. In most of the cases, the auditing standards are based on the ISA or the ISA are applied directly. In the other cases, the audit of the financial statements are conducted in accordance with INTOSAI based standards.

At the local level the results are different. Three groups of countries could be identified. In about one third of the responding countries the responsibility and the performance of the audit of accrual based financial statements is assigned to a centralised audit institution/office outside local government. In the second third the audit of the accrual based financial statements is performed by private sector auditors. In this group the private sector auditor is generally appointed by the local council. In the last third the person or institutions who performs the financial audit depends on different legislation/requirements which in most cases relate to the size of the municipality. In this group there is a tendency that bigger municipalities have their own audit office and smaller municipalities appoint a private sector auditor. Also on the local level in most of the cases, the auditing standards are based on the ISA or the ISA are applied directly.

Conclusion

The implementation of accrual accounting has had a significant impact on public sector audit. However, this has not been considered as a reform of the auditing by most of the respondents. In particular, those Supreme Audit Institutions that employ qualified auditors were well placed to respond to the audit challenges they faced by the introduction of accruals accounting.

The following key messages were obtained from the questionnaire responses and related research:

- The audit of accrual based financial statements is more complex and causes more judgements to be made by the auditor than the audit of cash based financial statements;

- It was generally found that the audit is performed by suitable auditors who are qualified either by exams or by trainings and experience;

- Subcontracting all or part of public sector audits to third parties (usually private sector audit firms) can help to bring specialist skills to those audits where those skills are not present in the public sector audit body. It can also ensure that public sector audit bodies maintain their audit methodologies in line with best practice in the private sector;

- Where the person responsible for the audit does not have the relevant expertise (for example a local council responsible for appointing an auditor for a local government audit), the council should ensure that whoever it appoints (whether private or public sector auditor) has the relevant public sector and audit knowledge;

- Whoever performs the audit at the local level would benefit from auditing several local government entities so as to gain the necessary experience which ideally can not be achieved by one audit a year;

- The educational requirements for the majority of bodies responsible for performing public sector financial audits was consistently high across the countries who responded. In most cases, the move to accruals accounting did not increase those educational requirements. However, all bodies needed to ensure that either their professional training covered the accruals accounting principles or had to provide specific training to their staff in those principles. Therefore professional syllabi may need to be reviewed to ensure that they meet the needs of public sector audits, this might also comprise aspects on compliance audit;

- Because the audit of accrual based financial statements is more complex and judgemental the application of generally accepted auditing standards is necessary to assure a uniform audit quality. The International Standards on Auditing (ISA) of IFAC are such generally accepted auditing standards in the public sector; and

- Quality control procedures in audit bodies may need to be enhanced with the introduction of accruals based financial statements, as audit judgements become more significant.

2. OBJECTIVES OF THE STUDY

2.1. The trend towards accrual accounting

FEE published in January 2007 a paper on *Accrual Accounting in the Public Sector*[1] based on a survey of 17 countries. The paper examined the progress being made by European countries, at both national and local level, in the implementation of accrual based accounting in the public sector. The paper highlighted a continuing trend in Europe to shift away from traditional cash based accounts towards the adoption of accrual based accounts.

The move from cash to accrual based accounts has a significant impact on those preparing the financial statements. Accruals based accounts include both a statement of financial performance (income statement) and a statement of financial position (balance sheet). The statement of financial position requires preparers to perform valuations of assets and liabilities.

The implementation of accrual accounting in the public sector has been identified as a fundamental change for the public sector. Accrual accounting facilitates better planning, financial management and decision making in government as well as a robust and accepted way of measuring the economy and efficiency of public policies. Furthermore, one of the objectives of financial reporting is to allow accurate comparison to be made between different organisations. The use of the accrual basis for public financial statements will increase comparability of public sector organisations, whilst retaining the comparability of an individual organisation on a period by period basis.

2.2. The impact on public sector audit

Under accrual based financial reporting, it is necessary that an auditor verifies that the financial statements of the audited entity give a true and fair view of the net assets, financial position and results of operations in accordance with the relevant financial reporting framework.

In its 2003 paper *The Adoption of Accrual Accounting and Budgeting by Governments*, FEE remarked that:

> "successful implementation of accrual accounting does depend heavily upon the understanding of and willingness to support the system by the government external auditor. As accrual accounting requires not only more complex systems but also a range of new judgments (e.g. about asset values and lives, matching issues, prudence and materiality), the responsibilities and expectations of the auditor will increase and change considerably. Therefore, the external auditor should be involved in the process from the outset. That may require that the organisation, career structure and training of auditor staff should be significantly enhanced. Auditors will need a thorough understanding of accounting principles and how those principles can be maintained under the pressure of day-to-day administrative decisions. That may require the appointment to the government audit staff of qualified accountants (ideally members of a professional body), rather than relying upon the more traditional training of auditors"[2].

[1] The FEE Paper is available at http://www.fee.be/publications/default.asp?library_ref=4&category_ref=44&private=False&content_ref=635.

[2] The FEE Paper from 2003 "The Adoption of Accrual Accounting and Budgeting by Governments" is available at http://www.fee.be/publications/default.asp?library_ref=4&category_ref=44&private=False&content_ref=263.

FEE has therefore produced this discussion paper to examine what impact the introduction of accrual based accounts has had on public sector audit in Europe. In particular, the paper focuses on the following areas:

1. The commissioning of audit experts from outside the public sector auditing profession;

2. The educational background, professional training and qualifications of the persons who perform the audit of the financial statements;

3. The application of auditing standards; and

4. The introduction of a quality control system.

The paper seeks to identify whether the introduction of accrual based accounts represented a fundamental reform of public sector audit. It also seeks to identify some common areas of good practice for those who have made the change from cash to accruals, to assist those who may be making the change in the future.

The adoption of IPSAS and IFRS (for example by the UK Government from 2009-2010) presents further challenges for the auditor.

2.3. Methodology

The key source used to prepare this paper was a questionnaire that was sent to selected public authorities in European countries. The questionnaire was circulated in March 2007 and is attached at Annex A. The questionnaire comprises seven sections totalling 18 questions. Some of the questions offer a choice of answers, but most of the questions ask for a description. The respondent was asked to complete the questionnaire for three levels of government; the national or federal level, the state or regional level, and the local level of government for their respective country.

Between March 2007 and April 2008, FEE received questionnaire responses from 26 countries. A list of those who responded is included at Annex B.

The responses to the questionnaire were then analysed and the results are reported in this discussion paper. Following the analysis, it was decided not to report the findings in two particular areas:

- Clear analysis could not be performed for the state or regional level of government. Not all countries who responded have three levels of government (e.g. Finland, Israel and Poland), and the different ways in which regional government is organised in those countries which do make it difficult to identify clear trends; and

- Section two of the questionnaire asked for information about the objectives of the audit, and section four asked for information about the reorganisation of the audit process. Clear trends were not identified from the responses to these sections.

This paper therefore analyses the responses at two levels of government (national and local) in the four areas described above.

However, as with any survey, the responses and therefore any analysis performed on them, should be treated with care for the following reasons:

- The report is based solely on the results from those countries which responded. The trends identified are necessarily limited to those responses and no assumptions should be inferred from those countries from which responses were not received;

- The way that the questions were framed was open to interpretation by the respondents depending on their own circumstances;

- An international survey bears the risk that technical expressions are interpreted by the questioner and the respondent with a different meaning due to a different language background; and

- The bias of the persons who analysed the questions might also have some impact on the interpretation of the results.

3. RESULTS ON THE NATIONAL LEVEL OF GOVERNMENT

3.1. Introduction of Accrual Accounting by the Analysed Respondents

The questionnaire asked the respondents to state whether they had introduced accrual accounting at the national level. Of the 26 respondents, 15 have already introduced some form of accrual accounting at the national level of government, with introduction ranging from full implementation in some countries to partial introduction in others. Table 1 gives an overview of when accrual accounting was introduced and to what extent for those 15 countries.

Table 1: The introduction of accrual accounting at the national level

Country	Introduced	Comments
Spain	1983	Accrual based accounting was introduced for the federal government of Spain in 1983. By 1994 a new Accounting Plan for the Public Sector was approved in order to align the accounting rules/standards with those for the private sector.
Portugal	in the early 1990´s	
Sweden	1991	In Sweden only parts of the central government have introduced accrual accounting.
Netherlands	1994	In the Netherlands accrual accounting was not introduced government-wide, but since 1994 parts of the government (executive branches) have used an accrual based accounting system. In 2008 40 executive branches, which represent 60% of all employees of the national government, account on an accrual basis.
Italy	1997	In Italy accrual accounting has been introduced for the central government by the “accrual accounting centralised system” developed by the *Ragioneria Genrale dello stato* (operating under the supervision of the Ministry of Finance).
Finland	1998	
United Kingdom	2000	In the United Kingdom the requirement for accrual accounting (termed “resource accounting”) was introduced for financial years beginning on or after 1 April 2000. From 1 April 2009 the UK will be implementing IFRS for the public sector.
Malta	2002	In Malta accrual accounting has not yet been introduced officially, but since 2002 an additional set of financial statements are prepared on the accrual basis of accounting for internal purposes.
Denmark	2002 - 2007	In Denmark by May 2002 the government published a policy for the introduction of accrual (cost based) accounting in the entire public sector and for assessing the possibilities for accrual budgeting. Pilot projects were carried out in state administration 2003-04. By mid 2004 government decided to implement full scale accrual accounting in the central administration as from 2005 and full scale implementation of accrual budgeting as from 2007. By the turn of the year 2007/08 this reform has become fully implemented throughout central administration (ministries,

		agencies, state institutions etc.). National heritage, public infrastructure (rails, roads, bridges etc.), grants and transfers such as old age pensions are not included in the balance sheet.
Latvia	2003	Latvia introduced accrual accounting for the federal level of government in order to comply with the International Financial Reporting Standards (IFRS/IAS) and the International Public Sector Accounting Standards (IPSAS).
Israel	2004	Israel implemented accrual accounting not for the entire federal government, but for eight ministries.
France	2006	In France accrual accounting was partially introduced in the 1990´s, with full implementation since 2006.
Romania	2006	In Romania accrual accounting was introduced in 2005 as an experiment. In 2006 it was introduced officially.
Switzerland	2007	In Switzerland starting January 1, 2007 the Neues Rechnungsmodell (NRM) was introduced for the federal level. The NRM follows the IPSAS[3].
Slovak Republic	2008	In the Slovak Republic the new accounting standards on an accrual basis became effective on the 1st of January 2008.

Some of the respondents, for example Israel, the Netherlands and Sweden, have introduced accrual accounting for part of the national government (such as certain ministries or executive branches). As the financial audit of these countries includes those parts that have accounts prepared on an accruals basis, they are included in the following analysis.

In addition to the 15 countries shown in the table, Austria (2013), Czech Republic (2010) and Lithuania (2009) responded that they will soon be introducing accrual accounting at the national government level. As this report covers the current requirements for audit, their responses are not included in the following analysis.

[3] The principle of prudence of the Swiss Code of Obligations is replaced by the principle to present fairly the financial position, financial performance and cash flows (true and fair view). This change requires a systematic revaluation of the accounting and revaluation of all balance sheet items. The adoption of accrual accounting and budgeting as well as the assimilation (in accordance to art. 53 of the Federal Public Budget Regulation) to the International Public Sector Accounting Standards (IPSAS) strengthens the relevance of the federal balance sheet and increases its explanatory power. See NRM Eröffnungsbilanz per 1. Januar 2007, Bericht des Bundesrats über die Anpassungen der Bundesbilanz per 1. Januar 2007 an die Grundsätze des Neuen Rechnungsmodells Bund (NRM), p. 5.

3.2. *Contracting of Third Parties*

Each of the 15 countries which have implemented accrual accounting at the national level of government has a supreme audit institution. In 8 of those 15 countries, the supreme audit institution or a part of government can subcontract the audit of the financial statements or certain audit tasks to a third party, usually a private sector audit provider. Where whole audits are not sub-contracted (for example the Cour des comptes in France and the Rigsrevisionen in Denmark), the supreme audit institution can engage external specialists or private audit firms for specific tasks such as IT audits or actuarial calculations of pension schemes. In these cases, the audit report and the responsibility for the quality of investigations remain solely at the supreme audit institution. As a further example, in Switzerland the Swiss Federal Audit Office is responsible for the audit of the national government, but it subcontracts audit work to third parties when expert knowledge is needed or in case of missing human resources.

As mentioned previously, in Israel just eight government ministries have implemented accrual accounting. The audit of the financial statements of those ministries is performed by eight different private sector audit firms.

In the Slovak Republic, only members of the Slovak Chamber of Auditors (“Slovenská komora audítorov” (SKAu)) perform the audit of the financial statements in the public sector. The members of the Slovak Chamber of Auditors are appointed by appropriate parts of the government within the control system. The Slovak Chamber of Auditors is a member of IFAC and FEE, its members are auditors and audit firms. Accrual based accounting was just introduced in the Slovak Republic. Therefore accrual based financial statements of national government will be audited in 2010 for the first time. The respective auditor, a member of the Slovak Chamber of Auditors, is not appointed yet. In contrast, the Slovak Supreme Audit Institution (Najvyssí Kontrolný Úrad) has the responsibility to control whether the national government kept within the allocated budget and the budget rules.

7 of the 15 countries responded that the supreme audit institution does not have the possibility to subcontract audit work (Finland, Italy, Latvia, Malta, the Netherlands, Romania and Sweden).

Table 2 shows whether audit tasks are subcontracted out or not and the percentages of financial audit work which is subcontracted to third parties.

Table 2: Countries that subcontract audit work and the amounts subcontracted

	Possibility to subcontract a third party for the audit or specific tasks	**Percentages of subcontracted audit work Approx.**
Denmark	Yes	20 %
Finland	No	
France	Yes	5 to 10 %
Israel	Yes	100 %*
Italy	No	

Latvia	No	
Malta	No	
Netherlands	No	
Portugal	Yes	not specified
Romania	No	
Slovak Republic	Yes	100 %
Spain	Yes	Near to 0 % **
Sweden	No	
Switzerland	Yes	Not specified
United Kingdom	Yes	25 to 35 %

* The 100% does not relate to the national government as a whole, only to the eight ministries which do accrual accounting and are audited by audit firms.

** The audit of the financial statements of government is not subcontracted to third parties, but the audit of external entities owned by public governments done by private sector auditors is estimated by about 40%, and the audit of grants to private companies is near 100%.

Conclusion

Except for the Slovak Republic, the responsibility for the audit of the financial statements of the national government remains in the hands of the respective supreme audit institution. In about 50 per cent of the countries who responded certain audit work is performed by private sector auditors or other specialists not found in the supreme audit institution, but in general the proportion of subcontracted audit work is small.

3.3. Educational Background

3.3.1. Background

Given that the responsibility for the audit of the financial statements of the national government remains with the respective supreme audit institution, the aim is to find out more about the educational background of the supreme audit institution staff and whether this has changed as a result of governments introducing accrual accounting. The results from Israel and the Slovak Republic have not been included in this section, as the audits are performed by private sector firms.

According to Article 3 of the European Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006, the statutory audit of annual accounts and consolidated accounts of statutory enterprises shall be carried out only by statutory auditors or audit firms which are approved by the EU Member State. A person may be approved to carry out such a statutory audit only after having attained university entrance or equivalent level, then completed a course of theoretical instructions, undergone a practical training of at minimum three years and passed an examination of professional competence at university final or an equivalent examination level. The expression “professional accountancy qualification” was used in the questionnaire for a qualification in accordance with the above mentioned directive or a comparable qualification. If the examinee fulfils the qualification, he or she gets a statutory title like the Chartered Certified Accountant of the British ACCA, the “Experts

Comptables" in France or the "Wirtschaftsprüfer" in Germany. In general, the use of this title by a person who is not certified is prohibited.

3.3.2. Education

With this background, 8 of 13 supreme audit institutions employ staff which have a professional accountancy qualification. Denmark is included in the 8, but they do not currently employ staff with a professional accountancy qualification but they will do so from 2012.

Table 3 shows the educational background of the staff at the supreme audit institution who perform the audit of the financial statements.

Table 3: Educational background of supreme audit institution staff

	Professional accountancy qualification	Lawyer	Degree in public management/ administrative science	Degree in finance and/or economics
Denmark	✓	✓	✓	✓
Finland	-	-	✓	✓
France	✓	✓	✓	✓
Italy	-	✓	-	-
Latvia	-	✓	✓	✓
Malta	✓	-	✓	-
Netherlands	✓	✓	✓	✓
Portugal	✓	✓	✓	✓
Romania	-	-	-	✓
Spain	-	-	-	✓
Sweden	✓	-	-	-
Switzerland	✓	✓	✓	✓
United Kingdom	✓	-	✓	✓
	8	**7**	**9**	**10**

In answering the questionnaire, countries were allowed to select more than one option, as for example a person who first studies finance or economics may later become a professional qualified accountant. A positive response for the professional accountancy qualification does not mean necessarily that such a qualification is required for the job by the supreme audit institution, but that staff with such a qualification are employed on the audits. The next table shows whether there are requirements in the educational background.

In Spain the employees of the supreme audit institution are civil servants with appropriate background. Senior staff usually have a qualification in finance or economics.

In Italy the passing of a competitive state exam is required to be appointed as a judge in the supreme audit institution (Corte dei Conti). The competitive state exam for becoming a magistrate of the supreme audit institution is open, over and above the aforementioned lawyers with at least 5 years of enrolment, to: ordinary magistrates who qualified as court magistrates; public prosecutors with a second-tier wage; military magistrates and administrative magistrates; governmental employees and employees of the two branches of Parliament and of the General Secretariat of the Presidency of the Republic listed in Art. 1, para. 2, of Legislative Decree No. 165 of 30 March 2001, provided they graduated in law in a university course of at least four years and have been holding – for no less than five years overall - an executive post or a non-executive post for which a university degree is required.

Some of the respondents point out that the qualification depends on the function of the staff. An accountancy qualification is not always necessary for certain functions of the supreme audit institutions (for example value for money or performance audit in the UK). One respondent pointed out that their scope of recruitment is very broad and one of the objectives is to mix diverse professional experiences. In UK, all financial auditors in the supreme audit institution are required to be qualified accountants other than those on training contracts. Besides the mentioned educational background, the supreme audit institution employs other experts, for example IT-specialists (chartered EDP auditor), evaluators, chartered internal auditors, construction auditors, chartered operational auditor, or other government auditors.

Further, the respondents were asked if the employees of the audit institutions have to pass an exam (like the CPA-Exam) or any other test to prove their knowledge of accrual accounting and auditing. In connection with this question, they were also asked if this requirement was newly introduced as a consequence of the transition to accrual based accounting.

Table 4 summaries the responses of the two questions:

	Supreme audit institution employs professional qualified accountants	Requirement for an exam or test		If yes, introduced due to the introduction of accrual accounting
		No	**Yes**	
Denmark	✓	✓		
Finland		✓		
France	✓	✓		
Italy			✓	No
Latvia		✓		
Malta	✓		✓	No
Netherlands	✓		✓	No
Portugal	✓	✓		
Romania		✓		
Spain			✓	No
Sweden	✓		✓	No
Switzerland	✓	✓		
United Kingdom	✓		✓	No
	8	**7**	**6**	

4 of the 7 countries which responded that there was no specific test associated with accrual accounting do employ professional qualified accountants at the supreme audit institution (Denmark from 2012, France, Portugal and Switzerland). It may be in this case that the question was not interpreted in the same way across the countries who responded.

In one case it is not clear whether the exam or test is comparable with an accountancy qualification in terms of the EU directive on statutory audits of annual accounts and consolidated accounts of enterprises: In Malta all officers superior to a certain grade in the Financial and Compliance Audit Section are to be in possession of a degree in Accounting. Officers in other grades are at least to have attained an Advanced Level Standard in Accounting. The requirements were introduced to enhance the Office's professional approach to audit work.

In two other cases the exams are not comparable with an accountancy qualification. In Spain, the knowledge of accrual accounting and auditing is tested in a new exam to become an internal or external control civil servant. In Italy the passing of a competitive state exam is required to be appointed as a judge in the supreme audit institution (Corte dei Conti).

None of the countries which have a requirement to attain qualifications in accounting and auditing had introduced this specifically as a consequence of the transition to accrual based accounting in their countries.

3.3.3. Training in accrual accounting

The respondents were asked how the audit staff were trained in the new accounting concepts and the associated new issues for the audit. Most of the 15 countries responded that they provided specific training for the audit staff in connection with the introduction of accrual accounting, with the main focus of the introduced training being on the accounting principles. France, Latvia and the Netherlands note that the training provided in their countries also included audit issues. In Latvia new audit standards based on International Auditing Standards (ISA) of IFAC were introduced at the same time as the accrual accounting standards. The Latvian response emphasised that the two projects were initiated detached from each other. Nevertheless, training was provided through twinning projects.

In Denmark the agency for governmental management (part of the ministry of finance) prepared comprehensive thematic guidelines based on knowledge and practical experience, and good practice examples. These were generated following a number of "true scale" pilot projects in the early stages of reform implementation. Along with the launching of guidelines the agency carried out a targeted number of courses and training courses. Because private consultancy companies also offer various professional training courses to relevant public sector staff, the agency has taken up a project to establish a proper platform for external consultancy and education/training.

Malta, Sweden and the UK remarked in the questionnaire that, due to the educational background (qualified accountants), staff were well aware of the accounting and auditing issues which relate to accrual accounting. Therefore no fundamental training as a result of the introduction of accrual accounting was necessary, although regular training in connection with the continuing professional development of staff continued as before.

Conclusion

8 of 15 supreme audit institutions employ or will employ staff with a professional accountancy qualification to perform the financial audit. Only in 3 cases is there an explicit requirement for such a qualification (Netherlands, Sweden or the UK). In a further 2 cases, the financial audit is performed by private audit firms (Israel and Slovak Republic), leaving 5 countries (Finland, Italy, Latvia, Romania,

Spain) where no professional qualified accountants are involved in the audit of the financial statements of the national government. Leaving aside the professional accountancy qualification, the majority of supreme audit institutions employ staff with a degree in finance and/or economics.

As none of the respondent answered that they introduced new professional examination requirements as a result of the transition from cash to accrual accounting, it appears that the supreme audit institutions were or are well prepared for the change from cash to accrual accounting in the public sector.

3.4. Applied Standards on Auditing

To ensure a consistency of approach and quality, auditing standards are in place to govern the performance of a financial audit. Commonly applied standards are International Standards on Auditing (ISA) which are professional standards for the performance of financial audit of historical financial information. These standards are issued by the International Federation of Accountants (IFAC). IFAC is the global organization for the accountancy profession. It works with its 157 members and associates in 123 countries and jurisdictions, representing more than 2.5 million accountants employed in public practice, industry and commerce, government, and academia. IFAC, through its independent standard-setting boards, establishes international standards on ethics, auditing and assurance, education, and public sector accounting.

Within each jurisdiction, regulations may govern the issue of auditing standards. The ISA only apply directly if the respective jurisdiction has endorsed the ISA as its auditing standards for the public sector. Some countries do not apply the ISA directly; however the national auditing standards are based on the ISA. Sometimes the national auditing standards include additional national requirements. The ISA based auditing standards are common for the financial audit of enterprises. Nevertheless the ISA include references to the public sector perspective. The aim of this section of the study is to find out whether the ISA are also applied for the financial audit in the public sector, especially for governments.

The International Organization of Supreme Audit Institutions (INTOSAI) also sets auditing standards. INTOSAI operates as an umbrella organisation for the external government audit community, it provides an institutionalised framework for supreme audit institutions to promote development and transfer of knowledge, improve government auditing worldwide and enhance professional capacities, standing and influence. INTOSAI is an autonomous, independent and non-political organisation. It is a non-governmental organisation with special consultative status in the Economic and Social Council (ECOSOC) of the United Nations. INTOSAI has 188 Full Members and 2 Associated Members.

The transition from cash to accrual accounting affects the scope and nature of the financial audit. The questionnaire sought information on what auditing standards were followed in the respondent countries and whether new requirements were introduced as a result of the move to accrual accounting.

All 15 countries who responded have auditing standards for the audit of the national government. 7 of these were explicit in stating that new auditing standards, or revisions to existing auditing standards, were not required as a result of the transition to accruals.

The Maltese response notes that the question is not applicable because accrual accounting has not been officially introduced for the federal government. For the audit the cash based financial report is relevant. In this connection, the Maltese supreme audit institution follows the INTOSAI International Standards of Supreme Audit Institutions (ISSAIs).

For the government wide accounting system in the Netherlands the question does not apply either because only parts of national government uses accrual accounting. Nevertheless, the introduction of the accrual accounting for executive parts of the government has had some effect on the auditing standards and therefore several parts of the government-wide audit guidelines had to be supplemented.

Latvia and Slovak Republic implemented auditing standards based on the ISA at the same time when accrual accounting was introduced, however the two projects were initiated separately from each other.

In 12 of 15 countries, the standards are based on ISA or the ISA are applied directly. Latvia, Portugal, Romania, and Switzerland responded that their respective auditing standards are based on ISA as well as on the standards of INTOSAI. In Denmark and Finland, the auditing standards are called “Good Public Audit Practice” and are based on the standards of INTOSAI. However, it was not explicitly asked whether the auditing standards are based on the INTOSAI standards. Therefore, it cannot be excluded that the auditing standards of other countries are in alignment with the INTOSAI standards.

Table 5 gives an overview of the responses to the questions who sets the standard and on which standards the applied auditing standards in the public sector are based.

Table 5: Applied auditing standards in countries who responded

		Auditing standards		
	Standard Setter	**Direct application of ISA**	**ISA based auditing standards**	**Other Basis**
Denmark	Supreme audit institution (“Rigsrevisionen”)*			Good Public Audit Practice based on INTOSAI
Finland	Board of Chartered Public Finance Auditing which operates under the auspices of the Ministry of Finance			Good Public Audit Practice based on INTOSAI
France	N/A, because direct application of ISA	✓		
Israel	Israel CPA Standard Board		✓	
Italy	Ragioneiria generale dello stato/Observatory for auditing and finance of local entities		✓	
Latvia	N/a, because direct application of ISA	✓		INTOSAI
Malta	INTOSAI			INTOSAI
Netherlands	Ministry of Finance for specific federal government aspects (e.g. legality auditing standards and materiality). In general the audit standards of the Royal NIVRA (Netherlands institute of		✓	

	Standard Setter	Auditing standards		
		Direct application of ISA	**ISA based auditing standards**	**Other Basis**
	auditors) are effective.			
Portugal	Supreme audit institution		✓	INTOSAI
Romania	Supreme audit institution*		✓	INTOSAI
Slovak Republic	N/a, because direct application of ISA	✓		
Spain	"Intervención General de la Administración des Estado" (General Inspection Office)		✓	
Sweden	Supreme audit institution ("Riksrevisionen")		✓	
Switzerland	INTOSAI		✓	
	Swiss Institute of Certified Accountants and Tax Consultants ("Schweizer Treuhand-kammer")		✓	Swiss Audit Manual, release 1998, part 9.4 "Audit in public administration"
				The Institute of Internal Auditors "Basics of Internal Auditing" - Code of Ethics - IIA Standards - Practice Advisories
United Kingdom	UK Auditing Practice Board (APB) of the Financial Reporting Council		✓	
		3	10	

* Within the legal framework (e.g. Constitution, Auditor General's Act)

Conclusion

In all the countries that responded, the audit of the accrual based financial statements of national government is conducted on the basis of auditing standards. In 12 of 15 countries, the auditing standards are based on the ISA or the ISA are applied directly. Besides the ISA based standards 4 countries apply additionally standards of INTOSAI for the audit of the financial statements. 3 countries (Denmark, Finland and Malta) conduct the audit of the financial statements in accordance with INTOSAI based standards.

In about half of the countries, the transition to accrual accounting required some revisions to the auditing standards that were followed. Some countries adopted ISA for the first time, others needed to add to existing guidance in order to address the audit issues arising from the preparation of accruals-based accounts.

3.5. *Quality Control System*

Quality assurance generally has two aspects:

- The implementation of an internal quality control system within the audit body or institution; and

- External quality assurance, often by peer review or an oversight board.

For the arrangements of an internal quality control system the IFAC International Standard on Quality Control 1 (ISQC1) "Quality control for firms that perform audits and reviews of historical financial information, and other assurance and related services engagements" is an important standard. It requires audit firms to establish a system of quality control designed to provide it with reasonable assurance that the audit firm and its personnel comply with professional standards and regulatory and legal requirements, and that the auditors' reports issued are appropriate in the circumstances.

The requirement to be subject to an external quality assurance system was introduced by the Directive of the European Parliament and of the Council of 17 May 2006 on "Statutory Audit of Annual Accounts and Consolidated Accounts" for all statutory auditors and audit firms of enterprises. The quality assurance system shall be organised in a manner that remains independent of the reviewed statutory auditors and audit firms and subject to public oversight[4].

The questionnaire asked what other changes with regard to the audit of the financial statements of government were required due to the introduction of accrual accounting, in particular asking whether changes to the quality control system were required. The questionnaire did not explicitly ask whether the country has internal quality control systems in place or not. Therefore, the analysis of the answers may be incomplete.

The comparability of the responses is limited, because the responses are very specific. 7 countries said that they do have quality control systems within the audit institution, but this does not infer that the other 8 countries do not. In Finland in 2005 an external quality assurance system organised by the Board of Chartered Public Finance Auditing was introduced.

According to the French response, a quality control system was implemented.

A quality management system is being implemented at the Latvian supreme audit institution; it is already implemented regarding audits. More attention is being paid to cooperation with audited entities. The supreme audit institution has started to rely on work done by qualified auditors and this has become possible due to the fact that the supreme audit institution works in accordance with IFAC standards.

Portugal is also implementing a quality control system, but not as a direct effect of accrual basis of accounting.

The auditing standards of the Romanian Court of Accounts stipulate the achievement of the audit quality analysis. This standard is currently under implementation.

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4 For more information on Quality Assurance Arrangements Across Europe see identical titled FEE Report of December 2006 which is available at http://www.fee.be/fileupload/upload/Quality%20Assurance%20Arrangements%20Across%20Europe%200612181200761426.pdf

In Spain there was no significant amount of audit performed before the introduction of the accrual accounting in governments. There is now a quality control system in place.

In Switzerland a quality control system was also implemented, but its requirements are independent from the introduction of the IPSAS based accounting standards. The Swiss quality control system is based on the Standard of the Institute of Internal Auditors "Basics of Internal Auditing"[5].

The National Audit Office of the UK also has quality control arrangements, but those which did not change due to the introduction of accrual accounting.

Conclusion

7 of 15 countries pointed out that they have some kind of quality control system within the audit institution. In Finland in 2005 an external quality assurance system organised by the Board of Chartered Public Finance Auditing was introduced. As it was not explicitly asked whether the country have internal quality control systems in place or not, it can not be inferred that the other 8 countries do not have a quality control system. In general, the answers received show that the implementation of accrual accounting has strengthened the quality control procedures in place over the audit process.

5 1300: Quality Assurance and Improvement Program, 1310: Quality Program Assessments, 1311: Internal Assessments, 1312: External Assessments, 1320: Reporting on the Quality Program, 1330: Use of "Conducted in Accordance with the Standards", 1340: Disclosure of Non-compliance

4. RESULTS ON THE LOCAL LEVEL OF GOVERNMENT

4.1. Introduction of Accrual Accounting by the Analysed Respondents

20 of the 26 countries that responded have introduced some form of accrual accounting at the local level of government. Table 6 gives an overview when accrual accounting was introduced in the different countries.

Table 6: Introduction of accrual accounting at the local level

Country	**introduced**	**Comments**
Norway	Starting 1924	In Norwegian municipalities the development of what is still a modified accrual accounting system, has taken place over a long period of time. By a regulation in 1924, the cash accounting system (simple cameral accounting) was changed to the first modified version of accrual accounting.
United Kingdom	ca. 1950´s	
Switzerland	1975 till 2000	The way in which local governments in Switzerland have to account depends on the legislation of each canton. Depending on the canton accrual accounting was introduced for the local governments between 1975 and 2000.
Netherlands	1982	In the Netherlands accrual accounting for the local governments was introduced in 1982 by Royal Decree Municipal Accounting Regulations (Besluit gemeentelijke comptabiliteitsvoorschriften). In 1995 the accounting standards were updated based on accounting principles for private companies. In 2004 the accounting standards are changed and based on accounting principles which are based on the principle of individuality of provincial and local government and their specific characteristics.
Cyprus	1985	In Cyprus accrual accounting has not yet been introduced for the 356 community boards (covering the population living in villages in rural areas). However, most of the 24 municipalities have applied accrual accounting (IFRSs) since 1985.
Sweden	1986	
Portugal	in the early 1990´s	
Poland	in the early 1990’s	In Poland the local governments use mixed systems (cash and accrual accounting). Depending on the entity / business unit the reporting system may be based on pure cash, mixed cash / accrual and pure accrual accounting. The system was introduced in the early 1990’s with numerous subsequent modifications.
Spain	1992	Accrual based accounting was implemented by the local governments of Spain in 1992. In 2006 a General Accounting Plan came into force.
Italy	1995	In Italy accrual accounting was introduced in 1995 for the local governments. The accrual accounting is optional and may be adopted in addition to the cash accounting; it is used to draw a

		propitiation plan to highlight the accrual part of the balance sheet. Government bodies can also choose to introduce permanently the accrual system jointly with the financial system.
Malta	1995	
Belgium	1995*	Since 1995 the municipalities account on the accrual basis and public social entities since 2002.
France	in the late 1990´s	
Finland	1997	
Greece	1999	In Greece the municipalities introduced accrual accounting in 1999. In 2003 the public hospitals followed.
Latvia	2003	Latvia introduced accrual accounting for the local governments in order to comply with the International Financial Reporting Standards (IFRS/IAS) and the International Public Sector Accounting Standards (IPSAS) in 2003.
Denmark	2004	In Denmark, from 2004 government and political representatives for regional authorities and municipal authorities respectively agreed that accrual accounting (cost based accounting) should be introduced supplementary to the ordinary cash based accounts. Budgeting has so far not been converted to the cost basis.
Germany	2004 till ca. 2016	The way in which local governments in Germany have to account depends on the legislation of the 16 states. Most of the states decided to introduce accrual accounting for the local level and have already ratified the respective legislation. In some states the local governments have a choice to retain cash accounting or to introduce modified cash or accrual accounting. The transition periods depend on the respective state legislation. Most of the local governments will implement accrual accounting between 2004 and about 2016. Therefore only a minority of local governments have completed the conversion from cash to accrual accounting.
Romania	2006	In Romania accrual accounting was introduced in 2005 as an experiment. In 2006 it was introduced officially.
Slovak Republic	2008	In the Slovak Republic, the new accounting standards on the accrual basis became effective on January 1st, 2008. However, before that date the accounting standards were closer to accrual accounting than to cash accounting.

As well as these countries, Lithuania (2009) and Czech Republic (2010) plan to introduce accrual accounting at the local government level in the future. As they do not currently follow accrual accounting they are not included in the following analysis. For the local level of government in the following report, only the 20 countries in the table are analysed.

4.2. Contracting of Third Parties

4.2.1. Responsibility for the audit

The overall responsibility for the audit, supervision or control of the local governments is not always with the same institution which actually performs the financial audit. For example, in some countries the audit is performed by a private sector auditor, but the responsibility for the appointment of the private sector auditor, the reception of the auditors' report and the drawing of the conclusion is with an institution of the public sector (e.g. audit institution or audit committee of the local council).

The table 7 shows the 6 countries (of the 20 surveyed) where the responsibility for and the performance of the audit of the local government is assigned to the same institution.

Table 7: Countries where the responsibility for and the performance of the audit is assigned to the same institution

	Responsibility for the financial audit
Belgium	Supreme Audit Institution for the provinces / Provincial governments for the municipalities
Cyprus	Audit Office of the Republic of Cyprus
France	Chambres régionales des comptes
Portugal	Supreme Audit Institution which audits the work of the internal audit bodies
Romania	Supreme Audit Institution respectively county chambers
Spain	Regional audit institution and local level internal control

In France the Chambres régionales des comptes do not formally certify the financial statements of local governments even if the accounts are audited.

In Belgium the Court of Audit exerts external control on the budgetary, accounting and financial operations of the provinces but not of the municipalities which are controlled by the Provincial governments.

The table 8 shows the 7 countries in which the financial audit, and sometimes the performance of other audit issues, is contracted out, i.e. performed by private sector auditors or, in the case of Finland, by public finance auditors.

Table 8: Countries where all financial audits are performed by private sector auditors/public finance auditors

	Audit performed by	**The auditor is appointed by**
Denmark	Private sector auditor, especially "Kommunernes Revision", which is an audit firm	Local council
Finland	Chartered Public Finance Auditor	Local council
Greece	Qualified auditor*	Local government
Italy	Auditing body of 1 or 3 qualified auditors enrolled with the roll of Dottori Commercialisti and Esperti Contabili	Local council
Latvia	Qualified auditors	Local government

Malta	Private sector auditor	Supreme Audit Institution
Slovak Republic	Qualified auditors (only members of Slovak Chamber of Auditors)	Local government

* The accrual based financial statements that are published are audited by a private sector auditor. The cash based statements that are reported to the central government are audited by the Greek Court of Auditors.

Before 1992, the public sector in Finland lacked any examination for approving public finance auditors. Therefore a new examination for Chartered Public Finance Auditors (CPFA) was introduced in order to meet the increased focus on auditing, and to meet the growing need for skilled public finance auditors. The requirements for the Chartered Public Finance Auditors have been developed to meet the requirements of the EU´s Eight Council Directive on company law[6]. The Chartered Public Finance Auditors can work on an individual basis, in a CPFA corporation or can be employed, for example by the internal audit divisions of large towns or by joint municipal boards.

In the Slovak Republic, only members of the Slovak Chamber of Auditors ("Slovenská komora audítorov" (SKAu)) perform the audit of the financial statements in the public sector. The members of the Slovak Chamber of Auditors are appointed by the local government.

In a third group of 7 countries the respective legislation permits a degree of choice with respect to the person or institution that performs the financial audit (Germany, Netherlands, Norway, Poland, Sweden, Switzerland and the UK).

For example, in Germany depending on the state legislation the local council itself or an audit committee (Rechnungspruefungsausschuss) is responsible for the audit. Municipalities with more than 20,000 inhabitants have to establish an audit office within the municipality (in general called "Rechnungspruefungsamt"). In municipalities without such an audit office the financial audit can in theory be performed by the audit committee of the local council. In practice the audit committee will use the audit body of a larger neighbouring municipality or a private sector auditor. In municipalities large enough to have an audit office, the financial audit of the cash based statements was performed by that audit office. Since the transition to accrual accounting the audit office has the choice to perform the financial audit itself or to appoint someone else (for example a private sector auditor) with the agreement of the local council's audit committee. Due to the fact that Germany is a federation there are differences in detail between the legislation of the different states.

In the Netherlands the local council is responsible for the audit and appoints an audit firm to carry out the audit of the financial statements. Four big cities have an internal audit department. Three of those carry out the audit themselves. In one of the cities the audit is carried out by an audit firm based upon the pre-work of the internal audit department.

Also in Norway the council of the municipality or county has the option to either to employ an auditor internally within the municipality, to engage a firm of cooperating municipal auditors, or to appoint a private sector auditor to perform the financial audit.

In Poland, separate audit bodies in the structure of the local administration are responsible for the audit of the financial statements (cash and mixed system). The accrual based financials statements are audited by independent auditors.

6 See section 3.3.1. of this report.

In Sweden the members of the local council are responsible for the audit but make use of professional auditors (especially when it comes to the financial audit). Larger cities have their own audit office, thus performing a larger portion of the audit themselves.

In Switzerland the responsibility for the audit depends on the local organisation and legislation. Big cities have their own audit offices, smaller communities often subcontract to a third party. Others may be audited by members of the local council.

In the United Kingdom the responsibility for the audit depends on the state legislation. In Scotland the Accounts Commission is responsible for the audit; in Northern Ireland the Department of the Environment designates certain staff members of the Northern Ireland Audit Office to local government auditors which report the results of their work to the Department of the Environment. In England and Wales the Audit Commission and Wales Audit Office respectively are responsible. They can either perform the audit themselves or appoint a private sector auditor.

4.2.2. Contracting of third parties

The respondents were asked whether the responsible body has the opportunity to subcontract someone else (e.g. audit office of the neighbouring municipality, private audit firm) to carry out the financial audit. The table 9 shows the results. If it is possible to subcontract someone else the table shows to whom and what proportion of the financial audit is subcontracted.

Table 9: Subcontracting of audit work and the amounts subcontracted

	Possibility to subcontract to a third party	**Who is the third party?**	**Percentages of subcontracted audit work Approx.**
Belgium	No		
Cyprus	Yes		Not practised
Denmark	Yes	Independent audit companies	100%
Finland	Yes	Chartered Public Finance Auditor	100%
France	No		
Germany	Yes	Not restricted to certain persons or institutions	not available
Greece	Yes	Qualified auditors	not specified
Italy	Yes	Auditing body of 1 or 3 qualified auditors enrolled with the roll of Dottori Commercialisti and Esperti Contabili	100%
Latvia	Yes	Qualified auditor	not specified
Malta	Yes	Private sector auditors, also known as local government auditors	100%
Netherlands	Yes	Audit firm	up to 100%

	Possibility to subcontract to a third party	**Who is the third party?**	**Percentages of subcontracted audit work Approx.**
Norway	Yes	Private audit firm: or a firm of cooperating municipal auditors:	5% 80%
Poland	Yes	private sector auditor	No exact figures available, but rather very small percentage
Portugal	Yes	Private sector auditor	Not available
Romania	No		
Slovak Republic	Yes	Auditors or Audit firms which are members of the Slovak chamber of Auditors	100%
Spain	Yes	Private audit firms	almost 0%
Sweden	Yes	Qualified auditors	25 to 100%
Switzerland	depends on the local organisation/ legislation	Audit firms	exact figures are not available
United Kingdom	Yes	Private audit firms	25 to 35%

17 of the 20 countries have the possibility to subcontract the audit to a third party. In just 3 of the countries who responded is subcontracting not permitted.

In France, the audit institution would not contract out the audit of the financial statements, but the audit institution engages external specialists or private audit firms for specific tasks such as IT audits or actuarial calculations of pension schemes. However, the conclusions of reports issued by these auditors or specialists must be endorsed by the audit institution and the accountability for the quality of investigations remains solely with the audit institution.

For Germany there are no figures available yet. Due to a long transitional period only a smaller portion of local governments have set up their opening balance sheet on the accrual basis of accounting which is subject to an audit.

Conclusion
In 30 per cent of the responding countries the responsibility and the performance of the audit of the accrual based financial statements is assigned to an audit office outside the local government.

In 35 per cent of the countries the audit of the accrual based financial statements is performed by private sector auditors or in the case of Finland by a special accountancy profession for the public sector. In general, the private sector auditor or the Finnish chartered public finance auditor is appointed by the local council.

In the third group of countries (35%) the person or institutions that perform the financial audit depends on the different legislative requirements which in most cases relate to the size of the municipality. The tendency is that bigger municipalities have their own audit office and that the smaller municipalities appoint a private sector auditor or firm of cooperating municipal auditors. In this group, between 25 and 100 per cent of the financial audit work is subcontracted to third parties, usually to private sector auditors.

4.3. Educational Background

4.3.1. Education

In more than 50 per cent of countries who responded, the audit of the financial statements of the local governments is performed by a centralised or local audit institution/office. The questionnaire aimed to find out more about the educational background of the staff of the audit offices.

The 7 countries in which the audit is performed by a person outside the audit office and has passed a professional accountancy qualification[7] or a respective audit firm is not considered in the following analysis. These countries are Denmark, Finland, Greece, Italy, Latvia, Malta and Slovak Republic (see also section 4.2.1.).

The table 10 summarises the educational background of the audit staff of the remaining 13 (of 20) countries.

Table 10: Educational background of audit institution/office staff

	Professional accountancy qualification	Lawyer	Degree in public management/ administrative science	Degree in finance and/or economics
Belgium				
Cyprus	✓	✓	✓	✓
France	✓	✓	✓	✓
Germany			✓	
Netherlands	✓	✓	✓	✓
Norway	✓			
Poland	✓			✓
Portugal	✓	✓	✓	✓
Romania				✓
Spain				✓
Sweden	✓			✓
Switzerland	✓	✓	✓	✓
United Kingdom	✓			
	9	**5**	**6**	**9**

7 For a description of the term “professional accountancy qualification” see section 3.3.1. of this report.

9 of 13 audit offices (about 70%) employ staff with professional accountancy qualifications. Some of the respondents point out that the qualification depends on the function of the staff. For some functions an accountancy qualification is not necessary (for example value for money or performance audit). In the UK, all financial auditors in the audit office need to be qualified accountants other than those on training contracts.

In Belgium, Germany, Romania and Spain the audit offices of the local governments do not employ staff with a professional accountancy qualification. Spain points out that the civil servants of the audit offices have an appropriate background to perform the audit.

Besides the mentioned educational background, the supreme audit institution employs other experts, e.g. IT-specialists (chartered EDP auditor), evaluators, or construction auditors. One respondent pointed out that their scope of recruitment is very broad and one of the objectives is to mix diverse professional experiences.

Furthermore, the respondents were asked if the employees of the audit offices have to pass an exam (like a CPA-Exam) or other test to prove their knowledge of accrual accounting and auditing. In connection with this question, they were also asked if this requirement was newly introduced as a consequence of the transition to accrual accounting.

Table 11 summarises the responses:

	Audit body employs professional qualified accountants	Requirement for an exam or test		If yes, introduced due to the introduction of accrual accounting
		No	**Yes**	
Belgium		✓		
Cyprus	✓		✓	No
France	✓	✓		
Germany		✓		
Netherlands	✓	✓		
Norway	✓		✓	No
Poland	✓		✓	No
Portugal	✓	✓		
Romania		✓		
Spain			✓	No
Sweden	✓		✓	No
Switzerland	Depends	✓		
United Kingdom	✓		✓	No
	9	**7**	**6**	

Four of the seven countries which responded that there was no specific test associated with accrual accounting do employ professional qualified accountants at the supreme audit institution. It may be in this case that the question was not interpreted in the same way across the countries who responded.

In Norway the auditors in charge of the audit must have passed the same exams as are required to become a qualified auditor (a bachelor's or a master's degree), however without the same required marks as to be authorised as a public accountant. In addition, the person must have at least three years of practical experience with audits of financial accounts, i.e. the same practical experience which is required to be a qualified public accountant. But it is not required that the responsible auditor is a qualified auditor.

In Spain staff members have to pass competitive examinations to become an internal or external control civil servant. This exam is not comparable with an accountancy qualification in terms of the EU directive on statutory audits of annual accounts and consolidated accounts of enterprises. The contents of the examination is much more influenced by public accounting rules and legislation, and less for pure audit issues.

In Romania, new employees are expected to be familiar with the Organization and Functioning Regulation of the Court of Accounts, the Control Provisions, and the Audit Handbooks together with the Auditing Standards of the Court.

None of the respondent answered that they introduced new professional examination requirements as a result of the transition from cash to accrual accounting.

4.3.2. Training

The respondents were asked how the audit staff were trained in the new accounting and auditing issues arising from the introduction of accrual accounting. 5 of 13 countries responded that they provided training for the audit staff in connection with the introduction of accrual accounting (Cyprus, Germany, Portugal, Romania, Spain). From the answers it is not clear whether the training focus only on accounting or also on auditing issues. In Germany public sector training centres offer training, but there is no general training concept. Each municipal audit committee or municipal audit office has to decide how to learn the new accounting and auditing subject. In some German states networks with web forums were set up. In general these networks are operated by the ministries of interior and by the accounting staff of those local governments that are frontrunners in the transition from cash to accrual accounting.

The Netherlands, Switzerland and the UK point out that the introduction of accrual based accounting is too long ago and that they therefore have no information available anymore. But in general, new and changing accounting and auditing requirements are covered in written briefings for auditors and through regular training events.

Poland and Sweden remarked in the questionnaire that, due to the educational background (qualified accountants or degrees in finance/economics), staff were well aware of the accounting and auditing issues which related to the introduction of accrual accounting.

Conclusion

In 13 of 20 countries the financial audit is performed solely or partially by an audit institution/office. 9 of these 13 audit institutions/offices employ staff with a professional accountancy qualification. In 5 cases, there is an explicit requirement for such a qualification. This leaves 4 of 13 countries (Belgium, Germany, Romania, Spain) where no professional qualified accountants are involved in the audit of the financial statements of local governments. However, in Spain staff members have to pass exams, but these exams are not comparable with an accountancy qualification. Besides the professional accountancy qualification, the majority of audit institution/office staff have a degree in finance and/or economics. None of the 13 respondents answered that the requirement to prove the knowledge in accounting and auditing was introduced because of the implementation of accrual accounting. Interestingly, in Finland a new professional accountancy qualification in the public sector was introduced about 5 years before the transition to accrual based accounting (so called chartered public finance auditors).

4.4. Applied Standards on Auditing

Not all of the 20 analysed countries have generally accepted auditing standards for the audit of the local government.

This is the case in Germany. Certain German institutions issue audit guidelines/handbooks which contain checklists and work programs (e.g. VERPA, GPA NRW). The application of these publications is not compulsory. Private sector auditors that are engaged for the audit of the financial statements of a local government are required to follow the auditing standards which are issued by the Institute of German Auditors (IDW) and are based on the ISA[8].

In France the Chambres régionales des comptes do not formally certify the financial statements of local governments even if the accounts are audited. Since there is no certification the ISA are not applied for the audit, but the auditors of the Chambres régionales des comptes use INTOSAI standards for their activity.

In Sweden no explicit auditing standards existed before the introduction of accrual accounting. There is a current debate taking place as to what extent ISA should be used in the public sector and what changes are needed to address the public sector specific issues.

In the questionnaire it was asked whether it was necessary to introduce auditing standards or to revise the existing auditing standards in connection with the introduction of accrual accounting. 5 answers of 20 respondents are not clear. Nevertheless these countries have auditing standards in order to conduct the audit of the financial statements of local government accordingly.

8 of 20 respondents explicitly responded negatively to the question whether new auditing standards were introduced or existing standards revised. Latvia and Slovak Republic implemented auditing standards based on the ISA at the same time when accrual accounting was introduced, however they point out that the introduction of ISA based auditing standards was not linked to the implementation of accrual accounting.

4 of 20 respondents emphasised that in their country the auditing standards were either revised or new standards were introduced due to the introduction of accrual accounting (Italy, Netherlands, Portugal, Spain). For example, in the Netherlands some new standards specific for the government auditing had to be introduced, because the private sector auditing standards did not cover some of the public sector specific issues (e.g. taxes transfers). The Norwegian response notes a similar aspect.

Table 12 gives an overview of the responses to the questions who is in charge of standard-setting and on which framework the applied auditing standards for the audit of the local governments are based.

[8] International Standards on Auditing of IFAC, see section 3.4. of this paper.

Table 12: Applied auditing standards in countries who responded

	Standard Setter	Auditing standards		
		Direct application of ISA	**ISA based auditing standards**	**Other Basis**
Belgium	Parliament			
Cyprus	N/A, because direct application of ISA	✓		
Denmark	N/A, because direct application of ISA	✓		
Finland	Board of Chartered Public Finance Auditing which operates under the auspices of the Ministry of Finance			Good Public Audit Practice based on INTOSAI
France	N/A, because no formal certification of the financial statements			INTOSAI
Germany	Depends on who performs the audit		Depends on who performs the audit	
Greece	Ministry of Finance and Economy		✓	
Italy	Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili (CNDCEC)		✓	
Latvia	N/a, because direct application of ISA	✓		
Malta	N/a, because direct application of ISA	✓		
Netherlands	Ministry of Interior and Kingdom Relations for specific municipal and provincial government aspects (e.g. legality auditing standards and materiality). In general the audit standards of the Royal NIVRA (Netherlands institute of auditors) are effective.		✓	
Norway	The Norwegian Institute of Public Accountants (“Den norske Revisorforening”)		✓	
Poland	Ministry of Finance		✓	
Portugal	Supreme audit institution		✓	INTOSAI
Romania	Supreme audit institution within the legal framework (e.g. Constitution, Auditor General’s Act)			INTOSAI
Slovak Republic	N/a, because direct application of ISA	✓		
Spain	“Intervención General de la Administración des Estado” (General Inspection Office)		✓	National auditing standards for the private sector
Sweden	Under construction		to some extent	

<table>
<tr><th rowspan="2"></th><th rowspan="2">Standard Setter</th><th colspan="3">Auditing standards</th></tr>
<tr><th>Direct application of ISA</th><th>ISA based auditing standards</th><th>Other Basis</th></tr>
<tr><td rowspan="2">Switzerland</td><td>Swiss Institute of Certified Accountants and Tax Consultants (“Schweizer Treuhandkammer”)</td><td></td><td>✓</td><td>Swiss Audit Manual, release 1998, part 9.4 “Audit in public administration”</td></tr>
<tr><td></td><td></td><td></td><td>The Institute of Internal Auditors “Basics of Internal Auditing”
- Code of Ethics
- IIA Standards
- Practice Advisories</td></tr>
<tr><td>United Kingdom</td><td>UK Auditing Practice Board (APB) of the Financial Reporting Council</td><td></td><td>✓</td><td></td></tr>
<tr><td></td><td></td><td>5</td><td>ca. 10</td><td></td></tr>
</table>

In about 15 of 20 countries, the standards are based on ISA or the ISA are applied directly. Portugal responded that their respective auditing standards are based on ISA as well as on the standards of INTOSAI. In Finland, the auditing standards are called “Good Public Audit Practice”. They are based on the standards of INTOSAI.

Conclusion
In most of the countries, the audit of the accrual based financial statements of local government is conducted on the basis of generally accepted auditing standards. In about 75%, the auditing standards are based on the ISA or the ISA are applied directly.

4.5. Quality Control System

The questionnaire asked what other changes with regard to the audit of the financial statements of government were required due to the introduction of accrual accounting, in particular asking whether changes to the quality control system were required. The questionnaire did not explicitly ask whether the country has internal quality control systems in place or not. Therefore, the analysis of the answers may be incomplete.

Belgium, Germany, Malta, Portugal, the Slovak Republic Sweden and Switzerland state explicitly that no other changes with regard to the audit were caused by the implementation of accrual accounting.

The Netherlands already introduced accrual accounting for the local level in 1982. Therefore, they do no longer have enough specific information available about the consequences of the introduction of accrual accounting at that time. The same holds true for the local level of government in the UK, where accrual accounting was introduced over 50 years ago.

The comparability of the other responses is limited, as the responses are very specific. 5 countries pointed out that they have some kind of quality control system within the audit office (Latvia, Portugal, Romania, Switzerland, UK). In Finland in 2005 an external quality assurance system[9] organised by the Board of Chartered Public Finance Auditing was introduced.

Portugal is also implementing a quality control system, but not as a direct consequence of accrual accounting.

The auditing standards of the Romanian Court of Accounts stipulate the achievement of the audit quality analysis. This standard is currently under implementation.

In Switzerland a quality control systems was implemented. The Swiss quality control system is based on the Standard of the Institute of Internal Auditors "Basics of Internal Auditing"[10].

In Spain no significant numbers of audit were performed before the introduction of the accrual accounting in governments. Nowadays, for instance, there exists a quality control system within the local government.

Conclusion
5 of 20 countries pointed out that they have some kind of quality control system within the audit office. In 2005 in Finland an external quality assurance system organised by the Board of Chartered Public Finance Auditing was introduced. Because it was not explicitly asked whether the countries have internal quality control systems in place or not, it can not be inferred that the other countries do not have a quality control system. The results from the countries that responded show that the implementation of accrual accounting has resulted in a strengthening of the quality control of the audit process.

[9] For a description of the term "external quality assurance system" see section 3.5. of this paper.

[10] 1300: Quality Assurance and Improvement Program, 1310: Quality Program Assessments, 1311: Internal Assessments, 1312: External Assessments, 1320: Reporting on the Quality Program, 1330: Use of "Conducted in Accordance with the Standards", 1340: Disclosure of Non-compliance

5. CONCLUSION AND IMPLICATIONS

5.1. Results on the National Level of Government

15 countries which already introduced accrual accounting for the national government or for parts of it were analysed. About 10 of the 15 countries introduced accrual accounting in the last 10 years. In 13 of 15 countries the responsibility for the audit of the financial statements of the national government remains in the hands of the respective supreme audit institution. In two countries, the financial audit is done by audit firms (Israel and Slovak Republic). In the 13 other countries maximum certain parts of the audit work is performed by private sector auditors or other specialist.

8 out of 13 supreme audit institutions employ or will employ staff with a professional accountancy qualification for the financial audit. In 3 cases, there is an explicit requirement for such a qualification (Netherlands, Sweden and the UK). Besides the professional accountancy qualification, the majority of supreme audit institution staff have a degree in finance and/or economics. In none of the cases the requirement to prove the knowledge in accounting and auditing was introduced as a consequence of the change in accounting.

In all countries, the audit of the accrual based financial statements of national government is conducted on the basis of auditing standards. In 12 of 15 countries, the auditing standards are based on the ISA or the ISA are applied directly. In the other cases, the audit of the financial statements are conducted in accordance with INTOSAI based standards.

About 50% of the countries have some kind of quality control system within the audit institution. In one country an external quality assurance system was introduced. Because it was not explicitly asked whether the countries have internal quality control systems in place or not, it can not be inferred that the other countries do not have a quality control system.

Finally, the respondents were asked whether they consider the changes altogether with regard to the audit due to the introduction of accrual accounting in government as reform of the auditing. Over 50% of the countries responded negatively to the question. Nevertheless, one respondent argues that the introduction of accrual accounting represented a reform of the accounting requirements; audits became more complex, with more judgements to be made, but the underlying audit methodology did not need to change. By the evaluation of this answer it has to be considered that some of the countries who had not implemented an audit reform in response to the adoption of accrual accounting already employed qualified professional accountants and applied ISA based auditing standards before the introduction of accrual accounting.

One country has difficulties to evaluate its situation because the audit process and the introduction of accrual accounting took place at the same time. In the response it is emphasised that the two projects did not depend on each other.

By contrast, 4 countries confirmed that the introduction of accrual accounting makes a reform of the audit necessary (France, Israel, Portugal and Spain).

5.2. Results on the Local Level of Government

20 countries which already introduced accrual based accounting for local governments were analysed. Only 6 of these 20 countries introduced accrual accounting in the last 10 years. In 30% of the responding countries the responsibility and the performance of the audit of accrual based financial

statements is assigned to an audit office outside the local government. In 3 of these cases the countries have the possibility to subcontract the financial audit or parts of it to a third party, but they do not or only in exceptional cases make use of this possibility.

In 35% of the considered countries the audit of the accrual based financial statements is performed by private sector auditors or in the case of Finland by a special accountancy profession for the public sector. In general, the private sector auditor or the Finnish chartered public finance auditor is appointed by the local council.

In third group of countries (35%) the person or institutions who performs the financial audit depends on different legislation/requirements which in most cases relate to the size of the municipality. The tendency that bigger municipalities have their own audit office and in smaller municipalities the council appoints a private sector auditor or firm of cooperating municipal auditors can be observed. In this group 25% to 100% of the financial audit work is subcontracted to third parties, in general private sector auditors.

In 13 of 20 countries the financial audit is performed solely or partially by an audit office. 9 of these 13 audit offices employ staff with a professional accountancy qualification. In 5 cases, there is an explicit requirement for such a qualification. This leaves 4 of 13 countries (Belgium, Germany, Romania, Spain) were no professional qualified accountants are involved in the audit of the financial statements of local governments. In Spain staff members have to pass exams, but these exams are not comparable with an accountancy qualification in terms of the EU directive on statutory audits of annual accounts and consolidated accounts of enterprises. Besides the professional accountancy qualification, the majority of audit office staff have a degree in finance and/or economics. None of the 13 respondents answered that the requirement to prove the knowledge in accounting and auditing was introduced because of the transition to accrual accounting. However, in Finland a new professional accountancy qualification for the public sector was introduced about 5 years before the transition to accrual based accounting.

In most of the countries, the audit of the accrual based financial statements of local government is conducted on the basis of generally accepted auditing standards. In at least 75% the auditing standards are based on the ISA or the ISA are applied directly.

25% of the responses pointed out that they have some kind of quality control system within the audit institution. In one country an external quality assurance system was introduced. Because it was not explicitly asked whether the countries have internal quality control systems in place or not, it can not be inferred that the other countries do not have a quality control system.

Finally, the respondents were asked whether they consider the changes altogether with regard to the audit due to the introduction of accrual accounting in government as reform of the auditing. 40% of the respondents countries responded negatively to the question. Nevertheless, one respondent argues that the introduction of accrual based accounting implied a reform of the accounting requirements; audits became more complex, with more judgements to be made, but the underlying audit methodology did not need to change. By the valuation of this answer it has to be considered that some of the respondents who denied an audit reform already employed qualified professional accountants and applied ISA based auditing standards before the introduction of accrual accounting.

One country has difficulties to evaluate its situation because the audit process and the introduction of accrual based accounting changed at the same time. In the response it is emphasised that the two projects have not been linked to each other. Another country notes that it would be too early in the transition process to answer the question. It might be that further changes with respect to the audit will be necessary.

By contrast, 35% of the respondents confirmed that the introduction of accrual accounting makes a reform of the audit necessary (Cyprus, Finland, Italy, Poland, Portugal, Slovak Republic and Spain).

5.3. Conclusions

The implementation of accrual accounting has had a significant impact on public sector audit. However, this has not been considered as a reform of the auditing by most of the respondents. In particular, those Supreme Audit Institutions that employ qualified auditors were well placed to respond to the audit challenges they faced by the introduction of accruals accounting.

The following key messages were obtained from the questionnaire responses and related research:

- The audit of accrual based financial statements is more complex and causes more judgements to be made by the auditor than the audit of cash based financial standards;

- It was generally found that the audit is performed by suitable auditors who are qualified either by exams or by trainings and experience;

- Subcontracting all or part of public sector audits to third parties (usually private sector audit firms) can help to bring specialist skills to those audits where those skills are not present in the public sector audit body. It can also ensure that public sector audit bodies maintain their audit methodologies in line with best practice in the private sector;

- Where the person responsible for the audit does not have the relevant expertise (for example a local council responsible for appointing an auditor for a local government audit), the council should ensure that whoever it appoints (whether private or public sector auditor) has the relevant public sector and audit knowledge;

- If the audit is performed at the local level by an audit institution/office, this audit institution/office would benefit from the audit of several local government, because the auditors need experience which can not be gained by one audit a year;

- The educational requirements for the majority of bodies responsible for performing public sector financial audits was consistently high across the countries who responded. In most cases, the move to accruals accounting did not increase those educational requirements. However, all bodies have needed to ensure that either their professional training covered the accruals accounting principles or have had to provide specific training to their staff in those principles;

- Because the audit of accrual based financial statements is more complex and judgemental the application of generally accepted auditing standards is necessary to assure a uniform audit quality. The International Standards on Auditing (ISA) of IFAC are such generally accepted auditing standards in the public sector; and

- Quality control procedures in audit bodies may need to be enhanced with the introduction of accruals based financial statements, as audit judgements become more significant.

ANNEX A: QUESTIONNAIRE ON AUDITS OF FINANCIAL STATEMENTS OF GOVERNMENTS

	Question	Federal government	Regional/state government	Local government	Remarks
1.	**General issues**				
1.1	When was accrual accounting introduced for the government?				
1.2	On every level of government (federal, state or local) a body/institution is responsible for the audit. In general, this responsibility is placed on an audit institution. On the local level sometimes the municipal council itself or a committee is responsible for the audit. Who is responsible for the audit of the financial statements of the government in your country? Please give a short description of the body/institution.				
1.3	To which category belongs the described body/institution?				
	• Audit Institution				
	• Audit Committee				
	• Private Sector Auditor (e.g. audit firm)				
	• Other, please explain				

	Question	Federal government	Regional/state government	Local government	Remarks
1.4	Depending on the jurisdiction the body in charge can subcontract someone else as an auditor, e.g. a private sector auditor. Does the body in charge in your country appoints someone else to perform the audit of the financial statements of the government? If yes, who is appointed (e.g. audit institution of the neighbouring municipal, private audit firm)? Please describe.				
1.5	If yes, how many percent of the financial audit work is subcontracted to third parties?	____ %	____ %	____ %	
1.6	If the audit of the financial statements is performed by the audit committee/institution itself, what is the educational background of the staff? Tick all that apply:				
	• Professional accountancy qualification (e.g. CPA-Exam, CCA, Wirtschafts-pruefer)				
	• Lawyers				
	• Degree in public management/administra-tive sciences				
	• Degree in finance and/or economics				
	• Degree in engineering				
	• Other, please explain				

	Question	Federal government	Regional/state government	Local government	Remarks
2.	**Audit objectives**				
	What are the objectives of the audit of the financial statements of the government? Tick all that apply:				
	• To form an opinion on whether the financial statements give a true and fair view of the net assets, financial position and results of operations of the audited entity				
	• To form an opinion on whether the financial statements are complete and accurate, and are disclosed in line with the relevant financial reporting framework				
	• To form an opinion on whether the assets and liabilities exist, are owned by the audited entity, are completely recorded and are valued according to appropriate, consistently applied accounting policies				
	• To form an opinion on whether the transactions undertaken by the audited entity are in compliance with laws and regulation other than accounting policies (compliance audit)				
	• To form an opinion on the effectiveness of the accounting-related internal control system				
	• Other or additional, please describe				

	Question	Federal government	Regional/state government	Local government	Remarks
3.	**Training**				
3.1	In connection with the introduction of accrual accounting how was the audit staff of the audit institution trained in the new accounting and auditing issues? Please describe.				
3.2	Do the employees of the audit institution have to pass an exam (like CPA-Exam) or other test to prove their knowledge of accrual accounting and auditing? Was this requirement newly introduced as consequence of the transition to accrual based accounting? Please describe.				
4.	**Reorganisation of the audit process**				
	In connection with the introduction of accrual accounting in government how was the audit process reorganised and how were the audit objectives changed? Please describe.				
5.	**Auditing standards**				
5.1	In connection with the introduction of accrual accounting was it necessary to introduce auditing standards or to revise the existing auditing standards in order to conducted the audit of the financial statements of government accordingly? Please describe.				
5.2	Who sets the auditing standards for the audit of the financial statements of government (e.g.				

	Question	Federal government	Regional/state government	Local government	Remarks
	national auditing standard setter, parliament)? Please describe.				
5.3	Are the auditing standards based on the following (Tick all that apply:):				
	• The international standards on auditing published by the IAASB of IFAC?				
	• National auditing standards for the private sector				
	• Others? Please describe.				
5.4	Are the same auditing standards for the audit of the financial statements used by the federal, the state and the local government of your country? Please describe.				
5.5	Are the same auditing standards for the audit of the financial statements used by all public sector auditors within the same level (federal, state and local government) of your country? Please describe.				
6.	**Other changes**				
6.1	What else was changed with regard to the audit of the financial statements of government due to the introduction of the accrual basis of accounting? For example, implementation of a quality control system for the audit body/institution or changes in the form of reporting. Please describe.				

	Question	Federal government	Regional/state government	Local government	Remarks
6.2	What other problems did your country faced with regard to the audit aspect in connection with the introduction of accrual accounting in government? What recommendations would you give countries which intend to implement also accrual accounting (lessons learned)?				
7.	**Conclusion**				
	Would you consider the changes altogether with regard to the audit due to the introduction of accrual accounting in government as reform of the auditing?				
	• Yes				
	• No, please explain				

Annex B: Countries which Responded to the Questionnaire and Status of the Introduction of Accrual Accounting in Europe

The following table shows which countries already introduced accrual accounting on the different levels of government and which not. If the respective level of government introduced accrual accounting, the year is given in which the introduction took place. In some countries in parts of the government accrual accounting is applied but not for the whole level. For example in Germany three of sixteen states account parallel on the cash and on the accrual basis. Another example is the Dutch federal government. The government wide accounting is on the cash basis, but some parts of the government (e.g. executive branches of the national government, called agencies) use since 1994 an accounting system based on accruals.

		National Level	**State/Regional Level**	**Local Level**
1.	Austria	2013		
2.	Belgium			1995
3.	Cyprus		N/A	1985
4.	Czech Republic			
5.	Denmark	2002 - 2007	2004	2004
6.	Finland	1998	N/A	1997
7.	France	2006	in the early 2000´s	in the late 1990´s
8.	Germany			2004 – ca. 2016
9.	Greece			1999
10.	Hungary			
11.	Israel	2004	N/A	N/A
12.	Italy	1997		1995*
13.	Latvia	2003	N/A	2003
14.	Lithuania		N/A	
15.	Malta	2002*		1995
16.	Netherlands		1979	1982
17.	Norway			Starting 1924
18.	Poland		N/A	in the early 1990's
19.	Portugal	in the early 1990´s	in the early 1990´s	in the early 1990´s
20.	Romania	2006	N/A	2006
21.	Slovak Republic	2008	2008	2008
22.	Slovenia		N/A	

		National Level	State/Regional Level	Local Level
23.	Spain	1983	1986	1992
24.	Sweden	1991	1986	1986
25.	Switzerland	2007	1975 - 2000	1975 – 2000
26.	United Kingdom	2000	2000	ca. 1950´s

Legend:

*	Accrual accounting has not yet been introduced officially, but since the given date an additional set of financial statements are prepared on the accrual basis of accounting for internal use.
	Accrual accounting was not yet introduced.
	In parts of the respective government level accrual accounting was introduced.
N/A	The respective level of government does not exist in the country.