



Extract from the report to the
Public Accounts Committee on
accrual and deferral entries in
government accounts

October
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1. Introduction and conclusion

1.1. Purpose and conclusion

1. This report concerns how ten government bodies make accrual and deferral entries in their accounts at year-end to address timing differences. The report focuses on assessment-based entries, ie assessments to determine whether items should be deferred to the following accounting year or be recognised in the current period. In some instances, the government bodies will also be required to estimate the size of the amounts involved. Compared with the overall government accounts, however, entries of this nature make up only a small number.

The key characteristic of such entries is that they are assessment based and have a bearing on the spending of the government bodies and thus their compliance with appropriations. For instance, if expenses that should have been distributed among several accounting years are all recognised in the same accounting year, the government body will appear to have exceeded its appropriation.

In 2012, the Danish government introduced a budget ceiling, which – among other things – means that government bodies are not allowed to transfer and use surpluses accumulated in previous accounting years, without prior agreement. There is therefore a risk that government bodies use these entries as a cover for transferring or hiding funds across fiscal years.

The audit findings related to the individual government bodies have been reported separately in connection with the annual audit for 2013 and will be followed up during subsequent annual audits.

2. The purpose of the study is to determine whether the examined government bodies have established satisfactory practices for recognition and distribution of expenses at year-end based on a clear and comprehensive set of rules. Rigsrevisionen has examined the following items in the accounts of the ten government bodies:

- appropriations for purposes that have not been completed during the fiscal year
- provisions
- overtime owing
- distribution of expenses among accounting years
- distribution of prepaid revenues and expenses among accounting years.

3. This report is a spin-off from the annual audit of the Danish government accounts and as such a narrow report.

The audit approach and quality requirements to **narrow reports** are identical with those applying to Rigsrevisionen's other reports, but the scope of narrow reports is more limited.

CONCLUSION

Rigsrevisionen has concluded that in general the ten government bodies have established satisfactory practices for inclusion and distribution of expenses and prepayments at year-end.

Rigsrevisionen is also of the opinion that the set of rules developed by the Ministry of Finance generally underpin that the government bodies distribute and recognise expenses and prepayments correctly in the accounts.

However, Rigsrevisionen noted isolated errors in the accounts and noted also that the government bodies tend not to establish the necessary minimum thresholds for distribution of expenses and prepayments among accounting years that are prescribed by the rules.

Rigsrevisionen therefore made a number of recommendations to the Danish Agency for Modernisation under the Ministry of Finance to promote a better practice in the individual government bodies in respect to including and distributing expenses and prepayments among accounting years.

Half of the accounting instructions of the government bodies fail to address minimum thresholds

The examination shows that half of the accounting instructions of the government bodies do not include minimum thresholds that determine whether expenses and prepayments should be recognised in one accounting year or be distributed among several accounting years. According to the set of rules developed by the Ministry of Finance, this information must appear from the accounting instructions to ensure a consistent practice from case to case and from one year to the next.

Rigsrevisionen sees a need to tighten the accounting instructions as regards the definition of minimum thresholds to ensure that the government bodies follow the rules. The Ministry of Finance should assist the government bodies with guidance and examples of how these thresholds can be determined and used in practice.

Isolated errors in the accounts

Rigsrevisionen found isolated errors in the government bodies' accounts in connection with, for instance, the use of funds reserved for specific purposes and entering of salary provisions and other operational provisions.

The audit also showed that one government body – with many and large provisions – had based its estimation of the related amounts on different principles; in several cases, the government body recognised all the estimated expenses, whereas it in one case recognised an amount that reflected what the expenses could potentially amount to. The principles used affect the financial results of the government bodies differently.

The annual audit showed that three government bodies had made provisions that were not in compliance with the set of rules developed by the Ministry of Finance. Rigsrevisionen estimates the value of these errors at in total DKK 9.7 million.

Rigsrevisionen also found that one government body had made a provision for an expected obligation to repay DKK 24.1 million concerning the accounts for 2012. This provision was made following an oral request and was thus recognised on an uncertain basis. The provision was not re-considered in 2013 despite the fact that written documentation of the repayment obligation had not been provided.

The audit also showed that one government body had recognised expenses of DKK 14.8 million for IT licenses in the accounts for 2013 without proper documentation that the amount should be recognised in that accounting year.

Rigsrevisionen also identified isolated cases where the accounts for salary and other operational provisions had been incorrectly used, which may have a bearing on the government body's statement of payroll costs in the annual report.

Provisions and overtime owing

In one specific case, the government body had made a provision on the basis of a decision by the Danish parliament, a political agreement and a proposed bill. According to the rules, government bodies are only allowed to make provisions that are either legally based or based on an actual obligation.

At the same time, the rules prescribe that provisions can only be recognised in the accounts when the probability of a drain on the financial resources exceeds 50 per cent. Assessing the probability of a bill being passed requires a certain measure of interpretation of the rules and the government body estimated that if the bill were passed it would entail expenses of approximately DKK 600 million.

In this specific case, the government body argued that the decision made by parliament in combination with the political agreement represented an actual obligation and a more than 50 per cent probability that the bill would be passed. Rigsrevisionen agrees with this assessment.

Rigsrevisionen has noted that another government body does not include overtime owing in the accounts because overtime is counterbalanced. According to the rules – and irrespective of whether the employees receive paid time off or are paid extra – the management of the government body should regularly consider whether the amount of overtime is such that it should be recognised in the accounts, Rigsrevisionen finds that this should be clarified to the government bodies.

The set of rules developed by the Ministry of Finance

Rigsrevisionen finds that the set of rules developed by the Ministry of Finance generally underpin that the government bodies distribute and include expenses and pre-payments correctly in the accounts.

Rigsrevisionen also finds that the ministry needs to specify the circumstances under which bills may provide a basis for making provisions in the accounts.

*The **accounting practice** applied in government administration is based on the accounting principles included in the executive order on the presentation of financial statements and other administrative guidance.*

The government accounting practice may be either cash or accrual based.

The accounting practice applied is reflected in the methods and criteria used for making accrual and deferral adjustments and for recognition of items entered in the accounts.

Rigsrevisionen recommends that the Ministry of Finance should intensify its efforts to ensure that the government bodies describe and justify their accounting practices in the areas where they have different options and are required to make assessments. This will serve to support the government bodies that have insufficient knowledge of the rules and improve the accuracy of the government accounts. Rigsrevisionen recommends that the Agency for Modernisation should

- support the government bodies and provide them with examples of how minimum thresholds for distribution of expenses and prepayments can be defined;
- clarify to the government bodies that they need to assess – on a regular basis – whether overtime owing should be recognised in the financial statements;
- further develop the rules on provisions and specify more clearly the status of bills;
- clarify the wording of the government's chart of accounts to facilitate identification of the appropriate accounts for entering of salary provisions and other operational provisions;
- clarify the wording of the government's chart of accounts to ensure that it is clearly stated which accounts the government bodies may use for distribution of expenses and prepayments among accounting years.