



MOMENTS IN THE MODERNISATION OF PUBLIC ACCOUNTING IN ROMANIA. A CASE STUDY REGARDING THE REVALUATION AND ARMONIZATION OF FIXED ASSETS

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Abstract

The introduction of accrual accounting in the public sector is a recent phenomenon and a worldwide subject of debate. In this article, we presented the steps taken by Romania in adopting accrual accounting, first as a candidate country for European Union accession and later as a member state. Furthermore, we studied how the transition to accrual accounting led to a better management of the assets of public institution while choosing, as a case study, the revaluation and amortization of fixed assets.

The scientific approach of this research paper consists of two parts: in the first part, we presented a gradual historical evolution of public accounting, combined with Romania's efforts in adopting accrual accounting. In the second part, we showed, in the form of a case study, the advantages of introducing amortization and revaluation of fixed assets as a first step in the strengthening of accrual accounting.

Keyword: accrual accounting, cash accounting, revaluation, amortization

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I. Introduction

Currently, the global public sector utilises two basic methods in determining when transactions or events are recorded in the financial statements: cash accounting (traditional method) and accrual accounting (modern method) (Tiron Tudor și Fătăcinean, 2006). Cash accounting, which is better understood by accounting practitioners, recognises transactions and events only when cash is received or paid while accrual accounting recognises transactions and events when they occur, regardless of when cash is paid or received (Ștefănescu, Țurlea, 2011). Accrual accounting, which has been shown to be the best in offering relevant and reliable information, is a component of the concept called New Public Management (NPM). This concept is supported by major international bodies: the International Monetary Fund, the World Bank, the European Bank, OECD and it aims to blur the boundaries between the public and the private sectors.

Internationally, Chile was the first country to introduce accrual accounting in the 70s, followed by New Zealand, USA (partially), Canada, as well as the member states of the European Union (Wynne, 2004). In fact, the European Union recommends the introduction of accrual accounting to all the countries wishing to apply for membership.

Another supporter of accrual accounting is IFAC. Established in 1977, the International Federation of Accountants (IFAC) (the global organization for the accountancy profession) has the mission of serving “the public interest, contributing to the development of high-quality standards and guidance, facilitating the adoption and implementation of high-quality standards and guidance, contributing to the development of strong professional accountancy organizations and accounting firms and to high-quality practices by professional accountants, promoting the value of professional accountants worldwide and speaking out on public interest issues.”

Eighteen years later, in 1995, IFAC created IPSASB (International Public Sector Accounting Standards Board). The purpose of establishing this organization was the development of accounting standards for the public sector which would have the following characteristics: to ensure the need for a common language on a world-wide level, to facilitate the work of those who prepare, audit or utilise the financial statements, to bridge the gap between public and private entities, to help ensure a common basis for accounting and reporting in all countries, to help reduce costs because accountants,



auditors, financial analysts, investors and regulators will no longer be forced to convert or to reconcile the financial statements of a set of standards to another set of standards.

The IPSAS standards (a total of 32), inspired by the International Financial Reporting Standards (IFRS), are intended for public sector entities other than state economic entities. At present, no country has fully implemented IPSAS since IPSASB cannot enforce the adoption of the international accounting standards for the public sector. Efforts in this respect have been made by France, Germany, UK and Australia.

On December 17, 2002, the European Union decided that 2005 should mark the transition from cash accounting to accrual accounting in order to present information which is credible, transparent and comparable in the public sector.

Romania, eager to join the EU, faced this challenge and started the transition from cash accounting to accrual accounting. Thus, one of the conditions of accession (introduced in chapter 11 “Economic and Monetary Union” of the Position Document) was the convergence of public accounting with the European Regulations, the International Public Sector Accounting Standards (Alec, 2010) and the reporting of public finances data in accordance with the European System of Accounts (ESA 95).

Convergence implies the taking over, on a national level, of the IPSAS spirit, its conceptual framework and the adoption of some of the accounting treatments specified in the international standards (Ilie, Alec, 2011). Romania opted for the indirect method of IPSAS implementation, which means that the national accounting norms are developed based on the provisions of international standards. The primary cause of choosing this method was the fact that most public accountants were unaware of the international accounting standards for this sector. More specifically, a study made by Tiron A. and Fătăcean Gh. shows that 73% of the public sector accountants have no experience in applying accrual accounting while the remaining 27% are knowledgeable in the field either from school or from having worked in the private sector.

At the basis of the convergence between Romanian public institutions accounting with IPSAS lies the financial statements that aim “to provide information that is useful for decision-making and to demonstrate the accountability of these entities for the resources entrusted to them.” Thus, with the implementation of order 1917/2005, public institutions in Romania must prepare financial statements that “offer a true image of the assets, liabilities, financial position (net assets/equity) as well as of the financial performance and equity statement” and that meet the requirements of IPSAS and of the consolidated



Financial Regulation applicable to the general budget of the European Communities no.1605/2002 and European Commission Regulation on detailed rules for implementing the Financial Regulation no.2342/2002, chapter referring to “Presentation of the accounts and accounting”:

- Statement of financial position (balance sheet). National norms comply with international recommendations, assets and liabilities are divided into current and non-current and, inside the groups, assets are presented in ascending order according to their liquidity and liabilities in ascending order according to their chargeability;
- Statement of financial performance (profit and loss account). The structure of the profit and loss account respects the minimum requirements by showing revenues and funding according to their nature or source (whether received or not) and the expenses according to their type or purpose (whether paid or not). The main characteristic of the equity statement is represented by employment and not collection or payment;
- Statement of changes in net assets / equity;
- Statement of cash flows grouped by type of activity in: operating, investing and financing activities. However there are still some differences between national standards and IPSAS 2;
- accounting policies and notes to the financial statements;

In addition to IPSAS 1 (“Presentation of Financial Statements”), the public institutions in Romania prepare budget execution accounts. This is due to the fact that the budget is cash-based while financial statements are accrual-based and, according to IPSAS 24 (“Presentation of budget information in financial statements”), when the budget and financial statements are not drawn up in the same system, a separate financial statement must be made.

II. Romanian’s efforts in adopting accrual accounting. Phases in the evolution of public accounting in Romania

The purpose of this research is to present the benefits of introducing fixed asset revaluation in the public institutions of Romania but not before presenting briefly the evolution of public accounting.



According to the research made, one can talk about three major periods in the evolution of public accounting in Romania:

✓ *Pre-communist period (1860-1947)*

Public accounting has its origins in the Financial Regulation adopted in 1860, after the union of Moldavia and Walachia. Four years later, in 1864, the Public Accountancy Act is adopted. It regulated the development, adoption and implementation of the state budget in Romania (Alec, 2010). Later, in 1929, after a period of tax reforms, a new Public Accountancy Act was adopted (Demetrescu, 1972). It contained the following innovations: the introduction of double entry accounting, the 12 months fiscal year instead of 18 months, the preventive financial control, the establishing of the four phases regarding employment, liquidation, authorization, payment, as well as mandatory inventory of public assets.

✓ *Communist period (1948-1989)*

During this period, public accounting was greatly influenced by the Sovietic Union and answered the needs of a planned economy (Calu, 2005). Cash accounting presented advantages such as: ease of use, comprehensibility for a wide range of users, concise presentation of the financial statements, reduced implementation costs. The major disadvantages in using accrual accounting consisted of the inability to create a complete image regarding assets and liabilities, debts and claims.

✓ *Post-communist period (1990-present day)*

In its turn, this period can be divided into the following phases:

- *Phase I: 1990-2002;*

After 1989, when Romania transitioned from a centralised economy to a market economy, and by 2002, there was little change. Public administration used the same system based on cash accounting, which was based on a legal framework available since 1984 and which had undergone little change (Deaconu et al., 2011). Thus, the first to undergo some changes was the Accountancy Act which makes reference to public accounting. It must include: income and expenditure accounts, general accounts (based on the principle of rights and obligations detection) and state treasury accounts.

At the end of 2002 the Ministry of Public Finances adopted two orders that take a step towards accrual accounting: Order 1746/2002, approving the methodological norms regarding the organization and management of asset accounting for public institutions, the chart of accounts and the monograph of the main operations (applied experimentally on



13 public institutions) and Order 1792, approving the four phases of budgetary execution of expenditure to be completed by all public institutions, irrespective of the financing manner of these expenses with the mandatory compliance with procedures. Public institutions are also required to organize, to lead the bookkeeping and report on budgetary and legal commitments starting with fiscal year 2003.

- *Phase II: 2003-2005, preparatory for accrual accounting adoption;*

In 2003-2005, the accounting-standard setter in Romania, the Ministry of Finance, through the Public Institutions Accounting Methodology General Directorate, adopted a series of laws by which the legal framework undergoes changes by assimilating specific elements of accrual accounting: improvement of budget classification, establishing of economic classification priorities according to the institutional and functional classification. Complementing the Accountancy Act, Order 520/2003 is issued on the organization and management of accounting revenues.

The novelty regarding the registration of fixed assets in accounting was introduced in 2003 when, by adopting Ordinance 81 and the Order 1487/2003, depreciation and reassessment are introduced to reflect the real value of goods (later replaced in 2008).

In 2005, in the context of undertaken commitments for accession to the European Union, Order no. 1917/2005 approving the methodological norms regarding the organization and management of accounting in public institutions was emitted. It was developed in accordance with IPSAS standards and European directives.

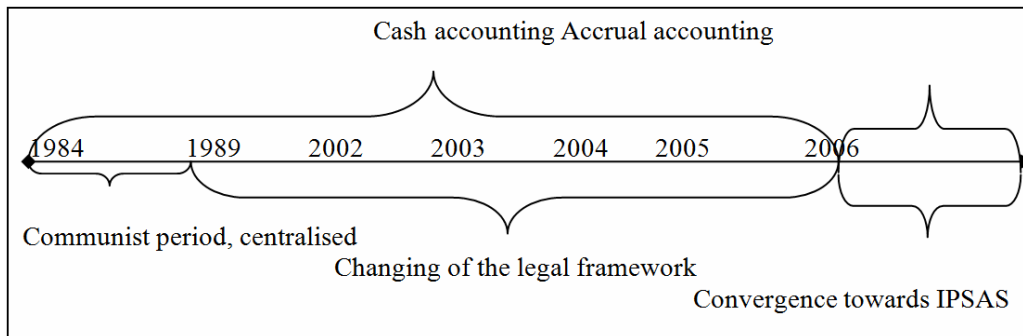
- *Phase III: 2006-present day*

By January 2006, the public institutions in Romania had applied the provisions of Order no. 324/1984.

According to Order 1917/2005, all public institutions must prepare financial statements congruent with accrual accounting conditions, lead double entry bookkeeping (until now a large number of public institutions, including rural town halls, led single entry bookkeeping).



Figure 3- Short presentation on the evolution of public accounting in Romania



Source: own processing

III. Case study on revaluation and depreciaton of fixed assets in the Romanian public sector

The revaluation of fixed assets is performed at their fair value. The fair value of fixed assets is, according to IPSAS 17, the market value determined by appraisal and performed by professional evaluators. Furthermore, the standards provide two methods of revaluation (Dascălu *et al*, 2006):

- Gross value method. This method consists in the simultaneous revaluation of the gross value of fixed assets and in the accumulated depreciation by multiplying the book value with an index (method adopted by national norms).
- Net worth method. This method consists in the revaluation of the accounting net worth.

For the first time in the history of Romanian public accounting, in 2003, by introducing revaluation, assets were brought to their “current cost or their book value updated in conjunction with the utility of these goods and their market value.” To exemplify, we present the following table on the revaluation of two buildings used for education.



Table 18- Comparative situation regarding the revaluation and depreciation of fixed assets

Name of asset	Year of entry as heritage	Book value (denominated) RON	Revaluated value 2003 (denominated) RON	Revaluated value 2009 (denominated) RON	Revaluated value 2010 (denominated) RON
Building A	1972	922,39	5.340.843,42	5.843.416,79	7.752.233,16
Building B	1982	1312,23	5.064.429,34	9.533.230,96	11.580.558,37

Source: own processing

For the revaluation of the assets, the book value of the fixed asset was taken into consideration at the entry date as heritage correlated with an update coefficient available on December 31, 2002. For the building A that had been included in the national heritage in 1972, the coefficient used is 5790,2 while for the building B the coefficient used was 3859,4 (Order 1487 of 2003 on revaluation and depreciation of fixed assets).

We notice that the two buildings are recorded in the accounts at token values. Generally, this causes an underestimation of the state's public assets. Because of this and of the need for compatibility between national norms and the Community acquis regarding the generally accepted accounting principles and rules on the preparation and presentation of the accounts of public institutions, the necessity of developing the legal framework which would allow the recording of revaluation and depreciation of fixed assets owned by public institutions. Regarding the time of revaluation, it coincides with the international accounting standards for the public sector (IPSAS 17): assets revaluation must be performed on a regular basis so that the book value will not differ significantly from the one that could be determined if fair value is used.

Next, we will present the manner in which book value in accounting was determined, updated for the building A:



Table 19- Practical example of a calculation; building revaluation and depreciation

No.	Bookkeeping entry value	Normal operating time	Normal operating time, consumed on revaluation date	Level of usage	Value corresponding to normal operating time, consumption function	Value corresponding to remaining normal operating time
	1	2	3	$5=3/2$	$6=1*5$	$7=1-6$
Building A	5.340.843,42	600	438	0,7300	3.898.815,70	1.442.027,72
Building A	5.843.416,79	600	452	0,7533	4.402.040,65	1.441.376,14

Consumption price index	Updated accounting book value (revalued)	Accounting revaluation differences to be recorded on revaluation date	Accounting revaluation differences to be recorded on revaluation date, corresponding to normal consumed operating time	Accounting revaluation differences to be recorded on revaluation date, corresponding to remaining normal operating time	Depreciated value
8	$9=1*8$	$10=9-1$	$11=10*5$	$12=10-11$	$13=7+12$
109,41%	5.843.416,79	502.573,37	366878,56	135.694,81	1.577.722,53
132,67%	7.752.233,16	1.908.816,37	1437975,00	470.841,37	1.912.217,51

Source: own processing

The accounting treatment of revaluation results, as stipulated by the standard, has been adopted by the national norms as follows (Ilie, Alecu, 2011):

- if, after performing revaluation, the asset value increases, this increase is treated as a growth in the revaluation reserve or as an income. This is achieved as long as it compensates an expenditure of that asset whose decrease was previously recognised;



- if, after performing revaluation, the asset value is reduced, this reduction is treated as a revaluation reserve decrease or as an expense, unless a reserve relating to that asset is recognised.

As far as the treatment of depreciation at the moment of revaluating an asset is concerned, national norms coincide with those of IPSAS 17:

- either depreciation is restated proportionately with the change in the gross book value of the asset. In this case, the book value of the asset after revaluation equals its revalued value. This method is used when the asset is revalued by applying the consumer price index announced by National Institute of Statistics.

- or depreciation is removed from the gross book value of the asset and the net amount restated to the revalued amount of the asset. This method is used when the asset is revalued to market value.

IV. Conclusion

Political decision at first, later, a challenge for the accounting profession, the adjustment of the Romanian public accounting to the International Standards for the Public Sector under accrual accounting conditions is certainly a step forward, bringing with it essential advantages, such as: a complete image of assets and liabilities, multi-annual financial statement presentation, analytical presentation of accounting records, increased efficiency of management and decision-making due to better information, more efficient audits due to clear and consistent records, tighter political control through a better understanding of the financial impact of policies, minimized risk of error in payments to beneficiary ([www. ec.europa.eu](http://www.ec.europa.eu)), provides international comparability, especially between EU Member States. Among the disadvantages of accrual accounting the high implementation costs and lack of specialized personnel can be mentioned. From the research carried out, we noticed that the staff used to working by cash accounting rules found it hard to adapt to those of accrual accounting.

Furthermore, for a better correspondence between the data presented in the budget and that provided by accountancy, adoption of the commitment budget is necessary. The currently used cash budget contains the following components, as far as revenue is concerned: initial budgetary provisions, final budgetary provisions, performed revenues and, as far as expenditure is concerned: achieved revenues, commitment appropriations,



initial budget loans, definitive budget loans, payments made (Alecă, 2010). An accrual budget should include information on identified entitlements and budgetary provisions, as far as revenue is concerned, and commitment and budget appropriations, as far as expenditure is concerned.

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