

Practical Issues in convergence to Accrual System of Accounting .

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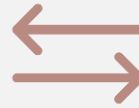
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Urban Local Bodies and need for accounting reforms



Accrual Based Double Entry System of Accounting (ABDEAS)



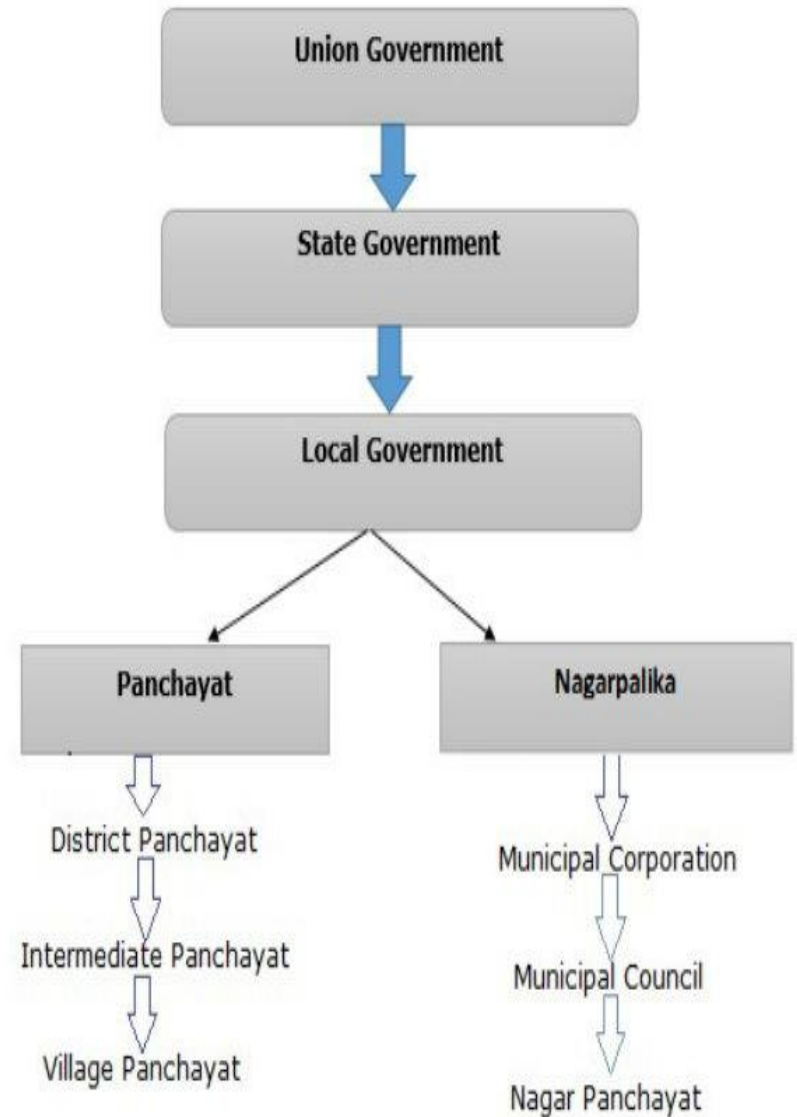
Conversion / Convergence to ABDEAS : An interesting and challenging journey



Practical issues and the suggested mitigation measures

INTRODUCTION

- The third tier of Government: Local Government.
- Municipal Corporation (Nagar Nigam)
- Municipal Council (Nagar Palika)
- City Council (Nagar Parishad).
“Urban Local Body” (ULB).
- Engaged in Construction and maintenance of Civic Infrastructure and in providing Citizen centric services:



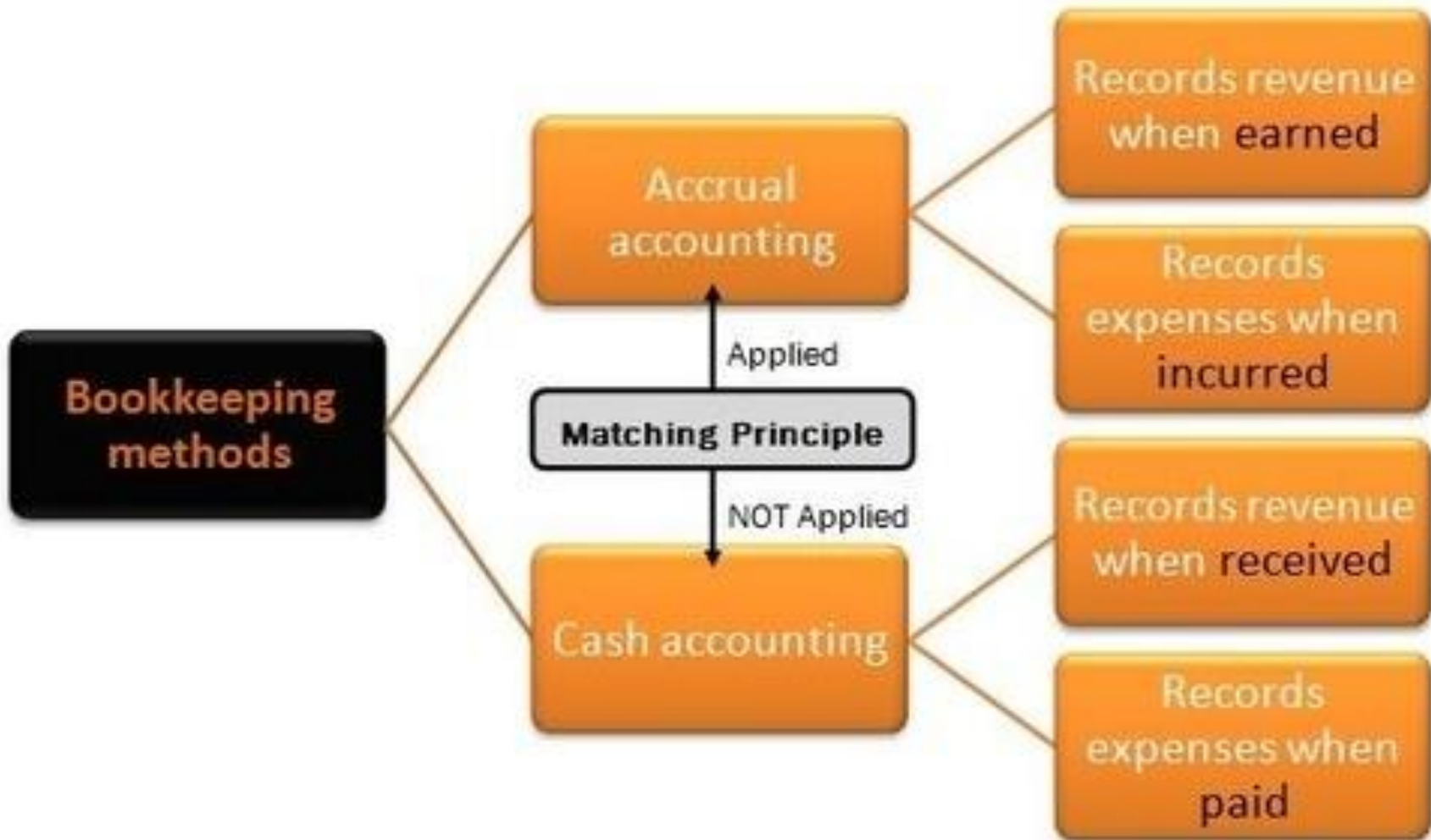
Functions of Urban Local Bodies

- Regulatory Role: Building permission, Fire safety permission, Trade License, Gumashta.
- Citizen centric services : Sanitation, Birth and death certificates, Health and Hygiene, Education , Water supply.
- Infrastructure creation and maintenance : Library, City hall, community center, city buses, bus stand, Ambulance service, Roads ,Pathways, Ponds , lakes, Lights , Parks , Cremation ground , Fire tender, Gym, monuments etc.



Need for accounting reforms :

- Financial Self sustainability is the target and accounting reform is the way to achieve it .
- Cash Basis of accounting. Matching of revenue receipts / expenditure .
- Single Entry system. Distinction between Revenue and Capital expenditure / receipt Asset / Liability not recognized.
- Back log of accounting and audit .
- Lack of internal financial controls / MIS .
- Budget more like a formality.
- Delayed/ Incomplete statutory compliances



Another graphic that may help explain the difference is provided below:

Cash method of accounting

- Transactions are recorded when money is received and money is paid .
- Revenues are not recorded until cash is received
- Expenses are not recorded until cash is disbursed.
- Hence if money is not received the income and expenditure account would not have any mention of it .
- Matching of Revenues and Expenditure not possible .
- Similarly a surplus may get reflected , just because payments are not made .
- Financial picture is neither sufficient nor conclusive to take any decision .

Single entry based accounts

- Single entry system does not recognise any enduring benefit of any money outgo and hence nothing is recognised as an Asset.
- Similarly there is no recording of any obligation and thus the receipt and payment account does not contain any information about how much the entity owes i.e Liabilities
- No distinction between revenue and liability
- No distinction between out go and asset .
- Single entry system of accounting is normally on cash method of accounting .
- Budgets are made and actual achievement is measured with respect to such budgets .

Challenges in working :

- Multiple stakeholders with different priorities. Center , State , District
- Lots of approvals required to execute projects.
- Inter department challenges.
- Slow speed of execution

- Capacity constraints
- lack of dedicated cadre for accounts and finance.
- Engagement of personnel in other Govt work such as, census, election duty
- Frequent transfers.

Finance related

- Slow assessment and recovery of taxes and charges.
- Lack of budgetary controls
- Insufficient funds at disposal.
- Dependence on State / Central Government support.

Accrual Based Double Entry Accounting System (ABDEAS)

BASIS OF DISTINCTION	SINGLE ENTRY CASH BASED ACCOUNTING	ACCRUAL BASED DOUBLE ENTRY ACCOUNTING SYSTEM
FINANCIAL PERFORMANCE	FINANCIAL PERFORMANCE CANNOT BE ASCERTAINED AS INCOME AND EXPENDITURE ACCOUNT IS NOT PREPARED	FINANCIAL PERFORMANCE OF AN ENTITY CAN BE ASCERTAINED AS INCOME AND EXPENDITURE ACCOUNT IS PREPARED
FINANCIAL POSITION	ONLY A STATEMENT OF AFFAIRS IS PREPARED WHICH DOES NOT GIVE THE TRUE AND FAIR STATE OF AFFAIRS	A BALANCE SHEET IS PREPARED ON GOING CONCERN BASIS WHICH GIVES A TRUE AND FAIR PICTURE OF FINANCIAL POSITION
AUTHENTICITY	THIS SYSTEM IS NOT CONSIDERED AUTHENTIC BY THE FINANCIAL INSTITUTION, LENDING AGENCIES AND OTHER BODIES	THIS SYSTEM OF ACCOUNTING IS WELL ACCEPTED BY THE FINANCIAL INSTITUTION, LENDING AGENCIES AND OTHER BODIES

An
interesting
and
challenging
journey :

1. Selection of NMAM or State Manual.
2. Selection of Software :
3. Sustainability of reforms : use of technology , training , capacity building.
4. Opening Balance Sheet : Assets and Liabilities :
5. Chart of Accounts . Function, Department, Source.
6. Conversion of Single Entry Based accounts in to Double Entry based accounts
7. Conversion of Cash Based accounting in to Accrual Based Accounting
8. Development of tools to get the desired MIS.



- Handholding is the key to successfully implementation of accounting reforms

Opening Balance Sheet : Assets

- Fixed Assets :
 - Immovable Assets :
 - Movable Assets :
- Current Assets :
 - Cash and Bank Balances :
 - Fixed Deposit receipts
 - Receivables : Tax and non Tax revenue
 - Inventory : Different departments viz : Health , Sanitation , Fire etc
 - Advances to various suppliers , employees , festival advance , travelling advance etc
 - Other Current assets :

Common Practical Issues : Assets

Identification of assets
: roads, sewage, Tanks ,
Parks , Monuments ,
buildings : Survey ,
compilation .

Depreciation on assets
:

Date of put to use :

Valuation / Cost
Ascertainment.

Source of funds
whether Grant
Donation or Municipal
Funds

Authentication of the
information .

Opening Balance Sheet : Liabilities

1. Loans from Government :
2. Loans from Banks / Fis / Multilateral Institutions :
3. Other term liabilities :Gratuity / Pension
4. Grant funds (Reserve): Earmarked / Capital
5. Grant funds : General / Revenue
6. Municipal Funds :
7. Unspent amount of grant :
8. Current Liabilities
 - (a)Payables
 - (b)Provisions
 - (c)Other current liability

Common Practical Issues : liabilities

Determination of amount payable

Issue with respect to final Bill of Contractor

Mismatch of unutilised grant with underlying Bank Balance / FDR

Interest on grant funds :

Matching of unspent grant with available physical funds.

Authentication of the information .

Approval on compilation .

PRACTICAL ISSUES AND MITIGATION MEASURES : Data and information Collection:

COMMON ISSUE	MITIGATION
Non-cooperation from ULB Staff	Regular Follow-up with Staff and UADD Officials, Use of Technology
Non-Availability of Data records and information.	Alternative records : payment details, completion certificates, grant utilization certificates , inauguration stone , direct confirmation from Banks, last paid bill , subsidiary records : Medicine stock , sanitation stock , purchases at the fag end of the year
Records Destroyed	Accounting with available records and information.
Contradictory information / Multiple set of records .	Consensus on use of any particular set of information.
Records seized by Police , EOW, tax authorities , investigative agency / Court	Demand photocopy of seized material .
Non Availability of personnel	Concept of Nodal officer , periodical meetings with higher official , documentation of proceedings .

PRACTICAL ISSUES AND MITIGATION MEASURES : Migration of Accounts

COMMON ISSUES	MITIGATIONS
Different ways of record keeping by different department in the same Ulb and / or amongst different ULBs.	Bringing consensus on using a similar pattern of record keeping and bringing defined new system of accounting .
Bank-wise balances not available in manual Cash Book	At the time of preparation of Bank Reconciliation Statements recheck the outstanding entries with Cheque Issue Register and other available records.
Totaling / Clerical Mistakes in manually maintained Cash Books	Identification and segregation.
Proper Narrations not given in Cash Books for payment entries	Voucher control sheet, study and interaction with ULB personnel.
CA normally perceived as an auditor	It is necessary to clarify to all stake holders that the assignment for convergence / conversion of accounts is not an audit transaction.

PRACTICAL ISSUES AND MITIGATION MEASURES

STAGES IN ABDEAS	COMMON ISSUES	MITIGATIONS
Accrual Entries Under ABDEAS	Details of Deductions made from Contractor's Bills like TDS, GST-TDS etc.	Cross Tally with TDS return , subsidiary records , Royalty deduction, contract agreement , last running bill
Revenue Collection cross tally	Tax Collections did not match with Receivable details (Vasooli Patrak).	Current demand and closing statements to cross check . Control account adjustment
Liabilities Provisions	Non-Availability of list of Outstanding Bills	Next period cash book / statements to cross check .
Fixed Asset Register	Non up-dation for years together	Opening FAR , up-dation based on capturing of transaction from preliminary records
Frequent transfers	Change in personnel brings a halt to the process	Concept of link officer need to be introduced from both ends.

PRACTICAL ISSUES AND MITIGATION MEASURES :

Capitalization of Assets

COMMON ISSUES	MITIGATIONS
Contractor's Bills were not finalized than how to capitalize the assets.	Formation of yard sticks and rules for capitalization of asset based on put to use .
Non-Availability of Information regarding Assets Transferred to ULB's without any Financial Transaction. For Instance, State Government Transfer Land to ULB.	Based on transfer letter and confirmation from the State Government .
Source of funds not known for old assets.	Based on Grant records / MRL .
Asset may be under PPP for example SHG operating SLRM, Smart Parking on ULB Land	Contribution from ULB need to be recognized in accounts .
Joint Venture with other Govt departments , Public Private Partnerships for Capex	

PRACTICAL ISSUES AND MITIGATION MEASURES : Preparation of Bank Reconciliation Statements

COMMON ISSUES	MITIGATIONS
Opening Difference in Bank Reconciliation Statement	Determination of cut off date . Old differences to be parked in a separate account and / or start with Bank Balances actually available .
Entries outstanding for more than 3 months	Reversal based on joint identification .
Amounts directly credited in Bank Accounts either any Grant or Interest and remain unreconciled.	Information from Bank , finding source and rectifications based on the same .
Non Availability of details of some Old Bank Accounts s- Some times there were some Bank Accounts recorded in Manual Cash Books showing some balance but no proper details were available.	
Unavailability of the Bank Statements in ULB	Meetings with ULB officials and Bank

PRACTICAL ISSUES AND MITIGATION MEASURES

STAGES IN ABDEAS	ISSUES FACED	MITIGATIONS
Transition to new technology	Non awareness of software , hardware	Training : class room as well as on site
Revenue Expenses	Timing of accrual	Work Order , agreement , contract , receipt of material / services
Other Revenue Income	Non availability of records for accrual : advertisement rights , lease rental	To get a system installed for the same
Revenue Income (Tax and User fees)	Non assessment of taxes , New properties not added to the system	
Approval of deliverables and getting fees for the work done	Most difficult task	Documentation , patience and persistence

A person wearing a blue suit jacket and a white shirt is holding a white rectangular sign with both hands. The sign has the word "QUESTIONS?" written on it in a bold, dark blue, sans-serif font. The background is a plain, light grey color.

QUESTIONS?



Thank
you!!