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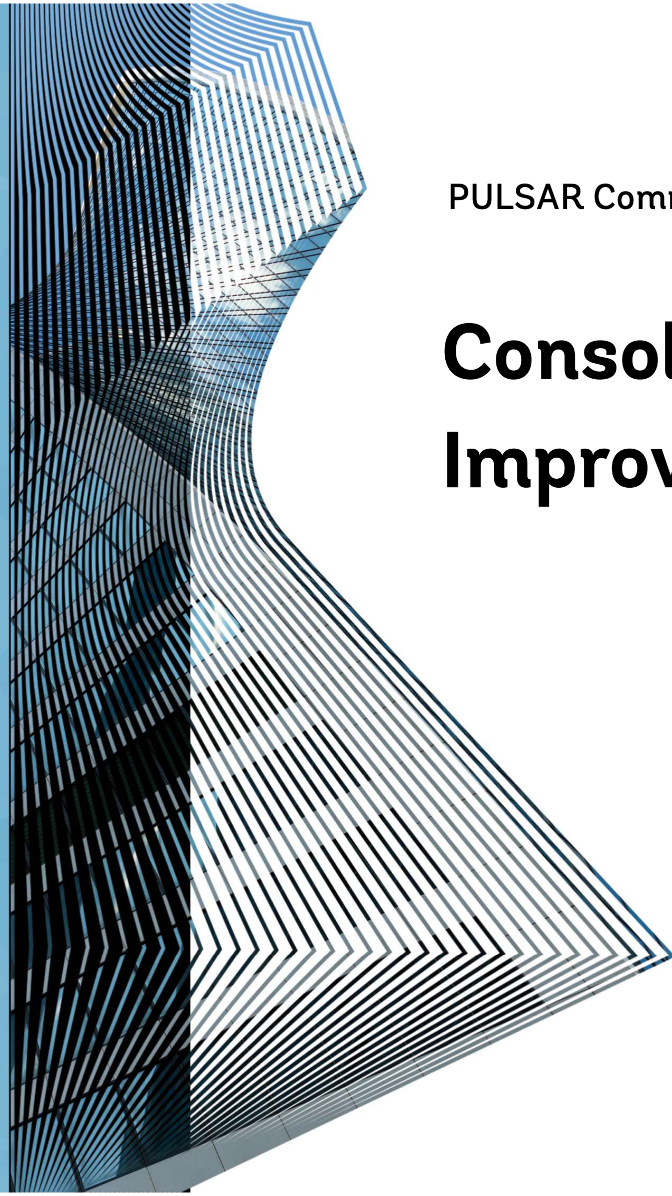

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Consolidation Practices to Improve Fiscal Reporting

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Outline

- Introduction
  - Understand the objectives of GFS
  - Understand what is meant by consolidation in GFS
- Scope of general government and public sector consolidation
- Practical Compilation and Consolidation Process
- Leverage accounting reforms to improve fiscal reporting

Introduction

To understand GFS consolidation practices – understand the objective of Government Finance Statistics (GFS)

- GFS is a set of macroeconomic statistics designed to support fiscal analysis and policymaking
- GFS is part of an integrated system of macroeconomic statistics
  - System of National Accounts is the core system – covering the domestic/national economy
  - Other specialized parts of macroeconomic statistics are
    - Government Finance Statistics (GFS)
    - External sector statistics (Balance of payments and International Investment Position)
    - Monetary and Financial Statistics
- GFS is suitable for fiscal policy analysis because it provides data that are: comprehensive, standardized, transparent, consistent, and comparable

Macroeconomic data for an economy need to be organized systematically

- » The economy needs to be organized/grouped to allow reporting and analysis
  - » Systematic and comparable
- » For macroeconomic statistics we need to:
  - » Firstly, delineate the domestic economy and the rest of the world
  - » Secondly, identify the various types of institutional units that operates in an economy
  - » Thirdly, groups the economy into sectors and subsectors
- » While differences exist between statistics and financial accounting – these can often be managed by policy and disclosure choices

Consolidation in GFS

- Consolidation is presenting statistics for a set of institutional units (or entities) as if they constitute a single unit
  - **Aggregate** of all stocks and flows – (line-by-line consolidation)
  - **Eliminate** in principle all stocks and flows that represent relationships among the units or entities consolidated (eliminate double-count)
  - Examples of stocks and examples of flows
    - Bonds/loans, grants/transfers, interest, etc.
- Include **intrasectoral** and **intersectoral** consolidation
  - Example, all ministries and all local governments
- Financial accounts limit consolidation to controlled entities while GFS also consolidate sectors of the economy

Scope of the General Government and Public Sector

Concept of Residence is used to delineate the domestic economy from the rest of the world

- The **residence** of each institutional unit is the economic territory with which it has the strongest connection
  - **Economic territory** is the broadest geographical area or jurisdiction for which statistics are compiled
    - Include territorial enclaves such as embassies, consulates, military bases, scientific stations, aid agencies , etc. with diplomatic status
  - **Strongest connection** means that the center of predominant economic interest is within that economic territory
- **Nonresidents** are part of the **rest of the world**
- In practice this delineation usually does not make a big difference in consolidation practices – Special purpose vehicles may be the exception

Identification of Institutional units

» An **institutional unit** is an economic entity that is capable, in its own right, of owning asset, incurring liabilities, and engaging in economic activities and in transactions with other entities

» An institutional unit has some important features

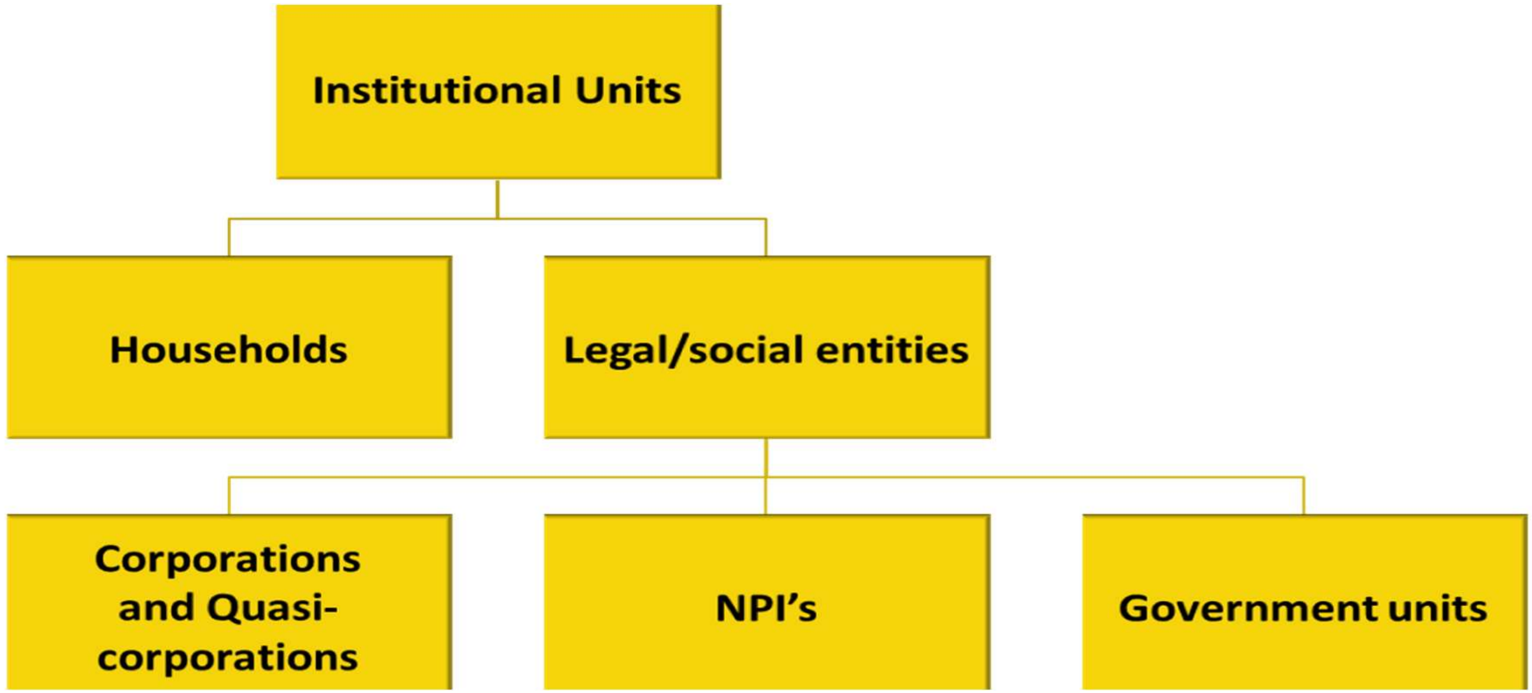
  » Ability to own assets – it is able to exchange these in transactions with other units

  » Able to make economic decisions and engage in economic activity for which itself is held responsible and accountable by law

  » Ability to incur liabilities on its own behalf, take on other obligations or future commitments and to enter into contracts

  » A complete set of accounts exist for institutional units, or it is possible/meaningful to compile a complete set of accounts, if required

Types of institutional units



Cannot always infer status of an institutional unit from its name - must examine its objectives and functions – example Infrastructure Corporation/Roads Company

In practice some individual reporting entities in financial reporting context may not qualify to be an institutional unit in statistics – example Contingency Reserve Fund

Institutional units relevant for public sector reporting

- **Government units** are unique kinds of legal entities established by political processes that have legislative, judicial, or executive authority over other institutional units within a given area
  - Principal functions of government units
    - Responsible for provision of goods and services to community or individual households primarily on a nonmarket basis
    - Redistribute income and wealth by means of transfers
    - Engage primarily in nonmarket production
    - Finance their activities primarily out of taxation or other compulsory transfers

- **Corporations** are defined as entities that are capable of generating a profit or other financial gain for their owners, are recognized by law as separate legal entities from their owners, and are set up for purposes of engaging in market production
  - Not its legal status, but notion of being a market producer determines its classification
  - Produce goods and services at economically significant prices

Delineating general government and public corporations

- **Public Sector** consist of all resident institutional units controlled directly, or indirectly, by resident government units, that is all units of general government sector and resident public corporations
- **Market** or **nonmarket production** determine whether they are part of the general government sector or public corporations sector
  - A **market producer** is an institutional unit that provides all or most of its output at prices that are economically significant
  - A **nonmarket producer** provides all or most of its output to others for free or at prices that are not economically significant
  - **Economically significant prices** are prices that
    - Have significant effect on the amounts that producers are willing to supply and on the amounts that purchasers wish to buy
    - Sales usually covers the majority of the producer's costs and consumers are free to choose
    - However, public control of prices complicates determination of economically significant prices
    - While no prescriptive numerical relationship exist – at least expect to cover the majority of production costs over a sustained period of time

Some special public sector units to be classified

- » Artificial subsidiaries – passive holders of assets and liabilities
  - » Not considered a separate institutional unit
- » Quasi-corporations – not incorporated or otherwise legally constituted but function as if they are a corporation
  - » If sufficient information is available to treat them as if they were a separate institutional unit – classify as a corporation in the data
- » Market establishments could exist in government units
  - » If they satisfy the criteria of a separate institutional unit, classify them as a quasi-corporation
  - » Otherwise, remain in general government

Institutional units are then classified into five mutually exclusive institutional sectors

General government sector	Nonfinancial corporations	Financial corporations	Households	NPISHs
Central govt State govts Local govts SSFs*	Public corporations	Public corporations	Private	Private
	Private corporations	Private corporations		

Subsectors could be identified and could be further presented as either budgetary or extra-budgetary units

Public corporations are all the market producers under control of a government unit or another public corporations – **control is not determined by ownership but rather a range of indicators of control**

Indicators of control to determine if a corporation is controlled by a government unit or an other public corporation

- Eight indicators of control should be considered
  - Ownership of the majority of the voting rights
  - Control of the board or other governing body
  - Control of the appointment and removal of key personnel
  - Control of key committees of the entity
  - Golden shares and options
  - Regulation and control
  - Control by a dominant public sector customer or group of public sector customers
  - Control attached to borrowing from the government
- Single indicator could be sufficient, otherwise a number of separate indicators may collectively indicate control

Subsectors of the public sector

- Public Sector
  - General government sector
    - Central government
    - State (or provincial or regional) government
    - Local governments
    - Social security funds presented either as
      - A separate subsector of the general government
      - According to level of government that organizes and manages them
  - Public Corporations sector
    - Non-Financial Public Corporations
    - Financial Public Corporations
      - Central Bank
      - Public deposit taking corporations other than the central bank
      - Other public financial corporations
- **Only general government and public sector data are internationally comparable**

Practical Compilation and Consolidation Process

Collection of source data

- Integrated financial management systems (IFMS) with a unified Chart of Accounts (CoA) greatly facilitated compilation
  - Unified CoA should
    - Have standardized categories of assets, liabilities, revenue and expense and be harmonized with budgetary, accounting and statistical reporting needs
    - Unified CoA could identify counterpart transactions in two manners
      - In the structure of the accounts, example “grants/transfers to local governments”
      - In identifying the counterpart in the accounting system using the administrative classifications in the CoA
- Standardized reports to be submitted to the compilers – using source data systems, reports are being compiled by reporting entities from their source data
- Financial statements are submitted as source data and then bridged to GFS during compilation process
- Often a hybrid approach using various of these processes are needed

Using data from the accounting system of government usually significantly improve the quality of source data

Adjustments to source data

» Adjustments for differences in accounting policies

» Adjustments for differences in the reporting date or basis of reporting

» Adjustments for methodological differences

Some adjustments needed before consolidation process starts, other adjustments incorporated after aggregation was done

Check consistency of data throughout the compilation process

Analyze major relationships and identify major items to be consolidated
"Consolidation is an imperfect science" (GFSM 1986)

» Grants/transfers (current and capital)

» Interest

» Taxes

» Purchases/sales of goods and services

» Acquisition and disposal of nonfinancial assets

» Loans

» Debt securities

» Equity

» Other accounts receivable/payable

Consolidation tips and tricks

» Focus on significant amounts that will impact fiscal analysis

» Some rules of thumb are commonly used in statistical consolidation

- » Consolidation is a symmetric process – balancing items do not change
  - ❖ Can therefore use consolidated or unconsolidated data if only interested in core balancing items to measure "overall impact of government"
  - ❖ Consolidation only impacts the magnitude of aggregates
- » Convincing evidence from one institution could be imputed to the counterpart
- » For financial assets and liabilities creditor information are usually accurate
- » Discrepancies between units can originate from various reasons – resolving these should be first option – second option is to decide which parties' information seem to be the more reliable
- » Generally higher level of government information is more reliable than lower levels of government

Leverage Accounting Reforms to Improve Fiscal Reporting

Some presentational choices in accounting reforms could support improved fiscal reporting

» Recent country experiences

- » Fiscal data for surveillance could be deemed of poor quality
- » Accounting reforms has led reforms such as Quarterly and Annual financial statements for the whole of government being compiled/audited and published – but these are not used in surveillance/analysis
- » Some crucial mistakes were made in accounting policies selected and presentation

MDAs Budget Execution Report

- MDAs ≠ MDAs
- Local government consolidated with corporations
- Public Corporations coverage incomplete
- Asymmetric consolidation

Financial Statements

MDAs Local Gov Public Corp Whole of gov.

Lessons to be learned

- Carefully consider accounting policy selections
- Phased consolidation could generate data first at general government level, and then at public sector level using individual financial accounts
- Label results of consolidation correctly
- Disclose the scope and stance of consolidated accounts transparently
- Disclose any deficiencies in scope of the data
- Consistency checks need to be performed rigorously
  - Consistent classifications need to be applied
  - Symmetrical consolidation practices should be adhered to

Thank you very much for your attention

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