THE ROLE OF FINANCIAL STANDARDS IN HUNGARIAN PUBLIC SECTOR ACCOUNTING

József SIMON,
Eötvös József College, Baja, Hungary

Henrietta ANDRÁS,
The Under Transdanubian Directorate of Water Management, Hungary

ABSTRACT

Improving the quality of Public Finance and Government has become ever so important recently. All European countries set high expectation regarding the efficient use of public monies. The right financial information system is a prerequisite of value for money public financing. The European Union has established rigorous accounting requirements for its members' public finance. As a result major changes had to be introduced into the representative practice of budgeting. Union members had to reshape their national accounts system parallel to their public finance accounting. This process has been lead by Western European countries.

Hungary must follow their examples in public accounting. Since the economic and social transition took place in Hungary, a series of public accounting reforms has taken place. This study focuses on introducing such reforms specifically in regard to public financing and accountability. After discussing the key characteristic of the reforms, we conclude that Hungary is lagging behind in regulating public accounting when compared to other Central Eastern European countries. This shortfall is mainly due to the instability of the transition period. Most efforts were directed towards economic progress and thus information generation lacked. This special case will be outlined through the practice of special accounting standards developed for public financing (IPSAS). Such practice is particularly prevalent in Anglo-Saxon countries. However, globalisation and supra/national cooperation led to the adoption of accounting standards in other countries. In Central Eastern Europe, the level of using accounting standards varies from country to country. Certain countries fully support the adoption of accounting standards while others approach them with caution.

Our study also aims to outline the managerial approach in the Hungarian Public Sector closely related to these standards. This new practice will be discussed in the specialist area of water management. We shall investigate how much of business accounting standards and practice has been introduced to the public sphere. Our research will also entail the studying the usefulness of accounting information.

Key words: public sector, public accounting, reform of accounting system, IPSAS standards

JEL code: H83

1. Introduction – Public Sphere Information System

Information system is the complementary networks of components among which new informations is communicated. Informations are necessary not only in the management of private entities but also of public institutions. In modern market economies, the public sphere has historically evolved to serve all state functions. The public sphere is a sub-sector of the economy which produces and manages collective goods Public entities can operate following public budgetary, non-profit or business regulations (Sivák-Vigvári, 2012).

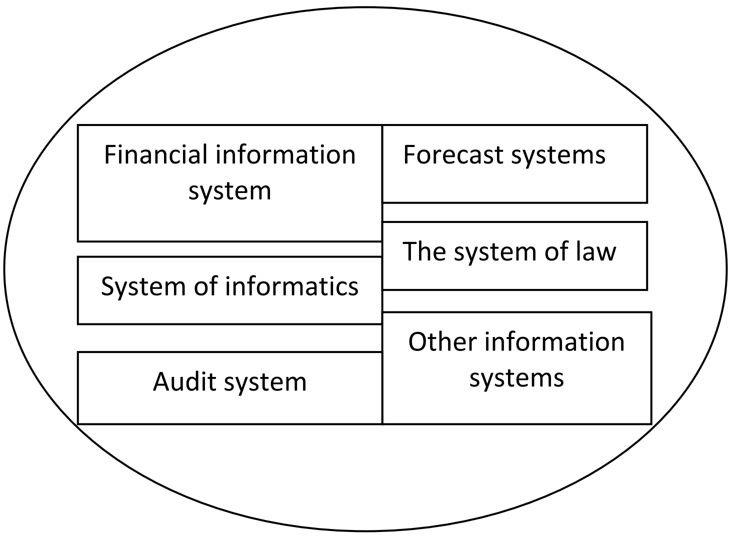
During the last few decades, the public sphere's significance has increased. The public sector has become an integral part of the economy. The sector's main objective is to fulfil its obligations to the public.

In the public sector, many sub-sectors can be distinguished according to their character or operational mechanism. Key differences in the operational objectives and methods; financial techniques; or the informations systems of the sub-sectors can be underlined. As such then information system of the public sector has a widely applicable definition.

The Public Sector Information System involves all components producing information necessary for the operations of the Public Sector. The Public Sector Information System forms a sub-system of the Public Sector Information System. The State Finance Information System forms part of the Public Sector Information System. Just like all other systems, the complex State Finance Information System can also be divided into smaller sub-systems. *Figure 1* describes the key sub-sections of the State Finance Information System.

Financial information play vital role in the State Finance Information System. In addition, public finance accounting is another key element in the information system.

Figure 1: State Finance Information System



Source: own editing

The State Finance Information System's environment

The typical function of the public sector is to provide public goods for society. Public sector institutions primarily carry out non-market activities. However, these institutions often have functions where efficient management and cost-benefits analysis play vital roles. However, a profit-oriented approach cannot always apply to public functions as public benefits are hard to account for or measure in monetary terms (Csermák, 2004.).

In addition, unlike in the private sector, public entities do not have a clearly defined managerial objective such as profit realisation or asset accumulation. Objectives for the public sector are often defined as functions open to individual interpretations. Often such functions are interpreted from a political angle as opposed to purely economic ones. As public management objectives are difficult to quantify, measuring objectives leads to various problems.

Subjectivity plays part not only in measuring objectives but also in defining them. In some areas of public management, profit oriented activities are mixed with activities aiming to produce public goods. Most typical of such behaviour are public utility companies (Horváth M., 2002).

Public management can be viewed as managing a large factory where public goods and services are produced (Kassó, 2006). Managing the production requires the co-ordination of a vast array of activities which consequently involves large number of agents, often working in different geographical units.

State financing also differs significantly from the financing of private enterprises. Financing public functions involves both internal and external resources. External resources arrive mainly from the central government budget, while internal resources include local tax revenues and asset utilisation. Additionally, some activities are financed from both public and private monies. To make matters more complex, the financing of certain tasks are realised through a multi-level decision making process. Three main levels of decision making can be distinguished: central government budget, local government and specialist agencies.

The effectiveness of operations is also measured in a significantly different manner in the private and public sectors. Public goods and services primarily cannot be replaced with other goods and services, even their non-consumption it limited. As a result, society's freedom of controlling or even influencing the quality of public good and services is highly limited (Vigvári, 2005).

The above observations lead to another characteristic of management, the different definitions of bankruptcy. If a private enterprise cannot cover its costs it can go bankrupt. On the other hand, as a consequence of soft budgetary limits, public entities can be, and are often, bailed out i.e. saved through additional central budgetary funds (Kornai-Maskin-Gérard, 2004.).

Planning plays a special role in managing public entities. The most important product of planning is the budget, providing a frame for the operations of any particular year. The budget details the objectives, the necessary resources, the operations and the timing of operations as well as the units responsibly for the operations (Csermák, 2004.).

The basic unit of planning in the public sector is the institution itself as opposed to the product or a service. In addition, the timescale of planning is generally shorter in the public sector than in the private sphere. Short- and medium-term planning is a special characteristic of local government systems.

There are significant differences in public and private management regarding ownership. Assets are owned by the State or local governments. Sometimes fulfilling a public function involves the temporary transfer of ownership of public assets. As the owner and manager of a public asset are different agents with different motivations asset management causes problems.

Measuring productivity of public entities poses various problems as a result of objectives not being clearly defined and difficulties with assessing effectiveness. Performance indicators commonly used in the private sphere have limitations in the public sector.

Following the above discussion, we can conclude that public financing and management requires a complex and multi-dimensional information system.

2. Public Sector Accounting

Three major periods can be distinguished in the history of modern public sector accounting in Hungary. During the first period, the 1990s, the same accounting techniques were applied as in the previous socialist, direct economy era. Unfortunately, the accounting practice of Western European countries could not find fertile soil to take root in Hungary during that period. On the other hand, during that time a frenzied legislation took place in general but also in relation to a public finance system. Due to the shortage of time and urgency of the matter, consultation with all parties concerned and detailed impact assessment studies regarding new legislation were often lacking.

The second period, from 2000 till 2013, can be characterised by providing a certain degree of stability in the system. Early legislation was reviewed and amended as well as new methodology was introduced.

Key legislation in the period included Act C of 2000 on Accounting and Government Order No. 249/2000. (XII. 24.), on the specifics of the annual reporting and bookkeeping tasks of state budgetary organizations. The latter government order adopts the regulations of the Accounting Act for government financed institutions. In the following part of our study we shall outline the main characteristics of this period.

The key guide in public sector accounting at this time was the traditional cash flow approach. In our view, most problems and shortcomings of public financing relates to adoption of this approach. This traditional viewpoint results in a misleading image of healthy public finances. Under the surface, however, major tensions could prevail.

The objective of the accounting and recording system in this period was to register cash flow items at completion. The adoption of pure cash flow approach in public sector financing leads to negative consequences for several reasons. In other words, the cash flow methodology presents a significant information risk for all areas of management.

Furthermore, the applied methodology is not able to reduce such risks. During this accounting period, research is limited to revenues, outgoings and related indices. Such data can only show a distorted picture of finance management.

Due to the cash flow management, Hungarian government institutions cannot budget accurately. Without accurate budgeting, tasks cannot be fulfilled properly. Hence, the government cannot fulfil its ownership and investing obligations as the current methodology does not allow for the full evaluation of its operations.

Accounting and compulsory data service only serves cash flow based planning, public monies accounting and related internal and external auditing (Kassó, 2006). However, the feedback function cannot work properly due to imprecise and liberal of administration practice.

Determining the real value of their financial capacity would be vital for budgetary institutions. However, the management of public finances is hindered in performing proper financial analysis. Data necessary for analysis cannot be generated. The balance sheet, cash flow and balance account fulfilling the functions of a profit and loss statement, as well as revenue and outgoings based budgets generate unreliable information. Furthermore, the balance sheet is incapable of supporting any asset related decision-making.

In order to secure the quality and financing of managing public assets and tasks, it is vital to fully understand the value and structure of accounts payable. Sustainable management cannot be maintained by inadequate handling of accounts payable and liabilities. Two types of accounts payable are particularly significant, one is suppliers' accounts and the other is long-term liabilities (loans and bonds). Both types of liabilities present degrees of indebtedness. Current account deficit and government indebtedness have far reaching consequences through the financial markets and the EU.

The balance of the public sector budget is also deceptive. The method of achieving a balanced budget is equally important. Analysing the internal coherence of budgetary and management decisions is a must.

Managing depreciation needs special attention. Depreciation is compulsory following set depreciation formulas and methodology. However, the accounted depreciation has no consequence or bearing for the management. The regulations ignore the most vital part of depreciation i.e. which resources are to be used for replacing the amortised asset. Furthermore, this fact cannot be presented in the registration and accounting system resulting mainly from the imprecisions of the asset records and the methods of accounting for changes in the equity account. In other words, the value of depreciation is corrected by short-term liabilities and new asset acquisition. All in all, accounting aims to maintain the overall value of assets. As non-asset items get incorporated in the calculations and the analysis ignores any changes in the asset needs of the entity, the accounting picture becomes hazed.

For politicians a cash flow based budgetary planning seems advantageous, as it clearly shows which institutions receive what amounts and at the end of the financial year all monies spent are accounted for. For the decision-makers it might seem that all objectives were fulfilled. However, this cash flow based financing mechanisms only answers the question of how much was spent by a certain institution in a certain year and ignores any concerns of efficiency and effectiveness.

An institution based financing practice will also disregard cost and benefit analysis. Rational management assumes the cost assessment of tasks and cost comparison of alternatives. However, budgetary institutions do not possess reliable information regarding actual costs.

Another issue regarding the management of public entities is the quality of asset management. This issue, however, meets with disinterest. Neither the account based not the market based valuation provides reliable information. Already the exact account of assets poses a problem as depreciation is not offset with money flow. As a result, the effectiveness of asset management cannot be correctly assessed.

The institution based approach does not follow the accounting concept as laid out in legislation, since in the institutions' budgets costs are not accounted and accumulated for each tasks separately. Most institutions carry out multiple tasks, thus their aggregate accounting makes the situation even more complicated.

Even the separation of tasks might not necessarily mean an obvious solution. Unfortunately, legislation regarding the operation of public entities allows for various tasks to mix and overlap and no methodology of separating such tasks exist.

Thus, the validity of information in the final accounts of public entities is highly questionable. On one hand, revenue items are presented without following a centrally regulated itemised financial reporting standard. On the other hand, the itemised financial statements only contain half of all outgoings. Furthermore, financial audit is only required for 30 percent of the itemised accounts (Kassó, 2006.).

Another problem concerning accounts is that information is aggregated ta institutional level.

The above mentioned characteristics of the accounting, registration and budgetary system negatively influence the adoption of ESA95 methodology in public sector accounting. The new approach set significant methodological challenges for the government statistical system where all problems of the itemised accounting and registration system accumulate.

Major reforms and changes

The above discussed shortcomings hinder the development of a responsible and efficient public budgetary management. Despite the fact that concerned institutions (public entities, controlling and auditing agents, specialist consulting organisations) constantly emphasise the problems, the situation has shown little improvement. However, the underlying causes for this lack of change must be seen in a wider context. In conclusion, the conditions for change were not present.

In the meantime, the European Union has expected an ever increasing rigour in the public accounting system. Reports on Hungarian public accounting system emphasise the need for more transparency and responsible budgetary management. Political circles perceive the criticism in relation to the actual and maximum levels of indebtedness and budget deficit. The EU provided the final push for the Hungarian Government to institute changes. It became apparent that only a newly reformed public sector accounting system could meet the EU's expectations.

This reform process led to the adoption of Government Order No. 74/2013 concerning public sector accounting. Budgetary institutions must continue to adhere to the Act on Accounting, thought the new order introduced amendments to the act as too.

This new order set very impressive objectives. Among others, it aims to fulfil the increasing informations needs of public entity management, a stronger cohesion with the Accounting Act, more emphasis on the adoption of accounting principles for budgetary institutions.

The new legislation allows only a year of transition - without any option for extension - for budgetary institutions to adopt new accounting systems.

The major reform lies in the separation of budgetary and financial accounting. Planning, accounting and reporting in budgetary accounting will continue to be based on cash flow. However, methodology for financial accounting sets out to represent assets in a unified structure and increase the reliability and validity of financial statements regarding assets. Furthermore, new legislations call for analysis on the effectiveness and efficiency of managing public entities and functions. These changes are both necessary and advantageous in terms of providing a sound framework or public financing.

Additional reforms introduced by the new legislation derive from the above mentioned key changes. Out of the additional changes the compilation of the Classified Balance Sheet stands out due to its significance. 31 December 2013 being the turning date, all accounts of the general ledger, prepared using previous accounting and registration logic, must be closed and amended with addition items as required by the new methodology. The compilation of the classified balance sheet poses a series of new accounting tasks including: the transfer of appropriate items, presentation and valuation of all accounts payable and liabilities, sorting of external moneys, or the transfer of advance payments.

Public sector accounting executes a threefold registration function by recording the budgets of and the completion of revenues and outgoings as well as recording assets and liabilities. The government order introduced a unified chart of accounts and order of headings. Account classes of the general ledger have gained more significance, particularly Class 0, which covers all registration accounts. Assets and liabilities form integral parts of the accounting registration now. The fundamental proviso for completing any assets and liabilities is the accurate recording of assets and liabilities against which completion can be made.

Concerning completed items, the most important new element is the economic and functional recording of completion. Although this element was expected in the previous regime, either the economic or the functional recording was thwarted as a result of the cash flow approach and other technical solutions.

The new government order has also altered the structure of the balance sheet e.g. abolishing the activated value of experimental development. Although abandoning this item made sense, it might lead to information loss which could further result in certain institutions (with research functions) establishing a separate registration of such activities (incl. costs and revenues etc.).Concerning assets and liabilities, the accrual concept has been adopted. From now on, assets and liabilities of a certain year will be separated from those due in following years.

Significant changes have been instigated regarding the asset valuation. Salvage values are now limited to 25 million HUF. In addition, government financed institutions may use centrally determined accounting formulas for the valuation of fixed assets.

The content of financial reporting in the government sector has also altered. The yearly budgetary report can be complied following two methodology, one is cash flow accounting while the other is accrual account. The report can be complied following 4 different classifications: economic, functional and administrative classifications as well as classification according to government functions. The profit and loss statement has gained significance in the new budgetary reporting system. In addition, new reports must be prepared detailing costs and recovered costs in order to harmonise finances via meeting revenues earmarked for specific tasks with direct, own costs.

Overall, recent reforms of public sector accounting signify improvement on previous tradition. Although not enough time has passed since the adoption of the new legislation to provide enough ground for deep analysis, a few notes can be made using reference material and practical experience.

The transition to a new accounting practice is made more difficult for a number of institutions as the new legislation did not allow sufficient time for it adoption. Generally speaking, government financed institutions are not adequately prepared for a speedy transition. The previously practiced accounting logic cannot be altered in such a short period.

Despite the validity of accrual accounting, public institutions are now burdened with a dual accounting system resulting heavier workload and fears towards any changes.

Compliance with legislation requires that all necessary personnel and material provisions are available. Unfortunately, there is a shortage of accountants specialising in public sector financing. Furthermore, training practice in the public sector does not help the situation. Only six month after the adoption of legislation started public institutions providing specialist training for their employees, which was far too close to the start of preparing the classified balance sheet. On the material side of the problem, the concerned institutions could not get hold of the updated version of the Resources Programme on time for the work to commence.

The new reforms in the registration system do not necessarily lead to growing information supply and increased reliability. Compatibility among the different classifications runs into various problems. Additionally, the presentation of the profit and loss statement in the determined structure could be based on inaccurate and vague information.

The reforms have been vital even though they have dubious concrete results. Errors and shortcoming emerging in the transition period must be corrected.

3. Public sector accounting in an international comparison

In the followings we shall discuss the reforms of public sector accounting in Hungary in an international context i.e.: How do the above mentioned reforms relate to progress in the field on an international level? The discussion will follow the development of accounting principles.

The way from a traditional to a reformed accounting system could be discussed through the operational principles of accounting. Table 1 lists the general principles of accounting information systems.

Table 1. Operational principles of the information system

1. Empowerment	7. Foresight
2. Transparency	8. Sustainability
3. Openness	9. Integrity
4. Controllability	10. Sufficient detail
5. Financially sound	11. Validity
6. Performance	

Source: the Law of Accounting

The principle of empowerment or delegation implies that all responsibility for budgetary decisions should lie with the delegated agent. This principle was already a corner stone of the traditional budgetary policy.

Full transparency must be achieved in the public finance legislation as well as in the budgetary processes of government institution. The flow of public money should be easily monitored. This principle has gained sufficient significance as expectations towards an efficient management of deficient public moneys is increasing.

Open access to information on public finances are encouraged as a means to strengthen the community element of government policy and to present the key characteristics of the economy to the public. Social criticism concerning public sector finance also encouraged the government to improve transparency.

Increased controllability not only involves controls on adherence to regulations (lawfulness) but also performance and value for money audits evaluating the rationality and efficiency of managing government assets and finances.

Modern public sector finance policy and valid budgetary decisions must be built on financially sound ground which is one of the key corner stones of public management. Performance, sustainability and foresight are all new financing principles alien to the old, traditional approach.

Integrity implies that all elements of public sector financing and management must be fully scrutinised. Assets and liabilities of government institutions financed from non-government sources receive special attention just like assets and liabilities impacting public budgeting and the management of government assets. The principle of sufficient detail supplements integrity in as far as it implies the classifications of public finance information into sub-categories of sufficient detail and content.

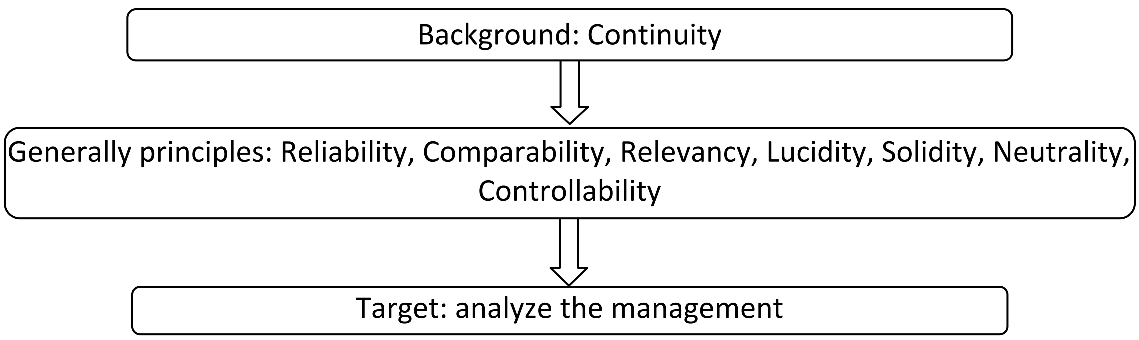
The principle of validity concerns on one hand the validity of information provided and also the increased content of public sector financing information. A valid picture of public sector finance management cannot be formed without performance assessment.

A change in the content of the information system's principles did affect the principles of public sector accounting. The introduction of public sector accounting standards (IPSAS) presents a good example.

IPSAS aim to prepare a unified financial statement system for public sector financing and management in order to provide sufficient and accurate information for all interested parties. The standards cover all area of accounting. Separate standards apply to accounting, evaluation, reporting and accessibility, publicity. The applicability of standards is not reduced to a single level of government but is relevant to all levels, central as well as municipal.

The majority of IPSAS were adapted from IAS, standards developed for the private sector. Hence most of the accounting principles of IPSAS come from IAS which can be divided into general principles and supplementary principles (See Figure 2).

Figure 2: IPSAS Principles



Source: original work based on Varga, 2009.

Figure 2 shows that the international accounting standard ignores the principle of providing a reliable and valid picture, which formed an elementary part of Hungarian accounting legislation.

According to the International Account Standard Board (IASB), the report will provide a reliable and valid picture of operations if during the preparation of the accounts all standards and other quality assurances are met. Quality assurances include reliability, comparability, relevance and clarity. US GAAP also highlights the significance of these standards with the only proviso that the understanding is the liability of the users. The operational principles of public sector financing and management are also relevant for public sector accounting.

General observations on international public sector accounting

Inevitably there is a significant variation among the accounting practices of European countries since each country has its own economic, political, social environment.

Each European country has taken steps towards accrual accounting. Parallel, the adoption of relevant accounting techniques has also started. The driving force behind accrual accounting is an ever increasing demand for economic related information. Besides budgetary control, performance assessment has also gained impetus.

There are many motives behind the adoption of accrual accounting including the reforming of public sector finance management, decentralisation and the changing attitude of managers.

On the other, there are issues hindering the smooth application of the new methodology such as lack of expertise, attachment to traditional budgetary techniques, opposition of concerned parties, insufficient IT support, non-compatibility with various element of government finance.

Countries that could overcome these obstacles made significantly more progress in accrual accounting. How fast and to what extent a country managed to transform its budgetary process also contributed to its overall success in accrual accounting compared to other European countries.

Different strategies have been developed in the adoption of accrual accounting. Although the duration of the transition period varies from country to country, it averaged 3 years.

How far a country relies on accounting standards shows a great diversity in Europe. Mostly Anglo-Saxon and a number of other Western European countries adopted full heartedly accounting standards. Other countries ignore these standards in their accounting legislation. However, all countries encourage the use of the IPSAS system to some extent.

Hungary should consider the international practice of public sector accounting. An analysis of the initial problems associated with the new accounting methodology emphasises a valid risk that the newly adopted legislation might not achieve the expected results. There is however the opportunity to intervene in the first stage of adoption.

4. Public accounting in the practice

The study has further target to present the spread of the management methods closely related to the standards in the Hungarian public sector. On behalf of this a typical public service, the water management will be presented.

Water management in accounting perspective

We would like to present the significance of the recent changes in the public accounting system through two main basic functions of the water management: the flood and inland waters protection and the management of state's property using by the directorates. This paper intends to reveal, how current changes in the legal regulation can influence the assessment of the quality of addressed basic functions on the local and national level as well. The reform may take effects many aspects of the operation, but the scope of this study is narrower we cannot introduce all changes. Therefore we will focus on the four main areas, all of which concern the above mentioned activities. These are the following:

- the opportunities inherent in the consolidation for the aim of providing the expected information of inhabitants and decision makers;
- the possibilities of measurement of performance and economic results according to the so-called statement about cost and returned cost;
- the effect of the reliable calculated depreciation on the efficiency, furthermore its influence on resource allocation in the scope of general functions and business activities;
- the impact of changes in the evaluation methods on the assessment of the real financial position.

In Hungary a significant improvement can be experienced regarding the consolidation method, but rules are still limited within the public area. (Ernst & Young, 2012) The government's right to set the rules of consolidation by decree is involved in the Act on CXCV 2011 on Public Finance (hereinafter: Public Finance Act), what has been entered into force on 31st of December in 2011. The government decree including the rules of consolidation was issued in January 2013 and it came into effect from 1st of January in 2014. This timelag presents ell the necessity of time and adequate preparation of the changes. The Hungarian State Treasury (hereinafter: Treasury) is due to collect and provide sufficient information about the budget estimates and budget implementation. Actually the Treasury has been aggregating the information since 2000 in the scope of some subsectors of the state budget. According to the Government Decree 4/2013 (I.11.) on Specialities of the General Government Organizations Reporting and Public Accounting Rules the Treasury is required to compile the consolidated financial statement on the level of each subsector and for the completely state budget as well. The aggregation applies solely to some particular information, what are the following: balance sheet, profit and loss account, and statement about the implementation of budget. Despite of its importance the another parts of financial statement have not been consolidated.

In Hungary the development of the consolidation method works continuously. It consists of the following steps:

1. In the year of 2000 the consolidation was relevant solely to the national Social Security (SS) subsector and SS budgetary institutions. (According to Government Decree 249/2000. (XII.24.) on Specialities of the General Government Organizations Reporting and Public Accounting Rules) (hereinafter: Government Decree 249/2000. (XII.24.)) (Ernst & Young, 2012)

2. From 2009 the consolidation was relevant to a wider scope, which involved the central budgetary and governmental subsectors, furthermore SS and other funds. The aggregation had to cover the complete budget estimates and implementations on the basis of Government Decree 292/2009. (XII.19.))

3. The withdrawal period was from 1st of January in 2012 until 31st of December in 2013 there was no declaration regarding consolidation.

4. From 1st of January in 2014 there is completely consolidation concerning both subsectors and state budget as well. The legal changes entering into force from 1st of January in 2014 are relevant to the whole public sector, and heir target is the realization of implementing unified public accounting policy in conformity with the 6th of IPSAS standard. (IPSAS Handbook, 2012)

The importance of the consolidation and transparence of the financial statements in the scope of water management resides in the calculation and national aggregation of the cost of the flood and inland waters protection. In the current practice the expenses incurring due to the protection are compensated ex-post by the state. This method requires wide range of data collections and supplying and owing to the cash flow approach and it is not suitable to identify the real costs. According to the relevant regulation the account for the cost of protection against water affairs shall be measured with the first cost (cost price) method in harmony with the law of accounting. Nevertheless there is a discrepancy in reference to cost concept defined by the law of accounting law and public accounting. It is a relevant problem, as historical cost is involved in the first cost (cost price). The regulation of accounting rules of the cost related to the water affairs use the terms cost" and "expenses" as synonyms for each other. This reflects well, that according to cash flow approach these costs are not distinguishable. Thanks to the reform the solution of the above mentioned anomaly cannot be delayed in the future. And also it is very important to make clear whether the financing of the expenditures or the compensation of effectively incurring costs is preferable. In the last case the items without cash-flow will be compensated as well. The accrual accounting can contribute to useful information supplement in the case of ex-post funding as well. Hereby the difference between the compensated and real consumption of the resources can be calculated, which information is necessary and impressive information for local and other concerned people on upper level too.

From an economic point of view the accurate estimation of the cost of flood and inland waters protection has significant importance especially because of the soft budget constraint referring to this. Owing to this conception the expenditure target can be exceeded on the basis of the governmental approval decisions. This shall entail the setting priorities in the scope of both financing and protection consistently. The flavour of flood control is that the prompt reactions and decisions are crucial, so specific stand-by equipments and inventories are essential. The SWOT analysis has been accepted in the early 2014 as a suitable method for the risk management in the scope of flood control. The difficulties of the financial planning in this area are well-presented by the fact, that the appropriation reserved for disaster recovery in the state budget has not changed since 2011. The cost incurring due to the protection are financed ex-post by the state, what involve the risk of the existence of sunk costs. The way to the recognition of the reliable cost leads over the solving of the anomalies related to the accounting. The information about effective costs contribute to a more accurate budget planning, thus to the economic and careful management. In our point of view in wider context the next step should be the consolidation of the statement about costs and returned costs. The measurement of the substantive costs for each general function of the state is the basis of proper and established resource-allocation. In the process of consolidation should pay distinguished attention to consequential corrections.

The statement about costs and returned costs is also part of the financial statement and the necessary information is provided by cash flow approach. It has the purpose to assess the results of the addressed functions, and according to this it uses the line items of the profit and loss account regarding both benefits and expenditures. The applied calculation method is very similar to the direct costing concept used in the business sector. In the public sector nowadays there is a very strong intention to realize the new business methods reflecting the compliance of the requirement of 3E. Essentially this derivation takes into account all of incurring cost and income concerning each task. As a result of that the cost and income per cost drivers and the balance of a particular activity can be identified. In the public sector similarly to the business sector the restriction of the concept has to be taken into account, namely the aggregation is limited. The activities classification according to the function classification structure and the matched bookkeeping supports he function focused approach. However there are some dysfunctions in the function classification structure, which prevents the clear sight and reliable information furnishing. The main groups of current system compress too many activities in one function compared to the complexity of those. Hereby the dimensions of this structure do not meet with the demand on information of the local decision makers, the inhabitants, and the government. The current concept is not able to identify the correct cost driver, since a particular function involves very different kind of activities, so that it cannot be featured by one index number correctly. The next station in the process of the development of the accrual based accounting should be the review of the function classification structure and adjust it to the required information. As the changes aim to improve accountability, furthermore transparency, efficiency and effectiveness in public administration, it is inconceivable without an appropriate framework of index numbers. This means also the basis of monitoring, which is one of the five interrelated components of the internal control.

One of the main characteristic of a water management directorate is that they operate with a very large amount of property, plant and equipment. These count about 90 to 95 percent of the balance sheet total. Accordingly the depreciation – what is actually potential cost – runs to high amount, so the preventive maintenance costs mean significant liability for the institutions. Owing to the straitened circumstances and reduced possibilities for innovations and renovations became the infrastructure increasingly outdated. The gross amount of the fully depreciated assets counts about 11 to 16 percent of the balance sheet total. Within this the proportion of the equipments and conveyances belonging to the indispensable precondition for the performance of tasks counts approximately 70 to 85 percent. Data express that the depreciation and so the commitment for the maintenance is necessary to be disclosed. Comparing these costs with the available financial resources the necessary incomings can be calculated, for which directorates need to raise funds by their own. At this point there some problems are arising associated with the calculation of price. As rates illustrate that the depreciation must play an important role in the operational cost, thus in the unite price of a particular activity. The knowledge about reasonable price of activities is crucial for appropriate resource allocation and tasks priority ranking, especially in the case of resource scarcity. However the institutions of public sector are non-profit oriented the expectations from shareholders (specifically the inhabitants and the European Union) for the adoption of market approach and business management methods will be more and more powerful. Actually the public entities are required to improve their assets utilization ratio in order to reduce the specific costs and enhance quality of the provided public services.

The business activities are not preferred in the public sector. The reasons are obvious: without measurability and accountability there is no confidence whether it is remunerative or not. The following risk surfaces: business activities may take resources out of general function, what leads to conflict of interest. The disallowance or limitation of business activities dispossesses budgetary institutions from the possibility of partially self-financing and encumber the performing their maintenance commitments. If the business management methods seem to be ideal and are required to adopt by public sector the government ought to promote it by responsible legal and control environment. At this point it is worth to turn back to the opportunities provided by the statement about costs and returned costs again. The depreciation is included in the cost of a costs driver, what could help to the budgetary institutions to include it in the unite price of a particular service or product. Hence the return of the amortization will floe to the entity, moreover the estimation and planning become more accurate. Through this statement the decisions can be supported and the results of the activities can be presented by accurate calculation, what means a feedback and control at the same time.

The changes do not cause effects on the depreciation rate, the accumulated depreciation and the remainder depreciation of the assets installed before 1st of January in 2014. On the basis of these the accounting reforms are applicable on the basis of the public entities own decision. The concept does not solve the problem existing in this area for ages, thus the results probably come forward after more years. The headway lies in the revaluation of all used assets, but it means a great hiatus. Currently there is no information, whether the revaluation will be obligatory for water management directorates or not. The final decision about this question is expected at the end of the first or the beginning of the second quarter of 2014. From our opinion furthermore necessary actions ought to be the differentiated specification of depreciation rate for public sector and the more flexible application of valuation methods in line with the nature of activities. The depreciation rate in accordance with the real useful life is consistent with the 17th number of IPSAS. In Hungary the Government Decree 249/2000. (XII.24.) allowed for institutions till 2014 to adjust the depreciation rates to the real useful life of assets, but after the reforms this possibility is not available anymore. According to the current regulation instead of the promotion of the practical realization of these prescriptions, solely those depreciation rates are applicable, which are involved in the Act LXXXI of 1996 on Corporate Tax and Dividend Tax.

The historical cost and carrying amount of the assets play an important role to assess appropriate the financial position and performance. After the public accounting reforms of 2014 the historical cost does not include the non-deductible value added tax. That is a discrepancy between the public accounting rules and the general accounting law. This modification eliminates the distortion thanks to the taxes, hereby contributes to disclose the proper amount of depreciation. The amortization will be made independently from the changes in taxation, thus data become comparable over a period of time. Further changes are that carrying amount shall be recognised suitably to the purchasing price, what is more narrow category than before. The appropriate amount of net assets requires the amendment of the rules concerning the residual value. According to the practice before 2014 all kind of assets depreciates fully, so their residual value at the end of useful life was zero. Due to the public accounting reforms the determination of residual value turned into essential in the cases of property, plant and equipment above cost of 25 million HUF (about 80.000 EUR), under that there is no possibility to determine the residual value. (Dömötörfy-Szamkó, 2013) Especially thanks to the high level of invested assets the changes facilitate the proper assessment of the financial position and performance. By the way in Hungary more time needs to meet the17th number of IPSAS requirement regarding the annual review of the residual value.

Within the assets the inventories are also very important for water management directorates, where the inventories appear almost solely in the form of materials and supplies to be consumed in the production process or in the rendering services. The inventories according to their nature are practically classified as follow:

- used for the general operation
- reserved for defensive purposes (stand-by materials and supplies)

These two categories also appear in the new public accounting separately. Consequently the consolidation has another unquestionable advantage beyond the previous. Information can be available on the national level about the stocks held for defensive purposes. This kind of inventories is analogous with the interchangeable inventories included in 12th number of IPSAS. For the completion of the tasks in connection with the flood control a certain amount of material and equipment is crucial. Actually these stocks are permanently engrossed current assets, what worsen the efficiency and effectiveness. This kind of inventories shows the following features: very slow turnover rate because of the conditioned consumption, the consumption implies the replacement obligations, low utilization rate, their impairment loss may run to high, significant demand on premises, their carrying costs are considerable, and the separated storage of them usually causes many problems. The carrying amount of the inventories is the historical cost less impairment loss adjusted by reversal of the impairment loss. Generally the stand-by inventories had been procured a long time ago and recognised in the statement as the historical cost of that time, what is now far away from their current market price or replacement cost. In the scope of these inventories a more accurate aspect is the recognition at the replacement cost in accordance with the 12th number of IPSAS. The present value calculation of the costs of flood and inland waters protection also requires the same method owing to the above mentioned features of the inventories and to the consistence with the ex-post funding system. Inventories bought and held for the ordinary course of activities have more favourable turnover rate. Thus the valuation method according to the corrected cost proves itself to be appropriate in this case, moreover it is the nearest approximation of the fair value. But there is such a specific type of inventory, what appears solely in the subsidiary ledger, and there is no information about their value. These are recognised as an expense at the date of purchase. This concept is harmonized with the IPSAS standards, because the activities of the water management directories are mostly service rendering, in which the consumed materials and supplies are accounted for expenses. But this category of inventory without value shall be amended. It involves such supplies, i.e. office furniture, which carry amounts are expected to be measured. The 12th number of IPSAS enables to apply different cost formula for inventories with a different nature or use. Hungary did the first step to this distinction through division the inventories into the two mentioned groups. The orientation towards the specifications of IPSAS is discoverable from other aspects as well: in contrast with the Hungarian law of accounting the advances given for inventories will be recognised in the future as accounts receivable rather than inventories.

Last but not least we would like to mention a few words about the aggravating circumstances, which hinder the application of changes in practice. These are mostly thanks to the unpreparedness of information system. The surfaced difficulties show that the changes procedure was rather too fast and came into force without the proper arrangements. The preparation of the information system should have started at least one year before the reforms of legal regulation. In the meantime the users would have taste the program, and by means of their opinion and experiences the failures could have been corrected. The concept is now the same, but the available time for that is extremely short: no more than one month was during closing the accounts. This situation rings the possibility of some mistakes in itself.

Conclusions

The Hungarian public sector requires reform. One element of this should be the improvement of accounting system. It must not to be done take no notice of the characteristics of Hungarian public sector and international tendencies. The development conception can be defined according to the resultant of these two factors. This conception should be feasible and it can reach the anticipated optimal effects for local governments and for other level of public sector.

Unfortunately in Hungary we should not polemize about what is the best accounting method for public sector the cash-based or the accrual based accounting system. Surely this problem is embedded in a wider problem group; it is the efficiency of public sector. Within the scope of this such problems are waiting for solution as the unambiguous defining of state tasks, the optimal distribution of tasks among the state levels, the rational determination of circle of tasks and jurisdictions connection with a state level, the constitutional reform of public administration, the reform of management's regulation and the complex improvement of financial system of local governments. The handling of these problems has vital importance.

According to the international experience it is impossible to set an objective of full adoption of accrual based accounting in Hungarian public sector, because now preconditions do not exist. But this does not mean that there is no opportunity to the development of public sector, the international experience certify that the most appropriate field for adoption of accrual based accounting is the local government system, surely it is possible to test the new different accounting methods "on a small scale", and there is more possibility to change methods in case of need, and moreover the accumulated experience are expansible later to other level of public sector, too.

The reform has started in the end of 2013. There are some changes in the public accounting system. These elements of reforms tend to the application of accrual based accounting. If we examine the actual situation of the Hungarian public sector's organizations we can verify that the process of accounting reform goes further very languidly. The actors of the public sector can not apply all new methods in the accounting system. They can fulfil all requirements which emerge from the side of the government. But the usage of the new settlement methods and other elements of accounting are very oppressive for the public sector. We are not optimistic that this reform could solve all problems in the accounting system. On the contrary we emphasize that hiatus will multiply in the area of Hungarian accounting system.

REFERENCES

Csermák Judit (2004): A költségvetési szervek gazdasági tevékenységének elemzése. Aula, Budapest.

Ernst & Young (2012): Overview and comparison of public accounting and auditing practices in the 27 EU Member States

Horváth M. Tamás (2002): Helyi közszolgáltatások szervezése. Dialog-Campus, Budapest.

International Public Sector Accounting Standards Board (2012): Handbook of International Public Sector Accounting Pronouncements

Kassó Zsuzsanna (2006): Miért van szükség az államháztartás pénzügyi beszámolórendszerének megváltoztatására? Vigvári András (szerk.): Decentralizáció, transzparencia, elszámoltathatóság. Magyar Közigazgatási Intézet, Budapest.

Kornai János - Eric Maskin - Gérard Roland (2004): Puha költségvetési korlát I. Közgazdasági Szemle 6., 608–624.

Sivák József – Vigvári András (2012): Rendhagyó bevezetés a közpénzügyek tanulmányozásába. CompLex Kiadó, Budapest.

Varga Imre (2009): *A valódiság elvének érvényesülése a magyar számviteli rendszerben. Ph.D. értekezés*. Nyugat-Magyarországi Egyetem, Gazdálkodás- és Szervezéstudományok Doktori Iskola.

Vigvári András (2005): Közpénzügyeink. KJK-Kerszöv, Budapest.

Dömötörfy Józsefné - Szamkó Józsefné (2013): Számviteli és gazdálkodási változások az államháztartás területén. Complex, Budapest